

ZOLTEK COMPANIES, INC.

**Moderator: Zsolt Rummy
August 12, 2005
10:00 a.m. CT**

Operator: Good day and welcome to Zoltek's third quarter 2005 earnings results conference call. As a reminder, today's call is being recorded. And now for introductions and opening remarks, I would like to turn the call over to Mr. Zsolt Rummy, President and Chief Executive Officer for Zoltek. Please go ahead, sir.

Zsolt Rummy: Good morning everybody. Welcome to our third quarter conference call. It will be slightly abbreviated as some of you may have noticed that we have not filed our Form 10-Q yet.

We seem to be victims of the downside of Sarbanes-Oxley and our auditors' quest to try to destroy the financial statements of the Company in order to protect themselves. In the process, we are having difficulty figuring out how to calculate our earnings per share on a fully diluted basis. For this reason we have had to delay our 10-Q filings while we were able to issue our earnings release since there is no question about the numbers in the balance sheet/earnings area.

So, with that introduction, I will turn it over to Kevin Schott to go through a very short financial report. He will be limited in answering any financial questions that are related to anything that would normally be released to the public in the 10-Q. So, if you have any questions that he will not be able to answer, we anticipate filing Form 10-Q on Monday, and after that you are welcome to call him and ask any of the questions that you wish. With that introduction, I turn it over to Kevin.

Kevin Schott: Thanks, Zsolt. Just a little more regarding the issue, we experienced a loss in our third quarter June 30, 2005. However, we did have a gain from our derivative calculation, which is

related to a convertible security. The question is whether we should back that gain out of your reported net loss to calculate fully diluted earnings per share and then include those shares as part of the denominator in the calculation. PricewaterhouseCoopers is debating that issue as we speak. They have been debating it for about four days now and still have not come back with an answer that everybody at Pricewaterhouse has agreed upon at this point in time.

So obviously, that is the only reason that our Form 10-Q is late. We were allowed to report our operating earnings and our net loss for this quarter and for the nine months period.

My report will have to be fairly brief. Our sales for the quarter ended June 30, 2005 were \$19.7 million compared to the quarter ended March 31, 2005 of \$15.8 million, which is a \$3.9 million increase quarter over quarter. \$2.0 million of that related to our technical fiber sales, about \$1.0 million of that related to our carbon fiber sales, and about another \$1.0 million related to our specialty product divisions in Hungary.

The \$2.0 million increase in our technical fiber sales is obviously related to our aircraft brake business, which Zsolt will expand upon later in his conversations. But we did have a significant increase this quarter over our March quarter in aircraft brake business sales.

Based on that, our operating income improved significantly from a loss of \$2.0 million in the March second quarter to a loss of \$1.2 million in the third quarter. Again, a lot of that was due to our increase in the aircraft brake business along with creating better operating efficiencies in Abilene.

That is about all I can say right now given the status of our 10-Q. As Zsolt said, as soon as we have published our 10-Q on Monday, I would be more than happy to answer any further questions. You are more than welcome to give me a call and we can discuss further topics that might arise once you review the 10-Q. Now back to Zsolt.

Zsolt Romy: I'm sorry that I have to cut him short, but I believe the rules apply that this conference call would be considered insider information until the 10-Q information is submitted to the public. I will try to cover some of the business status, which I think is indicated in our earnings release.

Obviously our shipments were up during the quarter. The biggest event for our volume at the moment is the Abilene start-up experience in the past month. We have demonstrated our ability to run at full capacity and I think it is a major step forward. We are trying to reach a significant increase in the total percent of capacity output and we are running at a fairly high percentage of what we think that we can produce this quarter. All five of our production lines in Abilene are running and the facility in Hungary is running full-tilt and has been for some time.

On the demand side, our demand for carbon fibers is continuing to grow. Wind energy is still the leading new application. Actually, it is getting bigger than we anticipated so far and we have to deal with how to produce even more than we had planned during the next fiscal year.

Demand for all other applications is similarly growing. Almost every day we get a new customer who is looking for carbon fiber. So while there are some indications and speculation that in 2007 the demand and capacity will be more balanced than it is now, in my opinion, this excessive demand is going to go far beyond 2007.

I think we are in for a fairly significant period of high growth in carbon fibers and the capacity is going to be trying to catch up both in the aerospace industry as well as in the commercial areas that we are concentrating on.

Switching to aircraft brakes, I think I mentioned in the last conference call that we had a significant event, so to speak, that relates to the aircraft brake business. Acordis, who was the only commercial supplier or merchant supplier of precursor to the aircraft brake business, went into receivership or bankruptcy and since that time there has been some maneuvering going on. Basically what it amounts to right now, is that they are either going to be shut down or sold in October. It is my opinion that they will be shutting down. I don't think anyone would be crazy

enough to acquire them given the situation in the acrylic textile business and given the disruption that now exists in the aircraft brake business.

Of course, this plays very well into our hands. For some time I have been trying to convince our customers and give them incentive to try our own precursor-based fibers for aircraft brakes and the two biggest ones in the industry have been at various stages of qualification when this bankruptcy happened. I think both of them are taking significant steps to qualify our fiber exclusively. And, I think the other two companies in the business are also going through qualification. I think we are in a very good position to capture virtually all of this business.

It gives us a lot of responsibility and everyone is concerned about similar situations happening in the future where we would run into financial difficulties, and therefore, disrupt the brake business again. We are making a lot of presentations and trying to convince the industry that we will not have this problem in the future since our business is purely carbon fibers. I think we are doing pretty well and this is a great opportunity for us.

Pyron demand has also grown again. There is growing automotive business and other flame-retardant applications for Pyron. While the mattress business has not developed like we hoped and anticipated, there are many other flame-retardant applications that are developing.

So I think demand is very high across the board. As we are increasing our carbon fiber production and hopefully get ahead of our customers' requirements, we are looking at increasing our sales efforts in the value-added products such as woven fabrics and pre-impregnated products. This should boost our revenues with the same carbon fiber production as well as boost our earnings and help us finally get to a profitable position.

The only other big thing is our expansion. As I mentioned earlier, we need to step up our expansion plan. The current projects are on target for startup completion in September and October. As you recall, we are expanding our precursor capacity, which we hope to start up first, probably in mid-September. In early October we plan to add two new Pyron lines. Then through

mid-October, we should start-up two brand new carbon fiber lines - all of this is going on in Hungary.

We are now looking at the next phase of the expansion and trying to determine exactly what sequence we are going to increase our capacity in both precursor and carbon fiber, meaning how much at a time and what our timing is for getting it completed so we can stay even with our customers' requirements. More about that to follow in future conference calls...

Unfortunately, I think because we have not been able to demonstrate the full effect of the Abilene facility, our profitability is not what I had expected and the stock price has not moved much. So to begin our next phase of our projects, we will again be looking for financing, but probably not a public offering. I think in the last conference call I may have said that we will not do more convertible financing again, but we may have to. I might have to eat my words and it has been a lesson to never say never. But in any event, we will be looking to finance the next expansion.

I think there are some customers that are very interested in also supporting part of our financing, so we will see what kind of package we can put together. We will be doing that during this quarter.

That brings me to the end of my comments. Kevin wants to say a few more words and then we will turn it over for questions.

Kevin Schott: In my haste to talk about why our Form 10-Q has not been filed, I forgot to read our legal disclaimer that we always have to do, so I just need to read this quickly and then we will open it up for questions.

This conference call contains forward-looking statements, which are based upon the current expectations of the Company. Because these forward-looking statements are inherently subject to risks and uncertainties, there are a number of factors that could cause the Company's plans, actions and actual results to differ materially. Among those factors are the Company's ability to:

re-activate its formerly idle manufacturing facilities on a timely and cost-effective basis; to meet current order levels for carbon fibers successfully; add new capacity for the production of carbon fiber and precursor raw material; execute plans to exit the specialty business and reduce costs; manage changes in customers' forecasted requirements for the Company's products; continue investing in applications and market development; manufacturing low-cost carbon fibers and profitably market them. Timing and occurrences of, or non-occurrence of, transactions and events that determine the future effects of these factors on the Company, as well as other factors, may be beyond the control of the Company. The Company undertakes no obligation to update any forward-looking statements to reflect events or circumstances after the date of this conference call.

Zsolt Rummy: At this point, I will open for questions from anyone.

Operator: Thank you. The question and answer session will be conducted electronically. If you would like to ask a question, please do so by pressing the star key followed by the digit one on your touch-tone telephone. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Once again, please press star one at this time to ask your question. And we will pause for just a moment.

We will take our first question from Steven Osborn with Fragramatics Manufacturing.

Steven Osborn: Good morning.

Zsolt Rummy: Good morning, Steve.

Steven Osborn: I noticed that we showed a \$1.2 million operating loss for the quarter. Was that primarily due to the start-up costs in Abilene? Or were there other types of variable costs, possibly, from a manufacturing standpoint that had anything to contribute to that adversely?

Zsolt Rummy: I think, in general, the Abilene start-up costs have two factors. One is just the cost of actually starting it up and putting line four and five into production during the quarter. In addition to that, the inefficiency of the running – basically we were incurring all of the costs of the plant while not getting the benefits of the revenue. So the good news is as our production rate comes up in Abilene, most of that revenue goes directly to the bottom line. The answer to your question is yes, primarily the start-up costs.

Steven Osborn: And that is primarily behind us now so we think we might possibly, on an operating basis, be in the black for the fourth quarter? Or should we wait or expect to be profitable on an operating basis in the first quarter of fiscal 2006?

Zsolt Rummy: We will try our extreme best. That is my objective to try to go to operating profitably this quarter.

Steven Osborn: OK. Thank you.

Operator: And next we will move on to Larry Wysong with HEMCO Corporation. I'm sorry, Mr. Wysong, please press star one at this time.

Larry Wysong: Question is what is the market price that you get per ton for Panex and Pyron? In a lot of your information you refer to the tonnage basis.

Zsolt Rummy: The good news is that we are referring in the tons-basis because that is how our major customers are buying and volume is that high. I'm not sure if I can give you an average price, but as I mentioned before, we used to have a goal of \$5.00 a pound as being the selling price to the largest customers. Given the inflation of energy and a lot of other things, that price is more like \$7.25. That is where we draw the bottom-line, and then based on volume, application and so on, the price goes upward from there. That is the general description of the Panex pricing.

On Pyron, the price per pound is somewhere in the \$4.00 range, give or take, again depending on the application and volume.

Larry Wysong: And one last question as it relates to the other gentleman's question, it sounds like you are at the point where your gross margins are going to begin to expand.

Zsolt Rummy: Right.

Larry Wysong: I have noticed quarter by quarter that your sales increases have basically equaled the increase in manufacturing overhead. What you are saying is that sales should begin to expand with manufacturing overhead staying more constant?

Zsolt Rummy: Yes.

Kevin Schott: That's correct.

Larry Wysong: All right. That's all I had.

Zsolt Rummy: OK. Thanks.

Operator: And as a reminder to ask your question, please press star followed by the digit one. And next we will move on to Dominic Golio, private investor.

Dominic Golio: I have several questions. The first is referencing back to your comments on the start-up costs. Why would these costs not be put on the balance sheet and amortized over time to match up with the revenues that are expected to be derived in the future? Why would they all be hitting the P&L right now?

Zsolt Rummy: I'll let Kevin answer that.

Kevin Schott: According to accounting rules, start-up costs can no longer be put onto the balance sheet and amortized over the life. They have to be recognized as period expenses. That is basically a new rule that came out a couple years ago.

Dominic Golio: OK. And then the other question I had was related to price. Given all of the demand and with the cost of energy going up and pre-supposing that we have many contracts with prices recited, have we protected ourselves for pass-throughs for energy-related cost escalations? And is there room in the contracts to perhaps modify our prices upwards to recognize that there is a high demand? I mean, look in the case of oil where demand is far exceeding the supply and it is ratcheting the price up. When do we get our payday is basically my question?

Zsolt Romy: Well, the quick answer to your question is actually to have an opportunity to raise prices in all of our contracts. I would just like to make a general comment that I have made before – one of the things that we are trying to watch is our entire strategy of the Company, which is to build a commercial carbon fiber business. We need to be somewhat careful of taking short-term benefits from the shortage and then killing the golden goose or some applications that are coming along that will give us the demand for the future. It is kind of a tightrope that we walk. But clearly, whenever an opportunity presents itself, we do get a higher price. And it is also our strategy to produce higher value-added products.

For instance, in our industry, to go from a pure fiber and resin combination to, let's say, a windmill blade, there are a number of steps in the process. In the past, some of the vendors providing the value-added services have exaggerated their prices, which then affected our ability to increase markets. What we are trying to do is move forward in the value chain and with relatively small amounts of additional input we can increase our profit margins significantly and still be promoting the competitiveness of the ultimate composite product. We are trying to expand our profitability in this way, which also brings us closer to the final user to make sure that the pricing of their product doesn't make their product prohibitive, therefore, eliminating the possibility of our carbon fiber volume increasing.

Dominic Golio: OK. Thank you.

Operator: And there are no further questions at this time. I'm sorry. We do have one that just came in.

We'll hear from Jon Gruber with Gruber McBaine Capital.

Zsolt Rummy: Hi, Jon.

Jon Gruber: Hi. I got on late. Now, why was the 10-Q not filed?

Kevin Schott: Jon, this is Kevin Schott. How are you doing? Our auditors are debating how to calculate fully diluted earnings per share when the Company has a loss but has an embedded gain from a convertible security in the income statement for that quarter. They are debating the appropriate treatment for that and have been debating it now for almost four days. We expect to have it filed no later than Monday.

Jon Gruber: Yes. OK...

Kevin Schott: So, that is why we were allowed to release earnings and have this conference call because it has no effect on anything other than calculating fully diluted earnings per share.

Jon Gruber: Yes, with that big sales gain from March to June, why do we still have an operating loss? It doesn't make sense since you said last time that things were improving in the latter part of the quarter.

Zsolt Rummy: Well, I think things are continuing to improve. And I think we answered that until the Abilene plant runs at a percentage of capacity that takes us into the black, we are incurring all of the costs of running a plant. In other words, when the lines are turned on, we are using electricity, we have the people, the depreciation – we have everything but the raw material. Once we start producing better than 60 percent of capacity, we start showing some profitability. And that's really the answer.

Jon Gruber: So, what kind of gross margin are you going to have this quarter? I mean, your gross margins...

Kevin Schott: Again, Jon – another thing I will also say is that a lot of the sales increase was in the aircraft brake business and not the carbon fiber business. And so those margins are a little smaller than what we make in carbon fiber but we didn't see as large a pickup in our carbon fiber sales as was expected based off the productivity coming out of Abilene right now.

Jon Gruber: And what have you seen in July and August?

Zsolt Rummy: We are improving.

Jon Gruber: OK. And what is the breakout for the aircraft brake and carbon fibers?

Kevin Schott: You will see that when it comes out in the 10-Q on Monday, Jon. I really can't comment on that because it's not published information.

Jon Gruber: And what is the gross margin on each of those and what is the goal on each of those?

Kevin Schott: You will see those when they are published in the 10-Q on Monday.

Jon Gruber: I doubt I will see them.

Zsolt Rummy: I can tell you our goal, which is something we stated many times.

Jon Gruber: I doubt I will see that in the 10-Q so why don't you answer my question?

Kevin Schott: After the 10-Q is published, I would be more than happy to answer that question for you. You are more than welcome to call me.

Zsolt Rummy: I think, again, that as far as our goal is concerned, we have stated many times we are looking at needing to have a 35% gross margin in our carbon fiber business in order to justify the capital investments and the rate of return. That is our goal and has been for some time.

Jon Gruber: When will we get there?

Zsolt Rummy: Again, I would say that when the Abilene plant is running somewhere around 85%+ capacity we will be there.

Jon Gruber: So that will be before the December quarter or...

Zsolt Rummy: Well, I'm hoping that we will demonstrate it this quarter, yes.

Jon Gruber: This quarter. Early, OK. And then the aircraft brake goals, gross margin?

Zsolt Rummy: Same kind of thing as it is also capital-intensive. It is lower priced because obviously in the conversion from Pyron to carbon you lose a high percentage of material. And the highest risk process is the oxidation. So, therefore, the price of Pyron products is a little more than half the Panex products, so we will lose 50% of the material in the processing, but again, the highest risk of the process is the oxidation. So, as far as gross margin, our expectation is essentially the same.

Kevin Schott: I will say, Jon, that you will see improvement in that technical fiber margin as we move on to using our precursor material product over the Acordis precursor material.

Jon Gruber: OK. But I thought you said the aircraft brake margins were lower than the carbon fiber margins in the...

Kevin Schott: They are rising – currently they are using the Acordis precursor.

Jon Gruber: OK. And when will you use yours?

Zsolt Romy: We are starting to use it now. I will say that on the long-term contract basis sometimes we are taking a hit on increased costs and sometimes we are doing better because the costs go down. We don't fluctuate the prices all the time when costs go up – we do an annual review. So, there are times where profitability is not as much as we want and sometimes a little more. On the average, we are looking over the period of time we need to have enough return that we can justify the investment and so on. And I think, as my comments were earlier, the aircraft guys are concerned about our financial viability, so it is important for them that we are a profitable business making a product for them. We are in pretty good shape to demonstrate reasonable profitability.

Jon Gruber: Last question, interest expense and financing fees and debt discount were huge. What's that going to be going forward?

Kevin Schott: Well, a lot of that falls on cash, Jon. The only piece that is cash is your interest costs.

Jon Gruber: Which is?

Kevin Schott: For this quarter it was right around \$1.0 million.

Jon Gruber: But that line item is going to be \$3.0 million going forward? Or what is that going to be? You have to make a lot of operating income to counteract that.

Kevin Schott: A lot of that is related to the derivative accounting, Jon. A lot of that is non-cash related. We are working on removing the derivative accounting from some of these agreements that we currently have. So there is potential going forward that the non-cash aspect of the derivative accounting will be removed. But we are working on that. The interest portion of that is about \$1.0 million.

Jon Gruber: And carbon fiber, what percent is wind power now?

Zsolt Romy: I don't know the exact percent but it's the largest single application.

Jon Gruber: So would it be 30% or would it be more or less than that?

Zsolt Romy: Probably a little more than that. I'd say maybe, at the moment, given our production, probably closer to 50%.

Jon Gruber: 50%, wow. OK. Thank you.

Zsolt Romy: Thanks, Jon.

Operator: And we do have a follow-up question from Dominic Golio, a private investor.

Dominic Golio: Yes. In the earlier comments, you mentioned that we would need future financing and you had previously mentioned the potential opportunity for an equity offering. Given the enormous cost of the latest round of financing and your words of not wanting to go that route again, with which I completely agree, would it not be better to try to stage these so that we may get some positive impact on the stock price with some operating income and then perhaps pursue an equity option to minimize the cost going forward on the Company's P&L in the form of interest?

Zsolt Romy: Dominic, you just defined my dilemma. It's been a dilemma because a couple of things play into this thing. Doing an offering now at the stock price as-is...

Dominic Golio: It's not cost efficient. I understand that.

Zsolt Romy: ...and also time consuming. So if they have enough premium over the current stock price including the warrants, the convertible debt actually is a reasonable transaction. We got into a

situation where this derivative accounting has kind of blind-sided us and I still don't think, personally, that is the way we should be accounting for it, but that is neither here or there. To make a long story short, we are certainly thinking about financing forward. Number one, we are going to make sure that kind of thing isn't going to happen to us, and number two, we will try to do it in such a way that it is staged to minimize our P&L impact. We are trying to do our best, but you pretty well defined the dilemma that we are going through in making that decision.

Dominic Golio: On a follow-up question on the derivative accounting, I assume that what is being referred to as the requirement is mark to market?

Kevin Schott: That is correct.

Dominic Golio: And then, the question I have is what remedies are there, how do you go about unwinding something like this or reworking the agreement to avoid this?

Kevin Schott: There are certain clauses within the debt agreement that if changed, the derivative accounting goes away, and we are currently working with the current debt holders to potentially reword some of the terms related to this. The terms that actually go into derivative accounting do not have a lot of impact on the deal. We are currently trying to work with the current investors to deal with that.

Dominic Golio: OK. One final suggestion in any refinancing or banking arrangements, I would strongly suggest that any covenants that we are required to meet specifically exclude the non-cash items including derivatives.

Kevin Schott: Right. As we currently speak, none of our debt that we have on the books has any financial covenants. But eventually going forward they might, but none of them currently do.

Dominic Golio: That is very important because that will turn around and bite you.

Kevin Schott: Obviously. I understand. So it is about generating cash.

Dominic Golio: OK. Thank you.

Operator: And we do have a question from Charles DiBenedetto with CCD Investing.

Charles DiBenedetto: Good to see that the demand for carbon fiber is increasing. Do you have the means to produce, to meet the future demand as it develops? It seems to be developing so many areas that I'm wondering if you can actually meet the demand as it develops.

Zsolt Rumy: That is our primary concern to have enough capacity to not discourage anyone from continuing developing products and applications. That is certainly of concern. And that is concern for financing and our expansion plan. We are still in position as a company to expand the fastest of anyone – we are able to add new capacity much faster than any competitor.

Charles DiBenedetto: But if you need additional lines in Abilene and Hungary, will you be able to add them?

Zsolt Rumy: Yes. Right now, we do not have any plans to add to Abilene. Much of our demand is coming from Europe and Asia. When we get the Hungarian facility expanded, we hope to take care of Europe and part of Asia, and then we can take care of the U.S. and the other part of Asia from Abilene.

Charles DiBenedetto: I see. Are you also restricted by price increases to the point where you will lose sales if you increase your prices too much?

Zsolt Rumy: Again, all pricing is obviously elastic, certainly for the long-term. Short-term, we could probably extract some money from some of the customers, but I think you build a long-term bad will if you do that too much. But in all our contracts we have the ability to renegotiate the pricing at maximum annually and sometimes more frequently.

Charles DiBenedetto: Good. Thank you.

Zsolt Rummy: Thank you, Charles.

Operator: And we'll take a follow-up question from Steven Osborn with Fragramatics Manufacturing.

Steven Osborn: Zsolt, everybody in the marketplace knows that we need millions of dollars. It's not a secret. We have known it for a long time. And certainly the people that invested \$20 million in that last convertible deal knew that you were going to need more money. Are we making any effort to contact somebody on Wall Street or some other avenue or new people to raise money? Or is anybody contacting us?

Zsolt Rummy: We have contacts almost daily. Our investors who have provided our recent funding are a group led by reasonable individuals, a reasonable company, and they have been quite supportive and they believe in what we are doing. In this financing method, there are a lot of bad people and a lot of decent people. And I think we are with some of the decent guys and we will hopefully, if we have to do a convertible financing again, be able to include other people as well into this investor group.

So, we have lots of other discussions and a lot of other people are quite interested. And we are talking to people about a potential public offering, eventually. When it comes down to making a decision, obviously a lot of people that would like to do financing and realize that we need money also want to take advantage of the situation. So you start filtering out who is really interested and who thinks that we are desperate. Those are the kind of choices we make every day.

Steven Osborn: It makes me feel good to know how much stock you have in the Company.

Zsolt Rummy: Yes. Well...

Steven Osborn: I don't have to second-guess your intentions or anything else.

Zsolt Rummy: Well, there was one shareholder, years ago, and the shareholder said to me, "Mr. Rummy, when I lose money on Zoltek it makes me feel good that you're losing a lot more than I do."

Steven Osborn: All right. That's good enough.

Zsolt Rummy: I'm really looking forward to all of us making a lot of money, and I think we will. I think our strategy has proven to be correct and we just have to get through this execution period and then I think we will be in a pretty good position.

Steven Osborn: Thank you.

Zsolt Rummy: Thank you.

Operator: And there are no further questions.

Zsolt Rummy: Thank you very much for participating, and I'm sorry that we could not do a full-fledged 10-Q discussion, but please call Kevin any time after our filing.

Operator: And that concludes today's conference call. Thank you for your participation.

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