PAUL MUELLER COMPANY

2004 Annual Report

Financial Highlights

Operating Results for the Year

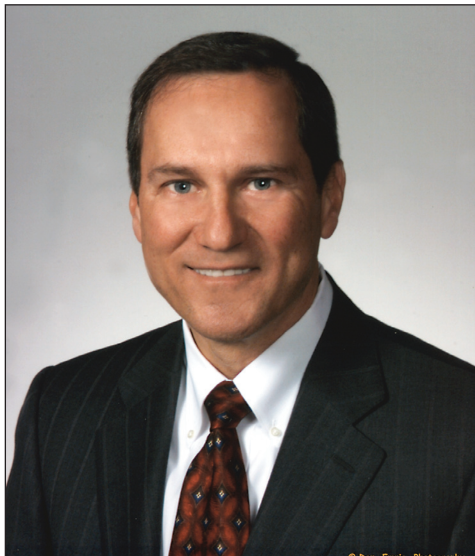
	2004	2003
Net Sales	$112,928,000	$116,766,000
Income (Loss) before Taxes	$ (6,364,000)	$ 2,683,000
Provision for Income Taxes	2,241,000	664,000
Net Income (Loss)	$ (8,605,000)	$ 2,019,000
Earnings (Loss) per Common Share:		
Basic	$ (7.36)	$ 1.73
Diluted	$ (7.36)	$ 1.71
Dividends Declared per Share	$ 2.40	$ 2.40

Year-End Position

	2004	2003
Total Assets	$ 57,083,000	$ 67,655,000
Working Capital	$ 5,826,000	$ 10,723,000
Current Ratio	1.19 : 1	1.34 : 1
Net Worth	$ 17,000,000	$ 29,247,000
Book Value per Share	$ 14.26	$ 24.50
Common Shares Outstanding	1,192,410	1,193,771
Backlog	$ 46,324,000	$ 38,612,000

Paul Mueller Company – Springfield, Missouri

Paul Mueller Company – Osceola, Iowa



DANIEL C. MANNA
President

Dear Shareholder,

Our results for 2004 were very disappointing, as we incurred a loss of $8,605,000 for the year. Lower sales and, in particular, lower operating margins contributed to the poor financial performance compared to the prior year. However, the majority of the reported loss related to a non-cash charge of $6,193,000 to write off all of our net deferred tax assets and also included an increase to the LIFO reserve of $1,680,000 on an after-tax basis.

Sales for 2004 were $112.9 million versus $116.8 million for 2003. The reduction in sales for the year was due to a combination of lower order entry and less beginning backlog. Order entry for 2004 was approximately $29 million short of forecast, with virtually all of the variance related to fewer orders for biotechnology and pharmaceutical equipment. The BioPharm industry experienced a slowdown in new facilities projects, which became apparent in mid-2003 and continued through 2004. Several large construction projects that would have provided the opportunity for large modular fabrication orders were also put on indefinite hold during this timeframe.

Our starting backlog for 2004 totaled $38.6 million, which was 29% lower than the backlog at the beginning of 2003. Again, the product line with the largest variance was BioPharm Systems with a starting backlog that was 37% less than at the beginning of 2003.

In addition to the reduced level of activity, profit margins were significantly lower than in 2003. The gross profit rate for 2004 was only 11.2% compared to 20.2% for the preceding year. The most significant factor affecting margins was a change in our mix of sales. BioPharm Systems, which historically has enjoyed higher margins than other products in our Industrial Equipment segment, comprised only 30% of our sales in 2004 compared to 44% in 2003. This was primarily due to an absence of large modular projects. During 2003, we fabricated and shipped the major portion of four large modular fabrication projects; but we were unable to maintain our backlog of module work, as very few follow-on projects became available for bid. Profitability was also adversely affected during 2004 by cost overruns on two very large and complex BioPharm orders.

Another major factor affecting margins in 2004 was the rapid escalation of stainless and carbon steel prices. Type 304 and 316 stainless steel, the materials we most commonly utilize, increased in price over the course of the year by 35% and 56%, respectively. The increase in carbon steel material was even more dramatic, nearly doubling for some items. For standard products, it was difficult to raise prices often enough to keep up with steel costs. For large, material-intensive orders in our Industrial Equipment segment, it was necessary to sell our products subject to surcharges in effect at time of delivery. This not only had the effect of reducing our margins, but no doubt also had a dampening effect on our ability to book new orders.

The significant escalation of stainless steel prices during 2004 resulted in a required addition to our LIFO reserve, which also lowered reported profitability. The increase in the LIFO reserve reduced our results on a before-tax basis by $2.7 million for 2004, compared to a reduction of $1.4 million to income before tax for 2003.

During 2004, a non-cash charge of $6.2 million was recorded to establish a valuation allowance for all of the Company's net deferred tax assets. The charge has been included in the tax provision on the accompanying Consolidated Statements of Income, and the effect was to increase the loss for the year by $6.2 million. The valuation allowance is required by generally accepted accounting principles, as we incurred a cumulative loss before tax of $0.8 million for the three-year period ended December 31, 2004. The cumulative three-year loss included LIFO provisions that reduced taxable income by $4.1 million. The significant increase in stainless steel prices during 2003 and 2004 was the primary reason for the LIFO provisions.

The loss for 2004 was solely attributable to the Industrial Equipment segment, as our other two major business segments operated profitably. The Industrial Equipment segment incurred a loss before tax of approximately $9 million on sales of $81.2 million for 2004, compared to income before tax of $1.3 million on $91.4 million in sales for 2003.

As previously mentioned, the performance for the BioPharm Systems product line significantly affected the Industrial Equipment segment. In addition, the other product lines within the Industrial Equipment segment faced a market that was very sluggish, as capital expenditures continued to be relatively flat for the markets that we serve. Market conditions contributed to a low rate of capacity utilization for the fabricated metal products industry during 2004, as it remained below historical levels. Low capacity utilization contributed to aggressive pricing for the projects that were available, which put added pressure on profit margins. Additionally, competition for industrial equipment projects was particularly keen during 2004 due to the absence of a sufficient level of work. Reverse auctions, internet bidding, and multiple bids for virtually every project characterized the 2004 marketplace.

While profitability declined in our Industrial Equipment segment, we achieved increases in profitability in our Dairy Farm Equipment and Field Fabrication segments.

Dairy Farm Equipment segment income before tax increased from $0.4 million for 2003 to $1.8 million for 2004. The improved profitability was a direct result of a 44% increase in sales from 2003 to 2004. Sales were higher primarily due to improved domestic market conditions, as the average milk price for the year exceeded the prior year by 35%, milk production was higher, and feed costs were favorable. Additionally, sales improved due to an OEM agreement signed during 2004, as well as a large order for milk cooling systems received from Mexico.

The Field Fabrication segment generated income before tax of $128,000 for 2004 compared to a loss before tax of $225,000 for 2003. Profitability improved, as sales were $10 million during 2004 compared to $8.3 million for the prior year. Order entry increased significantly for the Field Fabrication segment during 2004 and was $14.9 million higher than 2003. The timing of order entry was such that a substantial portion of work was not completed by year-end, providing a more favorable backlog of $10.5 million going into 2005.

In spite of our poor financial performance during 2004, we did have some important accomplishments during the year. After an extensive period of negotiation, we were successful in concluding a five-year OEM manufacturing agreement that provides for the exclusive supply of milk cooling systems to a competitor for their North American market. Subsequent to concluding this agreement, our new customer terminated their existing manufacturing operation in Mexico. This was of strategic importance, as in our view the rapidly consolidating dairy farm equipment market in North America could not reasonably support four manufacturers of milk cooling equipment.

We were also successful in booking a complete design/build project for a food plant now being built in Guymon, Oklahoma. Our responsibilities include design development, fabrication and purchasing of equipment, building erection, field installation of all equipment, and commissioning of the completed facility. The project, which is for a large Japanese company, will provide valuable experience as we expand our focus on supplying complete systems rather than just components for a project.

Looking forward to 2005, our starting backlog was $46.3 million compared to a backlog of $38.6 million at the beginning of 2004. By segment, our starting backlog this year was $32.4 million for the Industrial Equipment segment, $3.4 million for the Dairy Farm Equipment segment, and $10.5 million for the Field Fabrication segment. At the beginning of 2004, comparable backlogs were $36.2 million, $1.1 million, and $1.3 million, respectively. The improvement in the backlog is consistent with those segments that operated profitably during 2004.

We are optimistic that the performance during 2005 for the Dairy Farm Equipment segment will further improve compared to 2004. Domestically, production is expected to increase further as demand for dairy products remains good. It appears feed prices will remain reasonable and milk prices, although expected to be somewhat less than 2004, should be better than the average milk price for the last five years. Additionally, exports of dry milk powder are projected to be strong during 2005 due to the weak U.S. dollar.

Our level of activity in the Dairy Farm Equipment segment will also be favorably influenced by our new OEM manufacturing agreement as we enter the first full year of this arrangement. This will help to ensure better utilization of our Osceola, Iowa, manufacturing facility and to stabilize the level of our workforce.

Internationally, the market for Dairy Farm Equipment is expected to continue to be favorable in Ireland, Mexico, and Japan. For Ireland, positive factors include the strength of the Euro, the removal of retaliatory duties on U.S. products, and the European Union's grant program to assist farmers in upgrading their equipment. Also, the outlook for the markets in Japan and Mexico continue to be very encouraging with respect to Dairy Farm Equipment. The strength of the Euro against the U.S. dollar also provides for further opportunities in Continental Europe for additional Dairy Farm Equipment business.

In order to increase our sales and market share in the growing market for our products in South America, we have recently concluded a manufacturing agreement with a Chilean company. Under the terms of this agreement, they will manufacture milk coolers and certain other Mueller products under license and deliver them to our newly established LLC named Mueller Latin America, Limitada, for resale to our dealers. This approach was necessitated by import duties and high freight costs which make it uneconomical to serve the South American market with products manufactured in the United States.

Most forecasts indicate that economic growth will increase again in the United States during 2005 and that industrial capital expenditures will also grow at a favorable rate. The fundamentals for capital expenditures are generally positive, with both output and capacity utilization increasing. Corporate profitability and cash flow are favorable, and major projects that have been delayed for the past few years should become available for bid. We expect this to have a positive effect on both the Industrial Equipment and the Field Fabrication segments of our business.

In the Industrial Equipment segment, we expect very few large modular or bioreactor projects to become available during the year. However, a large order for pharmaceutical modules that was placed on indefinite hold in mid-2003 was reinstated during the latter part of 2004 and will be completed during the first half of 2005. This will help keep our activity level in BioPharm Systems high for the first half of the year. Overall, we are projecting an increase in order entry of approximately 20% for BioPharm Systems, with the bulk of this increase attributable to our standard line of multiple-effect stills and pure-steam generators. This increased level of order entry should be achievable, as we observe the market for these products to be somewhat more favorable this year.

Also, we operated through part of 2004 without a regional sales person on either the east or west coasts. We now have two experienced regional sales people to cover those territories and are optimistic that our level of new orders will improve as a result.

The outlook for our Heat Transfer Products is also favorable. We now have a new Business Unit Manager with a strong background in sales and marketing in charge of that product line. His focus to date has been on reorganizing the marketing group for more effective sales coverage and increasing the sales and marketing training for our staff. Our Heat Transfer Products sales staff also recently completed training our key manufacturer's rep organizations in the field. Initial indication is that these efforts are proving effective, and we expect to exceed order entry projections for the first quarter.

Another factor in our outlook for Heat Transfer Products is the broadening of our product line to include tube-and-shell heat exchangers. We are being very selective in selling these products for applications in which we also bring added value to our customers in terms of application knowledge that will enable them to operate more efficiently. So far, we have completed two tube-and-shell projects with good results. Our backlog of outstanding quotations is already significant, and we expect it will result in a considerable amount of new business for 2005.

The market for Processing Equipment products remains very competitive, as the tank fabrication industry continues to operate below historical capacity-utilization levels. We do not expect market conditions to improve significantly during 2005, and we expect continued competition from lower capability, but also lower-cost providers. In response, our strategy has been to continually expand upon our scope of services to include design and fabrication of modular assemblies, installation, repair, and field fabrication. We also have the capability to selectively offer complete turnkey, design-build services. Our order entry for the Processing Equipment product line is budgeted at approximately the same level as it was for 2004; but we have the opportunity to perform much better if we are successful in obtaining orders for several large projects expected to become available for bid.

In the Field Fabrication segment, we foresee a higher level of activity and improved performance for 2005. We began the year with a considerably larger backlog, and we are in the process of quoting some large projects for which a major portion of the work could be completed during 2005. If we are successful in obtaining these projects, this will also substantially help our Industrial Equipment segment, as a significant number of components will be fabricated in the factory and shipped to the field for final fabrication and installation.

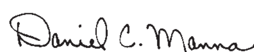
An area of continued concern is the price of stainless steel. The mills have been assessing surcharges due to the volatility in the price of nickel, chrome, and molybdenum, the key alloying elements used in the production of stainless steel. Although we do not anticipate the rapid rate of price increases to continue in 2005, there is little indication to suggest prices are expected to decline. This will no doubt have a dampening effect on the number of new business opportunities and will continue to put pressure on our margins as customers resist price increases necessitated by the higher cost for steel.

During April 2004, we were successful in signing a new three-year labor contract with the Sheet Metal Workers International Association – Local 208. We believe we have an excellent workforce and our relationship with our plant employees is one of trust and mutual respect. We take great pride in the skill and work ethic of our employees and view them as a competitive advantage in an otherwise very competitive marketplace.

In early January 2005, we filed a Form 15 with the Securities and Exchange Commission to deregister our common stock and suspend our reporting obligations under the Securities Exchange Act of 1934. The action was taken principally to avoid incurring inordinately high costs for complying with the ongoing requirements of the Sarbanes-Oxley Act of 2002. The compliance provisions of the Sarbanes Oxley Act would have resulted in significant out-of-pocket costs for items such as additional audit and consulting services and legal expenses. Even more importantly, they would have consumed extensive amounts of time for several key executives and managers. The decision to deregister and delist our stock will avoid significant cash expenditures and better enable management to focus on the task of successfully operating the business. Despite the deregistration and suspension of reporting obligations, we intend to maintain good corporate governance practices and will continue to make financial information available to our shareholders and the financial community. Our stock is currently traded on the pink sheets in the over-the-counter market.

In summary, we reported poor financial results in 2004, although the reported loss was amplified considerably by a non-cash charge of $6.2 million to write off all of our net deferred tax assets. Despite the reported result, we finished the year with a balance sheet reflecting virtually no long-term debt and a favorable cash position.

Financially, we are off to a much better start this year. Our beginning backlog is larger and of a higher quality than in 2004. Our market outlook is generally more favorable, and we have added new products which provide additional business opportunities. Also, we have recently concluded two important manufacturing agreements, which we believe will benefit us in the coming year. Furthermore, we have made important changes in key management and sales positions to improve upon our internal performance. As a result, we expect significantly improved financial performance for 2005.



Daniel C. Manna
President

March 2005

Corporate Profile

Paul Mueller Company, headquartered in Springfield, Missouri, was incorporated in 1946. For over half a century, we have been building a reputation as a manufacturer of high-quality stainless steel tanks and industrial processing equipment that make the customer's process smoother, faster, and more reliable. Our philosophy is simple: we are committed to meeting and exceeding our customer's expectations of value by providing quality equipment and excellent service.

Paul Mueller Company has grown to occupy about 950,000 square feet of manufacturing space in two manufacturing facilities located in Springfield, Missouri, and Osceola, Iowa. Mueller products are used in over 100 countries worldwide on dairy farms and in a wide variety of industrial applications, including food, dairy, and beverage processing; pharmaceutical, biotechnological, and chemical processing; water distillation; heat transfer; HVAC; heat recovery; process cooling; and thermal-energy storage.

Field fabrication, erection, and installation services are provided by Mueller Field Operations, Inc., a wholly owned subsidiary. Transportation of the Companies' products and backhauls of material and components are handled by another wholly owned subsidiary, Mueller Transportation, Inc. Mueller Montaña de México, S.A. de C.V., a 50%-owned joint venture, provides a presence for industrial equipment in the Mexican market.

Consolidated Statements of Income
For the Years Ended December 31, 2004, 2003, and 2002

	2004	2003	2002
Net Sales	$ 112,928,442	$ 116,766,018	$ 114,149,434
Cost of Sales	100,261,804	93,177,115	91,432,774
Gross profit	$ 12,666,638	$ 23,588,903	$ 22,716,660
Selling, General and Administrative Expenses	19,341,330	21,370,524	20,278,938
Operating income (loss)	$ (6,674,692)	$ 2,218,379	$ 2,437,722
Other Income (Expense):			
Interest income	$ 88,105	$ 78,148	$ 89,269
Interest expense	(34,760)	(82,700)	(25,955)
Other, net	341,167	459,770	350,186
	$ 394,512	$ 455,218	$ 413,500
Income (loss) before provision for income taxes and equity in income (loss) of joint venture	$ (6,280,180)	$ 2,673,597	$ 2,851,222
Provision for Income Taxes	2,241,000	664,000	967,000
Income (Loss) before Equity in Income (Loss) of Joint Venture	$ (8,521,180)	$ 2,009,597	$ 1,884,222
Equity in Income (Loss) of Joint Venture	(83,703)	8,956	4,936
Net Income (Loss)	$ (8,604,883)	$ 2,018,553	$ 1,889,158
Earnings (Loss) per Common Share:			
Basic	$ (7.36)	$ 1.73	$ 1.62
Diluted	$ (7.36)	$ 1.71	$ 1.61

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

Consolidated Balance Sheets December 31, 2004 and 2003

	2004	2003
Assets		
Current Assets:		
Cash and cash equivalents	$ 4,005,042	$ 2,887,471
Accounts receivable, less reserve for doubtful accounts of $713,545 for 2004 and $951,981 for 2003	19,478,131	17,129,082
Income taxes receivable	1,166,487	–
Costs and estimated earnings in excess of billings	281,109	2,176,135
Inventories: Raw materials and components	$ 5,897,232	$ 8,981,914
Work-in-process	2,847,559	6,034,912
Finished goods	1,488,219	2,282,026
	$ 10,233,010	$ 17,298,852
Prepayments	947,764	3,034,483
Total Current Assets	$ 36,111,543	$ 42,526,023
Property, Plant, and Equipment (at cost):		
Land and land improvements	$ 3,754,462	$ 3,719,255
Buildings	14,804,717	14,700,713
Fabrication equipment	40,051,867	39,484,000
Transportation, office, and other equipment	13,101,058	13,070,556
Construction-in-progress	367,187	121,618
	$ 72,079,291	$ 71,096,142
Less: Accumulated depreciation	53,158,023	50,042,119
	$ 18,921,268	$ 21,054,023
Other Assets	2,049,816	2,321,991
Deferred Taxes	–	1,752,823
	$ 57,082,627	$ 67,654,860
Liabilities and Shareholders' Investment		
Current Liabilities:		
Current maturities of long-term debt	$ 362,750	$ 567,000
Accounts payable	6,719,074	4,280,315
Accrued expenses – Income taxes	599,889	903,884
Payroll and benefits	3,567,725	6,964,260
Vacations	2,879,021	2,896,588
Other	1,210,593	1,553,196
Advance billings	7,798,779	14,176,469
Billings in excess of costs and estimated earnings	7,147,696	460,970
Total Current Liabilities	$ 30,285,527	$ 31,802,682
Long-Term Pension Liabilities	9,067,851	5,612,474
Other Long-Term Liabilities	728,876	992,208
Contingencies		
Shareholders' Investment:		
Common stock, par value $1 per share – Authorized 20,000,000 shares – Issued 1,370,475 shares for 2004 and 1,369,475 shares for 2003	$ 1,370,475	$ 1,369,475
Preferred stock, par value $1 per share – Authorized 1,000,000 shares – No shares issued	–	–
Paid-in surplus	5,182,090	5,154,090
Retained earnings	19,551,395	31,019,095
	$ 26,103,960	$ 37,542,660
Less: Treasury stock, 178,065 shares for 2004 and 175,704 shares for 2003, at cost	2,675,846	2,593,447
Deferred compensation	361,066	479,992
Accumulated other comprehensive loss	6,066,675	5,221,725
	$ 17,000,373	$ 29,247,496
	$ 57,082,627	$ 67,654,860

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

Consolidated Statements of Shareholders' Investment For the Years Ended December 31, 2004, 2003, and 2002

	Common Stock	Paid-in Surplus	Retained Earnings	Treasury Stock	Deferred Compen-sation	Accumulated Other Com-prehensive Loss	Total
Balance – 12-31-2001	$ 1,354,325	$ 4,661,932	$32,812,385	$(2,561,987)	$ (234,538)	$ (68,793)	$35,963,324
Add (Deduct):							
Net income	–	–	1,889,158	–	–	–	1,889,158
Other comprehensive loss, net of tax:							
Foreign currency translation adjustment	–	–	–	–	–	(67,718)	(67,718)
Change in minimum pension liability	–	–	–	–	–	(6,010,502)	(6,010,502)
Comprehensive (loss)	–	–	–	–	–	–	$(4,189,062)
Dividends, $2.40 per common share	–	–	(2,841,171)	–	–	–	(2,841,171)
Restricted stock issued	6,450	199,134	–	–	(205,584)	–	–
Restricted stock forfeiture	–	(2,776)	–	(31,460)	22,235	–	(12,001)
Amortization	–	–	–	–	95,658	–	95,658
Balance – 12-31-2002	$ 1,360,775	$ 4,858,290	$31,860,372	$(2,593,447)	$ (322,229)	$(6,147,013)	$29,016,748
Add (Deduct):							
Net income	–	–	2,018,553	–	–	–	2,018,553
Other comprehensive income, net of tax:							
Foreign currency translation adjustment	–	–	–	–	–	(37,506)	(37,506)
Change in minimum pension liability	–	–	–	–	–	962,794	962,794
Comprehensive income	–	–	–	–	–	–	$ 2,943,841
Dividends, $2.40 per common share	–	–	(2,859,830)	–	–	–	(2,859,830)
Restricted stock issued	8,700	295,800	–	–	(304,500)	–	–
Amortization	–	–	–	–	146,737	–	146,737
Balance – 12-31-2003	$ 1,369,475	$ 5,154,090	$31,019,095	$(2,593,447)	$ (479,992)	$(5,221,725)	$29,247,496
Add (Deduct):							
Net (loss)	–	–	(8,604,883)	–	–	–	(8,604,883)
Other comprehensive loss, net of tax:							
Foreign currency translation adjustment	–	–	–	–	–	8,656	8,656
Change in minimum pension liability	–	–	–	–	–	(853,606)	(853,606)
Comprehensive (loss)	–	–	–	–	–	–	$(9,449,833)
Dividends, $2.40 per common share	–	–	(2,862,817)	–	–	–	(2,862,817)
Restricted stock issued	1,000	28,000	–	–	(29,000)	–	–
Treasury stock acquisition	–	–	–	(82,399)	–	–	(82,399)
Amortization	–	–	–	–	147,926	–	147,926
Balance – 12-31-2004	$ 1,370,475	$ 5,182,090	$19,551,395	$(2,675,846)	$ (361,066)	$(6,066,675)	$17,000,373

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

Consolidated Statements of Cash Flows
For the Years Ended December 31, 2004, 2003, and 2002

	2004	2003	2002
Cash Flows from Operating Activities:			
Net income (loss)	$ (8,604,883)	$ 2,018,553	$ 1,889,158
Adjustments to reconcile net income (loss) to net cash provided by operating activities:			
Equity in loss (income) of joint venture	83,703	(8,956)	(4,936)
Bad debt (recovery) expense	(163,540)	246,026	469,181
Depreciation and amortization	3,548,876	4,037,461	3,429,006
Loss (gain) on sales of equipment	12,145	(18,514)	5,260
Valuation allowance – deferred tax assets	6,192,969	–	–
Changes in assets and liabilities –			
(Increase) decrease in accounts and notes receivable	(3,351,996)	5,602,123	(6,144,218)
Decrease (increase) in costs in excess of estimated earnings and billings	1,895,026	818,797	(2,994,932)
Decrease (increase) in inventories	7,065,842	(4,969,609)	(2,765,321)
(Increase) in prepayments	(198,529)	(351,864)	(515,252)
(Increase) decrease in other assets	(14,139)	(181,079)	2,461,043
(Increase) decrease in deferred taxes	(1,146,227)	(220,891)	1,530,476
Increase (decrease) in accounts payable	2,438,759	(2,761,321)	2,616,983
(Decrease) increase in accrued expenses	(5,065,195)	3,404,484	954,871
(Decrease) increase in advance billings	(6,377,690)	6,475,469	2,126,958
Increase in billings in excess of costs and estimated earnings	6,686,726	435,970	25,000
Increase (decrease) in other long-term liabilities	2,758,280	(2,149,280)	(2,038,379)
Net Cash Provided by Operating Activities	$ 5,760,127	$12,377,369	$ 1,044,898
Cash Flows (Requirements) from Investing Activities:			
Proceeds from maturities of investments	$ –	$ –	$ 1,000,000
Purchases of investments	–	–	(1,000,000)
Proceeds from sales of equipment	–	42,350	1,607
Additions to property, plant, and equipment	(1,280,340)	(2,774,369)	(4,754,029)
Treasury stock acquisition	(82,399)	–	–
Net Cash (Required) by Investing Activities	$ (1,362,739)	$ (2,732,019)	$ (4,752,422)
Cash Flow (Requirements) Provisions from Financing Activities:			
Short-term bank (repayment) borrowing	$ –	$ (4,183,155)	$ 4,183,155
Long-term debt proceeds	–	–	1,251,000
Repayment of long-term debt	(417,000)	(417,000)	(104,250)
Dividends paid	(2,862,817)	(2,859,830)	(2,841,171)
Net Cash (Required) Provided by Financing Activities	$ (3,279,817)	$ (7,459,985)	$ 2,488,734
Net Increase (Decrease) in Cash and Cash Equivalents	$ 1,117,571	$ 2,185,365	$ (1,218,790)
Cash and Cash Equivalents at Beginning of Year	2,887,471	702,106	1,920,896
Cash and Cash Equivalents at End of Year	$ 4,005,042	$ 2,887,471	$ 702,106

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

Notes to Consolidated Financial Statements
December 31, 2004, 2003, and 2002

(1) Summary of Accounting Policies:

Principles of Consolidation and Lines of Business – The financial statements include the accounts of Paul Mueller Company ("Company") and its wholly owned subsidiaries: Mueller Transportation, Inc., and Mueller Field Operations, Inc. ("Companies"). The Company specializes in the manufacture of high-quality stainless steel tanks and industrial processing equipment and serves the food, dairy, beverage, chemical, pharmaceutical, biotechnological, and other process industries, and the dairy farm market.

Use of Estimates – The preparation of financial statements, in conformity with generally accepted accounting principles, requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates.

Joint Venture – The Company has 50% interest in Mueller Montaña de México, S.A. de C.V. ("Mueller Montaña"), a Mexican fabricator of industrial equipment. The investment is accounted for under the equity method and is included in other assets on the Consolidated Balance Sheets.

Revenue Recognition and Retainages – Revenue from sales of fabricated products is recognized upon passage of title to the customer. Passage of title may occur at the time of shipment from the Company's dock, at the time of delivery to the customer's location, or when projects are completed in the field and accepted by the customer. For large multi-unit projects that are fabricated in the plant, revenue is recognized under the units-of-delivery method, which is a modification of the percentage-of-completion method of accounting for contracts. The units-of-delivery method recognizes as revenue the contract price of units completed and shipped or delivered to the customer (as determined by the contract) or completed and accepted by the customer for field-fabrication projects. The applicable manufacturing cost of each unit is identified and charged to cost of sales as revenue is recognized.

Revenues from long-term contracts that involve only a few deliverables and that meet the requirements of Statement of Position 81-1 – "Accounting for Performance of Construction-Type and Certain Production-Type Contracts" are recognized under the percentage-of-completion method of accounting. For plant-fabricated projects, percentage of completion is determined by comparing total manufacturing hours incurred to date for each project to estimated total manufacturing hours for each project. For field-fabricated projects, percentage of completion is determined by comparing costs incurred to date for each contract to the estimated total costs for each contract at completion. Estimates of total manufacturing hours and total contract costs for relevant contracts are reviewed continually and, if necessary, updated to properly state the estimates. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined. Costs and estimated earnings in excess of billings on uncompleted contracts arise when costs have been incurred and revenues have been recorded, but the amounts are not yet billable under the terms of the contracts. Such amounts are recoverable from customers upon various measures of performance, including achievement of certain milestones, completion of specified units, or completion of the contract. Billings in excess of costs and estimated earnings on uncompleted contracts arise as a result of advance and progress billings on contracts. Costs and estimated earnings on uncompleted contracts and related amounts billed as of

December 31, 2004 and 2003, were as follows:

	2004	2003
Costs incurred on uncompleted contracts	$ 19,084,672	$ 36,845,408
Estimated earnings	7,201,086	12,562,790
	$ 26,285,758	$ 49,408,198
Less: Billings to date	33,152,345	47,693,033
	$ (6,866,587)	$ 1,715,165

Amounts included in the accompanying Consolidated Balance Sheets at December 31, 2004 and 2003, under the following captions were:

	2004	2003
Costs and estimated earnings in excess of billings on uncompleted contracts	$ 281,109	$ 2,176,135
Billings in excess of costs and estimated earnings on uncompleted contracts	(7,147,696)	(460,970)
	$ (6,866,587)	$ 1,715,165

Costs and estimated earnings in excess of billings and billings in excess of costs and estimated earnings relate to contracts in progress and are included in the accompanying Consolidated Balance Sheets as current assets and current liabilities, respectively, as they will be liquidated in the normal course of contract completion, although completion may require more than one year.

Contracts with some customers provide for a portion of the sales amount to be retained by the customer for a period of time after completion of the contract. Retainages included in accounts receivable were $558,000 at December 31, 2004, and $336,000 at December 31, 2003.

Inventories – The Company's inventories are recorded at the lower of cost on a last-in, first-out ("LIFO") basis or market. Cost of subsidiary inventories is determined on a first-in, first-out ("FIFO") method; and they are not significant to the Consolidated Financial Statements. Cost includes material, labor, and manufacturing burden required in the production of products.

Under the FIFO method of accounting, which approximates current cost, Company inventories would have been $9,964,900, $7,298,400, and $5,912,800 higher than those reported at December 31, 2004, 2003, and 2002, respectively.

A reduction in inventory quantities during 2004 resulted in liquidation of LIFO quantities recorded at lower costs prevailing in prior years as compared with the cost of 2004 purchases. The effect was to decrease cost of sales, which decreased the net loss by $75,200, or $0.06 per share.

Research and Development – Research and development expenses are charged to expense as incurred and were $842,900 during 2004, $1,024,800 during 2003, and $1,103,800 during 2002.

Depreciation Policies – The Companies provide for depreciation expense using principally the double-declining-balance method for new items and the straight-line method for used items. The economic useful lives for the more significant items within each property classification are as follows:

	Years
Buildings	40
Land improvements	10 – 20
Fabrication equipment	5 – 10
Transportation, office, and other equipment	3 – 10

Maintenance and repairs are charged to expense as incurred. The cost and accumulated depreciation of assets retired are removed from the accounts, and any resulting gains or losses are reflected in net income currently.

Impairment of Plant and Equipment – If facts and circumstances indicate that the carrying value of identifiable plant and equipment may be impaired, the Company would perform an evaluation of recoverability. If an evaluation was required, the Company would compare the estimated future undiscounted cash flows associated with the asset to the asset's carrying amount to determine if a write-down is required.

Earnings per Common Share – The following table sets forth the computation of basic and diluted earnings per common share:

	2004	2003	2002
Net income (loss)	$ (8,604,883)	$ 2,018,553	$ 1,889,158
Shares for basic earnings per common share – Weighted-average shares outstanding	1,169,925	1,168,021	1,168,021
Dilutive effect of restricted stock and stock options	–	12,130	5,395
Shares for diluted earnings per common share – Adjusted weighted-average shares outstanding	1,169,925	1,180,151	1,173,416
Earnings (loss) per common share:			
Basic	$(7.36)	$ 1.73	$ 1.62
Diluted	$(7.36)	$ 1.71	$ 1.61

Stock-Based Compensation – As of December 31, 2004, the Company had two stock-based compensation plans for employees and non-employee directors, which are described more fully in Note (8). The Company accounts for those plans under the recognition and measurement principles of Accounting Principles Board ("APB") Opinion No. 25 – "Accounting for Stock Issued to Employees" and related interpretations. No stock-based compensation cost has been reflected in net income (loss), as all options granted under those plans had an exercise price equal to or greater than the market value of the underlying common stock on the date of the grants. The following table illustrates the effect on net income (loss) and earnings (loss) per share if the Company had applied the fair value recognition provisions of Statement of Financial Accounting Standards ("SFAS") No. 123 – "Accounting for Stock-Based Compensation" to stock-based employee and non-employee director compensation.

	Year Ended December 31		
	2004	2003	2002
Net income (loss), as reported	$ (8,604,883)	$ 2,018,553	$ 1,889,158
Less: Stock-based compensation expense determined under fair-value-based method for all awards, net of related tax	59,217	66,455	51,127
Pro forma net income (loss)	$ (8,664,100)	$ 1,952,098	$ 1,838,031
Earnings (loss) per common share:			
Basic – as reported	$(7.36)	$ 1.73	$ 1.62
Basic – pro forma	$(7.41)	$ 1.67	$ 1.57
Diluted – as reported	$(7.36)	$ 1.71	$ 1.61
Diluted – pro forma	$(7.41)	$ 1.65	$ 1.57

Comprehensive Income – The components of comprehensive income (loss) for the years ended December 31, 2004, 2003, and 2002, were as follows:

	2004	2003	2002
Foreign currency translation adjustment	$ 4,480	$ (59,533)	$ (107,490)
Tax (benefit)	(4,176)	(22,027)	(39,772)
Foreign currency translation adjustment, net of tax	$ 8,656	$ (37,506)	$ (67,718)
Change in minimum pension liability	$ (853,606)	$ 1,528,244	$ (9,540,479)
Tax provision (benefit)	–	565,450	(3,529,977)
Change in minimum pension liability, net of tax	$ (853,606)	$ 962,794	$ (6,010,502)
Other comprehensive income (loss)	$ (844,950)	$ 925,288	$ (6,078,220)

Statements of Cash Flows – For purposes of the Consolidated Statements of Cash Flows, the Company considers investments with a maturity of three months or less to be cash equivalents.

Interest and income tax payments for each of the three years during the period ended December 31, 2004, were as follows:

	2004	2003	2002
Interest payments	$ 34,400	$ 80,000	$ 24,900
Income tax payments	$ 161,000	$ 1,868,000	$ 52,400

Shareholders' Investment – The following table sets forth the analysis of common stock issued and held as treasury stock:

	Shares	
	Common Stock Issued	Treasury Stock
Balance, December 31, 2001	1,354,325	174,604
Restricted stock issued	6,450	–
Restricted stock forfeiture	–	1,100
Balance, December 31, 2002	1,360,775	175,704
Restricted stock issued	8,700	–
Balance, December 31, 2003	1,369,475	175,704
Restricted stock issued	1,000	–
Treasury stock acquisition	–	2,361
Balance, December 31, 2004	1,370,475	178,065

(2) Retirement Plans:

The Company has a Profit Sharing and Retirement Savings Plan [401(k) plan] in which substantially all employees are eligible to participate. The plan provides for a match of employees' contributions up to a specified limit. The plan also has a profit-sharing feature whereby an additional match is made if net income reaches predetermined levels established annually by the Board of Directors. The assets of the plan are deposited with a trustee and are invested at the employee's option in one or more investment funds. Total Company contributions to the plan were $370,000 for 2004, $382,000 for 2003, and $395,000 for 2002.

The Company has pension plans covering substantially all employees. Benefits under the plans are based either on final average pay or a flat benefit formula.

Total pension expense under the plans was $2,874,600 for 2004, $2,337,900 for 2003, and $1,278,000 for 2002. Management's policy is to fund pension contributions that are currently deductible for tax purposes. A contribution of $1,400,200 will be made during 2005, and the amount has been included in accrued expenses on the accompanying Consolidated Balance Sheets. The Company uses a December 31 measurement date for its plans.

The following table sets forth the required disclosures for the pension plans at December 31:

	2004	2003
Change in Benefit Obligation –		
Benefit obligation at beginning of year	$ 53,470,700	$ 47,218,400
Service cost	1,896,200	1,564,600
Interest cost	3,276,600	3,123,500
Actuarial loss	2,912,500	3,323,500
Benefits paid and expenses	(1,915,700)	(1,759,300)
Benefit obligation at end of year	$ 59,640,300	$ 53,470,700
Change in Plan Assets –		
Fair value of plan assets at beginning of year	$ 38,349,900	$ 32,517,700
Actual return on plan assets	4,236,800	6,676,100
Employer contribution	2,981,000	915,400
Benefits paid and expenses	(1,915,700)	(1,759,300)
Fair value of plan assets at end of year	$ 43,652,000	$ 38,349,900
Reconciliation –		
Funded status	$ (15,988,300)	$ (15,120,800)
Unrecognized net actuarial loss	14,445,000	13,256,700
Unrecognized prior service cost	672,800	887,100
Minimum liability adjustment	(9,597,500)	(8,951,000)
(Accrued) benefit cost	$ (10,468,000)	$ (9,928,000)

Amounts recognized in the Consolidated Balance Sheets at December 31 were as follows:

	2004	2003
Balance Sheet Reconciliation –		
(Accrued) benefit cost	$ (10,468,000)	$ (9,928,000)
Minimum pension liability	(9,597,500)	(8,951,000)
Intangible asset	622,300	829,400
Accumulated other comprehensive loss (pretax)	8,975,200	8,121,600
(Accrued) benefit cost	$ (10,468,000)	$ (9,928,000)

Components of pension expense for the three years were:

	2004	2003	2002
Service cost	$ 1,896,200	$ 1,564,600	$ 1,335,100
Interest cost	3,276,600	3,123,500	2,923,300
Expected return on plan assets	(3,226,800)	(2,943,200)	(3,199,100)
Amortization of prior service cost	214,300	217,000	218,700
Recognized net actuarial loss	714,300	376,000	–
Pension expense	$ 2,874,600	$ 2,337,900	$ 1,278,000

Accumulated benefit obligations of the pension plans exceeded plan assets at December 31 as follows:

	2004	2003
Projected benefit obligations	$ 59,640,300	$ 53,470,700
Accumulated benefit obligations	$ 53,995,300	$ 48,171,800
Fair value of plan assets	$ 43,652,000	$ 38,349,900

The increase (decrease) in minimum liability, net of tax, included in other comprehensive income/loss for each year was as follows:

	2004	2003
Increase (decrease)	$ 853,600	$ (962,800)

Weighted-average assumptions used to determine benefit obligations at December 31 were as follows:

	2004	2003
Discount rate	5.75%	6.00%
Rate of compensation increase	3.00%	4.25%

Weighted-average assumptions used to determine net periodic pension expense for the years ended December 31 were as follows:

	2004	2003	2002
Discount rate	6.00%	6.50%	7.00%
Expected long-term return on plan assets	8.50%	8.00%	8.50%
Rate of compensation increase	4.25%	4.25%	4.25%

Pension expense is calculated based upon a number of actuarial assumptions established on January 1 of the applicable year, detailed in the table above, including the weighted-average discount rate, rate of increase in future compensation levels for the applicable plan, and the expected long-term rate of return on plan assets. The discount rate used by the Company for valuing pension liabilities is based on review of high quality corporate bond yields with maturities approximating the remaining life of the projected benefit obligations. The discount rate used to determine pension expense was reduced from 6.5% for 2003 to 6.0% for 2004. The effect of the rate reduction was to increase pension expense by $436,000 for 2004. In developing the expected long-term rate of return assumption for plan assets (which consist mainly of U.S. equity and fixed income securities), input was considered from the actuaries and the investment advisors. The rate is intended to reflect the average rate of earnings expected to be earned on the funds invested or to be invested to provide plan benefits. In determining the rate, appropriate consideration was given to historical performance of the major asset classes held or anticipated to be held by the plans and the forecast for future rates of return for those asset classes. The long-term rate of return assumption was increased from 8.0% for 2003 to 8.5% for 2004. This had the effect of decreasing pension expense for 2004 by $190,000.

The weighted-average asset allocations of the pension benefit plans at December 31 were as follows:

	2004	2003
Asset Category:		
Fixed income	30%	32%
Equities	67%	66%
Other	3%	2%
	100%	100%

The long-term asset allocation on average will approximate 60% in equities, with 40% in fixed income securities. The objective, on a long-term basis, is to achieve an excess return over the actuarial assumption

for the expected long-term rate of return on plan assets. The investment strategy employed is a long-term risk control approach using diversified investment options with no exposure to volatile investment options, such as financial futures, derivatives, etc. The plans use a diversified allocation of equity and fixed income securities that is customized to each plan's cash flow benefit needs.

Pension benefits expected to be paid over the next ten years are as follows:

2005	$ 1,911,300
2006	2,024,800
2007	2,153,600
2008	2,481,600
2009	2,765,700
2010 through 2014	18,558,600
	$ 29,895,600

(3) Income Taxes:

The provision for taxes on income (loss) from operations included:

	2004	2003	2002
Current tax expense (benefit)	$ (1,880,200)	$ 1,415,600	$ 1,132,300
Deferred, net	(2,071,800)	(751,600)	(165,300)
Valuation allowance	6,193,000	–	–
	$ 2,241,000	$ 664,000	$ 967,000

During 2004, the Company determined that a valuation allowance was necessary. A non-cash charge of $6,193,000 was recorded during 2004 to establish a valuation allowance for all of the Company's net deferred tax assets. The charge was included in the tax provision in the accompanying Consolidated Statements of Income for the year. A consolidated cumulative loss before tax was incurred for the three-year period ended December 31, 2004. A cumulative three-year loss is sufficient objective evidence to preclude the assertion that the ultimate realization of the net deferred tax assets is more likely than not; and a full valuation allowance was required under the provisions of Statement of Financial Accounting Standards (SFAS) No. 109 – "Accounting for Income Taxes."

Deferred tax assets and liabilities arise from differences between financial reporting and tax reporting of assets and liabilities that most often result from differences in the timing of income and expense recognition. As previously mentioned, the Company has incurred a cumulative loss before taxes for the past three years ended December 31, 2004; and a full valuation allowance is required for all net deferred tax assets. The valuation allowance will be increased or decreased based on future changes in the Company's net deferred tax assets. The detail of the deferred tax assets and liabilities as of December 31, 2004 and 2003, is shown below.

	2004	2003
Deferred Tax Assets:		
Insurance	$ 166,700	$ 187,200
Vacation	1,007,300	951,700
Warranty	197,400	322,600
Doubtful accounts	273,000	342,200
Pensions	3,715,100	2,940,400
Healthcare benefits	232,200	288,800
Inventory	329,200	427,800
Other	302,200	383,100
Net operating loss and tax credit carryforwards	1,860,500	–
	$ 8,083,600	$ 5,843,800

	2004	2003
Deferred Tax Liabilities:		
Depreciation	1,890,600	1,722,600
Net	$ 6,193,000	$ 4,121,200
Valuation allowance	6,193,000	–
	$ –	$ 4,121,200

At December 31, 2004, the Company had a net operating loss and tax credit carryforwards. The tax benefit of the net operating loss carryforward is $210,600 and may be carried forward twenty years. AMT credit carryforwards total $124,300 and may be carried forward indefinitely. State credit carryforwards total $121,300 and have varying expiration dates of from five to twenty years. General business credits total $1,404,300 and may be carried forward twenty years. The years of expiration and related amounts are as follows:

Year	Amount
2021	$ 244,500
2022	$ 218,800
2023	$ 526,400
2024	$ 414,600

A valuation allowance totaling $6,193,000 was established to offset net current deferred tax assets of $3,847,700 and net non-current deferred tax assets of $2,345,300 as of December 31, 2004.

Current deferred tax assets were $2,368,400 at December 31, 2003, and are included in prepayments on the accompanying Consolidated Balance Sheets.

A reconciliation between the expected income tax expense at the statutory federal income tax rate (34%) and the reported income tax expense for each of the three years during the period ended December 31, 2004, follows:

	2004	2003	2002
Statutory federal income tax expense (benefit)	$ (2,135,400)	$ 909,000	$ 969,400
Increase (decrease) in taxes resulting from:			
Tax credits	(1,167,700)	(332,200)	(63,500)
State tax, net of federal benefit	(632,900)	88,100	50,800
Other, net	(16,000)	(900)	10,300
Valuation allowance	6,193,000	–	–
	$ 2,241,000	$ 664,000	$ 967,000

(4) Bank Borrowings:

The Company has a $3,000,000 bank borrowing facility that expires on May 31, 2005, which management intends to renew. Borrowings under the facility incur interest at the LIBOR Daily Floating Rate plus 1.75%. At December 31, 2004, there were no outstanding borrowings under the facility. In addition, the Company has a long-term note payable outstanding as of December 31, 2004, in the principal amount of $312,750. The note is repayable in quarterly installments of $104,250, with the final payment due August 2, 2005, and with a variable interest rate of the LIBOR Daily Floating Rate plus 1.75%. The interest rate for the note was 4.17% as of December 31, 2004. The note is secured by equipment with a cost of $1,563,000. The Company was in compliance with all note covenants at December 31, 2004.

(5) Guarantees:

The Company also has a $7,000,000 standby letter-of-credit facility; and as of December 31, 2004, there were standby letters of credit totaling $4,988,008 issued under the facility and all will expire within one year.

The Company's provisions for warranty expense have historically been a relatively consistent percentage of sales. Warranty claims tend to occur shortly after product delivery, as a significant portion of the Company's sales are custom-fabricated products built to customer specifications. Warranty claims are reviewed monthly and reserves are adjusted to properly reflect the remaining estimated cost to complete the repair or replacement.

The following is a reconciliation of changes in the warranty reserve for the years ended December 31, 2004 and 2003:

	2004	2003
Beginning balance	$ 1,326,838	$ 894,523
Costs incurred to satisfy warranty claims	(1,349,654)	(1,324,091)
Aggregate warranty reserves made	639,387	1,409,533
Aggregate changes to warranty reserves	285,300	346,873
Ending balance	$ 901,871	$ 1,326,838

(6) Contingencies:

A lawsuit was filed in May 2002 against the Company alleging breach of contract/breach of express warranty in connection with the sale of a heat exchanger in October 2000. The plaintiff alleged in the suit that it had suffered direct, consequential, and incidental damages in excess of $3,100,000. On March 5, 2004, the parties reached an out-of-court settlement of the lawsuit. Under the settlement, the plaintiff received $600,000. The Company paid $300,000 of the settlement, and the balance was covered by the Company's product liability carrier. The Company's liability of $300,000 was reflected in the results for 2003. The effect on 2003 results was to reduce net income by $189,000, or $0.16 per share on a diluted basis.

The Company and its subsidiaries are involved in other legal proceedings incident to the conduct of their business. It is management's opinion that none of these matters will have a material adverse effect on the consolidated financial position, results of operations, or cash flows.

The Company has operating leases with total aggregate future minimum payments of $753,000 and terms exceeding one year. It is expected that leases will be renewed or replaced as they expire. The future minimum payments for each of the years subsequent to December 31, 2004, will be:

Year	Amount
2005	$ 270,600
2006	$ 241,600
2007	$ 149,300
2008	$ 68,500
2009	$ 23,000

(7) Segment Data:

The Company has four reportable segments: Industrial Equipment, Dairy Farm Equipment, Field Fabrication, and Transportation. The Industrial Equipment segment includes sales of the following products directly to industrial customers: food, beverage, chemical, and industrial processing equipment; industrial heat transfer equipment; biopharmaceutical equipment; pure-water equipment; thermal-energy storage equipment; and commercial refrigeration equipment. Dairy Farm Equipment segment sales are made to independent dealers for resale and include milk-cooling and storage equipment and accessories, refrigeration units, and heat-recovery equipment for use on dairy farms. The Field Fabrication segment includes sales of very large, field-fabricated tanks and vessels that cannot be built and shipped from the plant. Typical projects are large stainless steel storage tanks for sanitary and industrial process applications. The Transportation segment delivers products to customers and backhauls materials and components. The segment also transports components for the Field Fabrication segment and performs contract carriage for third parties.

Management evaluates performance and allocates resources based on income or loss before income taxes. The accounting policies of the reportable segments are the same as those described in Summary of Accounting Policies in Note 1 to these Consolidated Financial Statements.

Reportable segments are managed separately because they offer different products and serve different markets. Industrial Equipment products have been aggregated because they are designed and built to a customer's specifications and they use common processes and resources in the Springfield, Missouri, manufacturing facility. Similar economic conditions affect the long-term financial performance of the product lines included in the Industrial Equipment segment. The Dairy Farm Equipment segment includes standard products that are built to stock in the Osceola, Iowa, manufacturing facility and are available for sale from inventory. The demand for Dairy Farm Equipment products is affected by the economic factors that influence the profitability of dairy farmers. The Field Fabrication segment uses different skills and fabrication methods and requires different technology and expertise than other segments. The Transportation segment is a trucking operation.

Net sales include revenues from sales to unaffiliated and affiliated customers before elimination of intersegment sales. Intersegment eliminations are primarily sales from the Industrial Equipment segment and Transportation segment to the Field Fabrication segment.

The Other/Corporate classification includes other revenues, unallocated corporate assets and expenses, and corporate other income (expense).

	2004						
	Dairy Farm Equipment	Industrial Equipment	Field Fabrication	Transportation	Other / Corporate	Intersegment Eliminations	Consolidated
Net sales	$20,548,996	$81,154,456	$ 9,975,683	$ 3,154,814	$ 1,045,293	$ (2,950,800)	$112,928,442
Depreciation & amortization expense	$ 266,847	$ 2,194,000	$ 536,526	$ 170,520	$ 380,983	$ –	$ 3,548,876
Income (loss) before income tax	$ 1,881,911	$ (8,968,734)	$ 128,273	$ 31,500	$ 646,870	$ –	$ (6,280,180)
Assets	$ 8,316,704	$34,269,880	$ 3,191,340	$ 2,511,756	$ 8,792,947	$ –	$ 57,082,627
Additions to property, plant & equipment	$ 231,314	$ 1,012,697	$ 18,402	$ 15,151	$ 2,776	$ –	$ 1,280,340

	2003						
	Dairy Farm Equipment	Industrial Equipment	Field Fabrication	Transportation	Other / Corporate	Intersegment Eliminations	Consolidated
Net sales	$14,306,860	$91,379,067	$ 8,299,941	$ 3,918,474	$ 594,564	$ (1,732,888)	$116,766,018
Depreciation & amortization expense	$ 298,145	$ 2,373,233	$ 754,283	$ 152,232	$ 459,568	$ –	$ 4,037,461
Income (loss) before income tax	$ 435,469	$ 1,347,191	$ (225,163)	$ 454,419	$ 661,681	$ –	$ 2,673,597
Assets	$ 7,610,101	$42,742,818	$ 3,569,769	$ 2,639,220	$11,092,952	$ –	$ 67,654,860
Additions to property, plant & equipment	$ 9,599	$ 2,038,914	$ 89,670	$ 289,340	$ 346,846	$ –	$ 2,774,369

	2002						
	Dairy Farm Equipment	Industrial Equipment	Field Fabrication	Transpor-tation	Other / Corporate	Intersegment Eliminations	Consolidated
Net sales	$20,274,303	$78,239,085	$14,939,379	$ 3,361,503	$ 542,604	$ (3,207,440)	$114,149,434
Depreciation & amortization expense	$ 338,975	$ 2,176,361	$ 444,413	$ 174,462	$ 294,795	$ –	$ 3,429,006
Income (loss) before income tax	$ 3,570,314	$ (2,737,321)	$ 1,181,802	$ 115,743	$ 720,684	$ –	$ 2,851,222
Assets	$ 8,973,496	$41,561,377	$ 6,031,589	$ 2,581,625	$ 9,182,669	$ –	$ 68,330,756
Additions to property, plant & equipment	$ 123,292	$ 1,897,760	$ 2,089,362	$ 70,096	$ 573,519	$ –	$ 4,754,029

Revenues from external customers by product category for the three years ended December 31, 2004, were:

	2004	2003	2002
Milk-cooling and storage equipment	$ 18,915,382	$ 12,950,878	$ 17,964,266
Process vessels and tanks	47,830,835	45,314,532	52,760,254
Other industrial equipment	46,182,225	58,500,608	43,424,914
	$112,928,442	$116,766,018	$114,149,434

Revenues from external customers by geographic location are attributed to countries based on the location of the customer and for the three years ended December 31, 2004, were:

	2004	2003	2002
United States	$ 93,593,998	$103,650,529	$100,736,612
North America (excluding the U.S.)	9,913,248	7,183,100	7,713,539
Asia and the Far East	4,180,296	3,378,499	4,018,883
Europe	3,993,742	1,474,634	924,600
Other areas	1,247,158	1,079,256	755,800
	$112,928,442	$116,766,018	$114,149,434

During the years presented, export sales to any one country were not in excess of 10% of consolidated sales.

All long-lived assets owned by the Company and its subsidiaries are located in the United States.

During 2004, sales to any one customer were not in excess of 10% of consolidated sales. During 2003 and 2002, sales to an individual U.S. customer exceeded 10% of consolidated sales. The sales amounted to $13,045,000 for Industrial Equipment in 2003 and $12,388,000 for Field Fabrication in 2002.

(8) Long-Term Incentive Plans:

The Company has two stock compensation plans: the 1999 Long-Term Incentive Plan (the "Employee Plan") and the Non-Employee Director Stock Option and Restricted Stock Plan (the "Director Plan").

The Employee Plan provides for two types of awards for executives and key employees: restricted stock and non-qualified stock options. An aggregate of 180,000 shares of common stock can be issued under

the Employee Plan, with 55,000 shares being the aggregate maximum number of shares that may be granted as restricted stock.

Under the Director Plan, non-employee directors can receive restricted stock and non-qualified stock options. An aggregate of 60,000 shares can be issued under the Director Plan in either restricted stock or non-qualified options.

The exercise price of each option under both Plans must equal or exceed the closing market price of the Company's common stock on the day before the effective date of grant. The options vest and are exercisable five years after the date of grant, and they must be exercised no later than ten years from the date of grant.

Under the Plans, restricted shares of stock vest five years after the effective date of grant. Compensation expense was computed by multiplying the number of shares granted by the fair market value of the common stock on the date of grant. The expense is being recognized ratably over the vesting period. Compensation expense recognized for the restricted shares was $147,926, $146,737, and $95,658 for the years ended December 31, 2004, 2003, and 2002, respectively. Under the Plans, 1,000 shares of restricted stock were granted during 2004 at the fair market value of $29.00 per share. At December 31, 2004, 21,450 shares of restricted stock were outstanding under the Plans.

A summary of activity in the Company's stock option plans is as follows:

	Number of Shares	Weighted Average Exercise Price
Outstanding at December 31, 2001..........	39,800	$ 36.00
Granted..	21,800	35.35
Forfeited..	(3,400)	36.00
Outstanding at December 31, 2002..........	58,200	$ 35.76
Granted..	23,300	35.00
Outstanding at December 31, 2003..........	81,500	$ 35.54
Granted..	2,800	29.13
Outstanding at December 31, 2004..........	84,300	$ 35.33

The following table summarizes information about stock options outstanding as of December 31, 2004:

	Options Outstanding		
Range of Exercise Prices	Number of Shares	Weighted Average Remaining Contractual Years	Average Exercise Price
$29.13 – $36.00	84,300	6.85	$ 35.33

Options for 18,200 shares outstanding as of December 31, 2004, were exercisable at $36.00 per share.

The Company applies APB No. 25 – "Accounting for Stock Issued to Employees" to account for employee stock options. Accordingly, no compensation expense has been recognized for non-qualified stock options.

Pro forma net income and earnings-per-share information (as required by SFAS No. 123 – "Accounting for Stock-Based Compensation") has been determined as if the Company had accounted for all stock options under the fair-value method described by SFAS No. 123.

The fair values for options were estimated at the date of grant using the Black-Scholes Option Pricing Model, with the following weighted-average assumptions:

	Stock Option Grants					
	October 1, 2004	May 16, 2003	July 25, 2002	May 20, 2002	March 1, 2001	May 13, 1999
Interest rate	3.70%	3.40%	4.80%	4.80%	4.90%	5.80%
Expected life in years	7.5	7.5	7.5	7.5	7.5	7.5
Expected volatility	27.40%	30.20%	36.10%	38.80%	64.20%	53.40%
Expected dividend yield	8.24%	8.17%	8.00%	7.50%	9.00%	7.40%
Value per option	$ 2.88	$ 4.94	$ 5.05	$ 6.35	$ 8.58	$ 8.60

The Black-Scholes Option Pricing Model was developed for use in estimating the fair value of traded options that have no vesting restrictions and that are fully transferable. In addition, option pricing models require the input of subjective assumptions, including the expected stock price volatility. Because the Company's options have characteristics different from those of traded options, the model, in the opinion of management, does not necessarily provide a reliable single measure of the fair value of its options.

For purposes of pro forma disclosures, the estimated fair value of the options is being amortized to expense ratably over the vesting period. The pro forma disclosures required by SFAS No. 123 are not likely to be representative of the effects on reported net income or losses for future years. The pro forma information follows:

	2004	2003	2002
Pro forma net income (loss)	$ (8,664,100)	$ 1,952,098	$ 1,838,031
Pro forma earnings (loss) per common share:			
Basic	$(7.41)	$ 1.67	$ 1.57
Diluted	$(7.41)	$ 1.65	$ 1.57

(9) Shareholder Rights Plan:

On January 26, 2001, the Board of Directors of the Company adopted an Amended and Restated Rights Agreement ("Rights Agreement") and declared a dividend distribution of one Common Share Purchase Right ("Right") for each share of the Company's common stock outstanding on February 15, 2001.

The Rights will be exercisable only if a person or group acquires 15% or more of the Company's common stock (an "Acquiring Person") or announces a tender offer that would result in ownership of 15% or more of the Company's common stock. Initially, each Right will entitle shareholders to buy one share of the Company's common stock at an exercise price of $117.25.

If the Company is acquired in a merger or other business combination and its common stock is changed or exchanged, or if 50% or more of its consolidated assets or earning power is sold, each Right will entitle its holder to purchase, at the Right's then-current exercise price, shares of the acquiring company's common stock having a market value of twice the exercise price. Also, if an Acquiring Person acquires 15% or more of the Company's outstanding common stock, each Right will entitle its holder to purchase, at the Right's then-current exercise price, common stock of the Company having a market value of twice the exercise price. Under either situation, Rights owned by an Acquiring Person will become null and void.

Prior to acquisition by an Acquiring Person of 15% or more of the Company's common stock, the Rights are redeemable at the option of the independent members (as defined in the Rights Agreement) of the Board of Directors at $0.01 per Right. The Rights will expire on January 29, 2011.

Until a Right is exercised, the holder thereof, as such, has no rights as a shareholder of the Company, including the right to vote or to receive dividends. The issuance of the Rights alone has no dilutive effect and does not affect reported earnings per share.

Independent Auditors' Report

To the Board of Directors of Paul Mueller Company:

We have audited the accompanying consolidated balance sheets of PAUL MUELLER COMPANY (a Missouri corporation) AND SUBSIDIARIES as of December 31, 2004 and 2003, and the related consolidated statements of income, shareholders' investment, and cash flows for each of the years in the three-year period ended December 31, 2004. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Paul Mueller Company and Subsidiaries as of December 31, 2004 and 2003, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2004, in conformity with accounting principles generally accepted in the United States of America.

KPMG LLP

Kansas City, Missouri,
February 11, 2005

Selected Financial Data – Five-Year Summary and Market and Dividend Information by Quarter For the Years 2004 and 2003

Selected Financial Data – Five-Year Summary

	2004	2003	2002	2001	2000
Net sales	$ 112,928,442	$ 116,766,018	$ 114,149,434	$ 94,288,219	$ 105,182,134
Net income (loss)	$ (8,604,883)	$ 2,018,553	$ 1,889,158	$ (1,359,840)	$ 3,847,397
Earnings (loss) per common share:					
Basic	$(7.36)	$ 1.73	$ 1.62	$(1.16)	$ 3.29
Diluted	$(7.36)	$ 1.71	$ 1.61	$(1.16)	$ 3.29
Common shares outstanding	1,192,410	1,193,771	1,185,071	1,179,721	1,173,721
Dividends declared per common share	$ 2.40	$ 2.40	$ 2.40	$ 2.40	$ 2.40
Total assets	$ 57,082,627	$ 67,654,860	$ 68,330,756	$ 55,910,473	$ 55,687,051
Long-term obligation, net of current maturities	$ 728,876	$ 992,208	$ 1,604,566	$ 947,189	$ 162,366
Shareholders' investment	$ 17,000,373	$ 29,247,496	$ 29,016,748	$ 35,963,324	$ 40,112,056
Working capital	$ 5,826,016	$ 10,723,341	$ 13,304,896	$ 13,910,555	$ 18,201,712
Book value per common share	$ 14.26	$ 24.50	$ 24.49	$ 30.48	$ 34.18
Average number of employees	843	1,007	968	876	870

Market and Dividend Information by Quarter

	2004 Quarter Ended				2003 Quarter Ended			
	Mar. 31	June 30	Sept. 30	Dec. 31	Mar. 31	June 30	Sept. 30	Dec. 31
Market Price of Stock								
High	$ 41.79	$ 41.58	$ 31.70	$ 31.23	$ 34.50	$ 41.50	$ 45.00	$ 42.50
Low	$ 40.00	$ 31.00	$ 26.83	$ 29.00	$ 29.45	$ 30.97	$ 39.25	$ 39.01
Cash Dividends								
Declared per share	$ 0.60	$ 0.60	$ 0.60	$ 0.60	$ 0.60	$ 0.60	$ 0.60	$ 0.60

The market price data was obtained from The Nasdaq Stock Market.

Financial Highlights by Quarter (Unaudited)
For the Years 2004 and 2003

(In Thousands, Except Per Share Data)

	Quarter Ended							
	March 31		June 30		September 30		December 31	
	2004	2003	2004	2003	2004 (b)	2003	2004 (a)	2003 (c)(d)
Net sales	$ 18,311	$ 27,579	$ 25,390	$ 29,961	$ 33,948	$ 29,720	$ 35,279	$ 29,506
Gross profit	$ 1,465	$ 5,974	$ 2,171	$ 6,569	$ 3,813	$ 7,026	$ 5,218	$ 4,020
Net income (loss)	$ (2,371)	$ 718	$ (1,725)	$ 984	$ (5,324)	$ 1,017	$ 815	$ (700)
Earnings (loss) per common share:								
Basic	$ (2.03)	$ 0.61	$ (1.48)	$ 0.84	$ (4.55)	$ 0.87	$ 0.70	$ (0.60)
Diluted	$ (2.03)	$ 0.61	$ (1.48)	$ 0.83	$ (4.55)	$ 0.86	$ 0.69	$ (0.60)

(a) Fourth quarter 2004 results were unfavorably affected by an adjustment to the LIFO reserve, which decreased net income by $192,000, or $0.16 per share on a diluted basis.

(b) A non-cash charge of $5,047,000 was recorded during the third quarter of 2004 to establish a valuation allowance for all of the Company's net deferred tax assets. As of September 30, 2004, the Company was in a cumulative loss-before-tax position for the prior three years; and this was sufficient objective evidence to preclude the assertion that the ultimate realization of the net deferred tax assets is more likely than not, and a full valuation allowance is required under the provisions of Statement of Financial Accounting Standards No. 109 – "Accounting for Income Taxes."

(c) Results for the three months ended December 31, 2003, were adversely affected by the settlement of a lawsuit on March 5, 2004. Under the settlement, the Company was responsible for a payment of $300,000, which has been reflected in the results for the fourth quarter of 2003. The effect on the 2003 fourth quarter results was to increase the net loss by $189,000, or $0.16 per share.

(d) Fourth quarter 2003 results were unfavorably affected by an adjustment to the LIFO reserve, which increased the net loss by $253,000, or $0.22 per share.

PAUL MUELLER COMPANY

DIRECTORS

WILLIAM L. FUERST
Dean and Henry D. Price Professor of
Business – University of Kansas

DONALD E. GOLIK
Senior Vice President and CFO

** **W. CURTIS GRAFF**
President –
W. J. Graff & Assoc.

* **DANIEL C. MANNA**
President

DAVID T. MOORE
Chief Information Officer

*** **WILLIAM R. PATTERSON**
Chairman of the Board
Member –
Stonecreek Management L.L.C.

*** **MELVIN J. VOLMERT**
Managing Partner –
Ardent Capital L.L.C.

* Executive Committee Member
** Audit Committee Member
*** Executive & Audit Committee Member

CHAIRMAN EMERITUS

PAUL MUELLER

EXECUTIVE OFFICERS

DANIEL C. MANNA
President

DONALD E. GOLIK
Senior Vice President, CFO
and Secretary

WHOLLY OWNED SUBSIDIARIES

MUELLER TRANSPORTATION, INC.

DIRECTORS

DANIEL C. MANNA – Chairman
DONALD E. GOLIK
AARON L. OWEN

OFFICERS

DANIEL C. MANNA – President
DONALD E. GOLIK – Secretary
GERALD S. MILLER – Treasurer
RONALD W. GIELOW – Controller

MUELLER FIELD OPERATIONS, INC.

DIRECTORS

DANIEL C. MANNA – Chairman
MATTHEW T. DETELICH
DONALD E. GOLIK

OFFICERS

MATTHEW T. DETELICH – President
DONALD E. GOLIK – Secretary
GERALD S. MILLER – Treasurer
RONALD W. GIELOW – Controller

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