UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(mark one)
[X] Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the Quarter Ended September 28, 2002

[ ] Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number 1-11406

KADANT INC.
(Exact name of Registrant as specified in its charter)

Delaware	52-1762325
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

One Acton Place, Suite 202 Acton, Massachusetts	01720
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: (978) 776-2000

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days. Yes [X] No [ ]

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

Class	Outstanding at October 25, 2002
Common Stock, $.01 par value	13,546,952

PART I - Financial Information

Item 1 - Financial Statements

KADANT INC.

Consolidated Balance Sheet
(Unaudited)

Assets

(In thousands)	September 28, 2002	December 29, 2001
Current Assets:		
Cash and cash equivalents	$101,741	$102,807
Available-for-sale investments, at quoted market value (amortized cost of $18,927 and $16,625)	18,927	16,625
Accounts receivable, less allowances of $2,774 and $2,515	30,265	39,178
Unbilled contract costs and fees	14,127	10,126
Inventories:		
Raw materials and supplies	12,918	13,625
Work in process	5,376	6,962
Finished goods (includes $1,071 and $1,917 at customer locations)	10,909	12,947
Deferred tax asset	8,379	6,991
Other current assets	3,194	3,198
	205,836	212,459
Property, Plant, and Equipment, at Cost	71,529	71,710
Less: Accumulated depreciation and amortization	46,104	43,225
	25,425	28,485
Other Assets	9,175	10,441
Goodwill (Note 7)	117,664	116,269

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$358,100	$367,654
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KADANT INC.

Consolidated Balance Sheet (continued)
(Unaudited)

Liabilities and Shareholders' Investment

(In thousands except share amounts)	September 28, 2002	December 29, 2001
Current Liabilities:		
Current maturities of long-term obligations	$ 585	$ 573
Accounts payable	20,641	18,661
Accrued payroll and employee benefits	8,686	7,990
Accrued warranty costs	3,839	4,598
Customer deposits	2,729	3,070
Accrued merger consideration	-	2,824
Other accrued expenses (Note 5)	12,161	15,360
	48,641	53,076
Deferred Income Taxes and Other Deferred Items	11,574	11,457
Long-term Obligations:		
Subordinated convertible debentures (Note 6)	86,176	118,138
Notes payable	580	1,129
	86,756	119,267
Minority Interest	300	297
Shareholders' Investment:		
Preferred stock, $.01 par value, 5,000,000 shares authorized; none issued	-	-
Common stock, $.01 par value, 150,000,000 shares authorized; 14,045,550 and 12,745,165 shares issued (Note 8)	140	127
Capital in excess of par value (Note 8)	98,657	81,229
Retained earnings	147,401	143,504
Treasury stock at cost, 498,598 and 505,146 shares	(21,042)	(21,345)
Deferred compensation	(53)	(5)
Accumulated other comprehensive items (Note 2)	(14,274)	(19,953)
	210,829	183,557
	$358,100	$367,654

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

KADANT INC.

Consolidated Statement of Income
(Unaudited)

(In thousands except per share amounts)	Three Months Ended September 28, 2002	Three Months Ended September 29, 2001
Revenues	$50,084	$56,085
Costs and Operating Expenses:		
Cost of revenues	31,576	35,458
Selling, general, and administrative expenses	12,490	14,613
Research and development expenses	1,149	1,644
Restructuring costs (Note 5)	101	588
	45,316	52,303
Operating Income	4,768	3,782
Interest Income	676	1,574
Interest Expense	(1,084)	(1,872)
Income Before Provision for Income Taxes, Minority Interest, and Extraordinary Item	4,360	3,484
Provision for Income Taxes	1,657	1,452
Minority Interest (Income) Expense	1	(13)
Income Before Extraordinary Item	2,702	2,045
Extraordinary Item (net of income taxes of $3; Note 6)	5	-
Net Income	$ 2,707	$ 2,045
Basic and Diluted Earnings per Share Before Extraordinary Item	$ .20	$ .17
Basic and Diluted Earnings per Share (Note 3)	$ .20	$ .17
Weighted Average Shares (Note 3):		
Basic	13,547	12,273
Diluted	13,716	12,348

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

KADANT INC.

Consolidated Statement of Income
(Unaudited)

(In thousands except per share amounts)	Nine Months Ended September 28, 2002	Nine Months Ended September 29, 2001
Revenues	$139,802	$171,717
Costs and Operating Expenses:		
Cost of revenues	87,141	107,738
Selling, general, and administrative expenses	37,757	45,054
Research and development expenses	3,589	5,307
Restructuring and unusual costs (Note 5)	3,738	588
	132,225	158,687
Operating Income	7,577	13,030
Interest Income	1,954	5,527
Interest Expense	(3,720)	(5,616)
Income Before Provision for Income Taxes, Minority Interest, and Extraordinary Item	5,811	12,941
Provision for Income Taxes	2,202	5,407
Minority Interest (Income) Expense	3	(87)
Income Before Extraordinary Item	3,606	7,621
Extraordinary Item (net of income taxes of $178; Note 6)	291	-
Net Income	$ 3,897	$ 7,621
Basic and Diluted Earnings per Share Before Extraordinary Item	$ .28	$ .62
Earnings per Share (Note 3):		
Basic	$ .31	$ .62
Diluted	$ .30	$ .62
Weighted Average Shares (Note 3):		
Basic	12,744	12,276
Diluted	12,911	12,311

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

KADANT INC.

Consolidated Statement of Cash Flows
(Unaudited)

(In thousands)	Nine Months Ended September 28, 2002	Nine Months Ended September 29, 2001
Operating Activities:		
Net income	$ 3,897	$ 7,621
Adjustments to reconcile net income to net cash provided by operating activities:		
Noncash restructuring and unusual costs (Note 5)	2,441	-
Extraordinary item (Note 6)	(291)	-
Depreciation and amortization	3,893	7,093
Provision for losses on accounts receivable	233	1,081
Minority interest (income) expense	3	(87)
Other noncash items	522	(17)
Changes in current accounts:		
Accounts receivable	9,225	4,046
Unbilled contract costs and fees	(3,404)	(2,629)
Inventories	5,352	(3,737)
Other current assets	(1,259)	(3,968)
Accounts payable	1,155	1,998
Other current liabilities	(4,593)	(1,490)
Net cash provided by operating activities	17,174	9,911
Investing Activities:		
Acquisition of minority interest in subsidiary	(1,364)	-
Purchases of available-for-sale investments	(2,302)	-
Proceeds from maturities of available-for-sale investments	-	69,350
Advances from former affiliates, net	-	5,704
Purchases of property, plant, and equipment	(2,215)	(3,750)
Proceeds from repayments of note receivable	200	1,800
Other, net	(178)	5
Net cash provided by (used in) investing activities	(5,859)	73,109
Financing Activities:		
Repurchases of Company subordinated convertible debentures (Note 6)	(31,369)	-
Net proceeds from issuance of Company common stock in public offering (Note 8)	17,648	-
Net proceeds from issuance of Company and subsidiary common stock	472	490
Purchases of Company common stock	-	(587)
Acquisition of subsidiary common stock	(1,461)	-
Repayments of long-term obligations	(537)	(509)
Transfer from former parent company	-	1,309
Net cash provided by (used in) financing activities	$(15,247)	$ 703

KADANT INC.

Consolidated Statement of Cash Flows (continued)
(Unaudited)

(In thousands)	Nine Months Ended September 28, 2002	Nine Months Ended September 29, 2001
Exchange Rate Effect on Cash	$ 2,866	$ 1,262
Increase (Decrease) in Cash and Cash Equivalents	(1,066)	84,985
Cash and Cash Equivalents at Beginning of Period	102,807	62,461
Cash and Cash Equivalents at End of Period	$101,741	$147,446
Noncash Activities:		
Amounts forgiven in exchange for the acquisition of 49% minority interest in Kadant Composites Inc.	$ -	$ 2,053

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

KADANT INC.

Notes to Consolidated Financial Statements
(Unaudited)

1. General

The interim consolidated financial statements and related notes presented have been prepared by Kadant Inc. (also referred to in this document as "we," "Kadant," "the Company," or "the registrant") without audit and, in the opinion of management, reflect all adjustments of a normal recurring nature necessary for a fair statement of the Company's financial position at September 28, 2002, the results of operations for the three- and nine-month periods ended September 28, 2002, and September 29, 2001, and cash flows for the nine-month periods ended September 28, 2002, and September 29, 2001. Interim results are not necessarily indicative of results for a full year.

The consolidated balance sheet presented as of December 29, 2001, has been derived from the consolidated financial statements that have been audited by the Company's former independent auditors. The consolidated financial statements and related notes are presented as permitted by Form 10-Q and do not contain certain information included in the annual financial statements and related notes of the Company. The consolidated financial statements and notes included herein should be read in conjunction with the financial statements and related notes included in the Company's Annual Report on Form 10-K for the fiscal year ended December 29, 2001, as amended, filed with the Securities and Exchange Commission.

2. Comprehensive Income

Comprehensive income combines net income and "other comprehensive items" that represent certain amounts that are reported as components of shareholders' investment in the accompanying balance sheet, including foreign currency translation adjustments, unrealized net of tax gains and losses on available-for-sale investments, and deferred gains and losses on foreign currency contracts. During the third quarters of 2002 and 2001, the Company had comprehensive income of $4,361,000 and $4,041,000, respectively. During the first nine months of 2002 and 2001, the Company had comprehensive income of $9,576,000 and $8,879,000, respectively.

3. Earnings per Share

Basic and diluted earnings per share were calculated as follows:

	Three Months Ended		Nine Months Ended	
(In thousands except per share amounts)	September 28, 2002	September 29, 2001	September 28, 2002	September 29, 2001
Basic				
Income Before Extraordinary Item	$ 2,702	$ 2,045	$ 3,606	$ 7,621
Extraordinary Item (net of income taxes of $3 and $178)	5	-	291	-
Net Income	$ 2,707	$ 2,045	$ 3,897	$ 7,621
Weighted Average Shares	13,547	12,273	12,744	12,276
Basic Earnings per Share:				
Income Before Extraordinary Item	$ .20	$ .17	$ .28	$ .62
Extraordinary Item	-	-	.03	-
	$ .20	$ .17	$ .31	$ .62

3. Earnings per Share (continued)

(In thousands except per share amounts)	Three Months Ended September 28, 2002	Three Months Ended September 29, 2001	Nine Months Ended September 28, 2002	Nine Months Ended September 29, 2001
Diluted				
Income Before Extraordinary Item	$ 2,702	$ 2,045	$ 3,606	$ 7,621
Extraordinary Item (net of income taxes of $3 and $178)	5	-	291	-
Net Income	$ 2,707	$ 2,045	$ 3,897	$ 7,621
Weighted Average Shares	13,547	12,273	12,744	12,276
Effect of Stock Options	169	75	167	35
Weighted Average Shares, as Adjusted	13,716	12,348	12,911	12,311
Diluted Earnings per Share:				
Income Before Extraordinary Item	$ .20	$ .17	$ .28	$ .62
Extraordinary Item	-	-	.02	-
	$ .20	$ .17	$ .30	$ .62

Options to purchase approximately 400,700 and 509,100 shares of common stock for the third quarters of 2002 and 2001, respectively, and 507,600 and 447,000 shares of common stock for the first nine months of 2002 and 2001, respectively, were not included in the computation of diluted earnings per share because the options' exercise prices were greater than the average market price for the common stock and their effect would have been antidilutive.

In addition, the computation of diluted earnings per share for each period excludes the effect of assuming the conversion of the Company's 4 1/2% subordinated convertible debentures, convertible at $60.50 per share, because the effect would be antidilutive.

4. Business Segment Information

(In thousands)	Three Months Ended September 28, 2002	Three Months Ended September 29, 2001	Nine Months Ended September 28, 2002	Nine Months Ended September 29, 2001
Revenues:				
Pulp and Papermaking Equipment and Systems	$ 46,322	$ 55,174	$128,822	$165,847
Composite and Fiber-based Products	3,762	911	10,980	5,870
	$ 50,084	$ 56,085	$139,802	$171,717

4. Business Segment Information (continued)

(In thousands)	Three Months Ended September 28, 2002	Three Months Ended September 29, 2001	Nine Months Ended September 28, 2002	Nine Months Ended September 29, 2001
Income Before Provision for Income Taxes, Minority Interest, and Extraordinary Item (a):				
Pulp and Papermaking Equipment and Systems (b)	$ 5,839	$ 6,773	$12,746	$20,156
Composite and Fiber-based Products (c) (d)	(272)	(2,204)	(2,647)	(4,440)
Corporate (e)	(799)	(787)	(2,522)	(2,686)
Total Operating Income	4,768	3,782	7,577	13,030
Interest Income (Expense), Net	(408)	(298)	(1,766)	(89)
	$ 4,360	$ 3,484	$ 5,811	$12,941
Operating Income, Excluding Restructuring and Unusual Costs and Goodwill Amortization:				
Pulp and Papermaking Equipment and Systems	$ 5,940	$ 8,146	$14,845	$23,138
Composite and Fiber-based Products (d)	(272)	(2,127)	(1,008)	(4,246)
Corporate (e)	(799)	(787)	(2,522)	(2,686)
	$ 4,869	$ 5,232	$11,315	$16,206
Capital Expenditures:				
Pulp and Papermaking Equipment and Systems	$ 266	$ 399	$ 897	$ 1,131
Composite and Fiber-based Products	583	961	1,173	2,619
Corporate	18	-	145	-
	$ 867	$ 1,360	$ 2,215	$ 3,750

(a) Includes consolidated goodwill amortization of $862 and $2,588 in the three- and nine-month periods ended September 29, 2001, respectively.
(b) Includes goodwill amortization of $803 and $2,412 in the three- and nine-month periods ended September 29, 2001, respectively.
(c) Includes goodwill amortization of $59 and $176 in the three- and nine-month periods ended September 29, 2001, respectively.
(d) Includes operating losses from the composite building products business, excluding restructuring and unusual costs, of $376 and $1,331 in the three-month periods ended September 28, 2002 and September 29, 2001, respectively, and $2,107 and $2,969 in the nine-month periods ended September 28, 2002 and September 29, 2001, respectively.
(e) Primarily general and administrative expenses.

5. Restructuring and Unusual Costs

During the first nine months of 2002, the Company recorded restructuring and unusual costs of $3,738,000. Restructuring costs of $1,129,000, which were accounted for in accordance with Emerging Issues Task Force (EITF) Pronouncement No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (Including Certain Costs Incurred in a Restructuring)," related to severance costs for 68 employees across all functions primarily at the Company's Pulp and Papermaking Equipment and Systems (Papermaking Equipment) segment, all of whom were terminated as of September 28, 2002. These actions were taken in an effort to improve profitability and were in response to a continued weak market environment and reduced demand for our products. Unusual costs of $2,609,000 include noncash charges of $2,441,000 for asset writedowns, consisting of $953,000 for the impairment of a laboratory in Ohio held for sale at the Papermaking Equipment segment, and $1,488,000 for the writedown of fixed assets held for sale at the Composite and Fiber-based Products segment; and $168,000 for related disposal and facility-closure costs.

A summary of the changes in accrued restructuring costs, which are included in other accrued expenses in the accompanying consolidated balance sheet, follows:

(In thousands)	Severance
Balance at December 29, 2001	$ 56
Provision	1,129
Usage	(1,031)
Currency translation adjustment	5
Balance at September 28, 2002	$ 159

The Company expects to pay the remaining accrued restructuring costs primarily during the remainder of 2002.

6. Extraordinary Item

During the first quarter of 2002, the Company repurchased $2,875,000 principal amount of its 4 1/2% subordinated convertible debentures for $2,806,000 in cash, resulting in an extraordinary gain of $29,000, net of deferred debt charges, and net of income tax provision of $18,000. During the second quarter of 2002, the Company repurchased $26,987,000 principal amount of these debentures for $26,385,000 in cash, resulting in an extraordinary gain of $257,000, net of deferred debt charges, and net of income tax provision of $157,000. During the third quarter of 2002, the Company repurchased $2,100,000 principal amount of these debentures for $2,079,000 in cash, resulting in an extraordinary gain of $5,000, net of deferred debt charges, and net of income tax provision of $3,000. In the first nine months of 2002, the combined extraordinary gain resulting from these transactions was $291,000, net of deferred debt charges, and net of income tax provision of $178,000. As of September 28, 2002, $86,176,000 principal amount of the debentures remained outstanding.

7. Recent Accounting Pronouncements

"Business Combinations" and "Goodwill and Other Intangible Assets"

In July 2001, the Financial Accounting Standards Board (FASB) released for issuance Statement of Financial Accounting Standards (SFAS) No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets."

7. Recent Accounting Pronouncements (continued)

SFAS No. 141 requires the use of the purchase method of accounting and prohibits the use of the pooling-of-interests method of accounting for business combinations initiated after June 30, 2001. SFAS No. 141 also requires that the Company recognize acquired intangible assets apart from goodwill if the acquired intangible assets meet certain criteria.

SFAS No. 142 requires, among other things, that the Company no longer amortize goodwill, but instead test goodwill for impairment at least annually. In addition, SFAS No. 142 requires that the Company identify reporting units for the purpose of assessing potential impairments of goodwill, reassess the useful lives of other existing recognized intangible assets, and cease amortization of intangible assets with indefinite useful lives. Intangible assets with indefinite useful lives are to be tested for impairment in accordance with the guidelines in SFAS No. 142. SFAS No. 142 is to be applied for fiscal years beginning after December 15, 2001, to all goodwill and other intangible assets recorded as of January 1, 2002, regardless of when those assets were initially recognized. The Company is currently evaluating goodwill for impairment using the two-step process as prescribed in SFAS No. 142. The first step is an initial evaluation for potential impairment, while the second step measures the amount of the impairment. The Company completed the first step of the goodwill impairment test in the second quarter of 2002. Having completed step one, the Company expects that a portion of the goodwill related to both of its segments may be impaired. The Company currently has $113,488,000 and $4,176,000 of goodwill in the Papermaking Equipment segment and the Composite and Fiber-based Products segment, respectively. The Company has not yet determined the amount of the potential impairment, but plans to complete the measurement of the impairment in the fourth quarter of 2002. In accordance with the SFAS No. 142 transition procedures, an impairment that is required to be recognized when adopting the standard will be reflected as the cumulative effect of a change in accounting principle in the first quarter of 2002.

Pro forma results as if SFAS No. 142 had been adopted at the beginning of 2001 are as follows:

(In thousands except per share amounts)	Three Months Ended September 29, 2001	Nine Months Ended September 29, 2001
Net Income, as Reported	$2,045	$7,621
Add back: Goodwill Amortization	584	1,757
Net Income, as Adjusted	$2,629	$9,378
Basic and Diluted Earnings per Share, as Reported	$ .17	$ .62
Add back: Goodwill Amortization	.05	.14
Basic and Diluted Earnings per Share, as Adjusted	$ .22	$ .76

Accounting for the Impairment or Disposal of Long-lived Assets

In October 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-lived Assets." The standard provides guidance on measuring impairment of long-lived assets and applying accounting for discontinued operations upon adoption. The Company adopted the standard during the first quarter of 2002. Adoption of the standard did not affect the Company's financial statements.

7. Recent Accounting Pronouncements (continued)

Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections

In May 2002, the FASB issued SFAS No. 145, "Rescission of FASB Statements No. 4, 44, and 64, Amendment of FASB Statement No. 13, and Technical Corrections." Adoption of the standard is generally required in the fiscal year beginning after May 15, 2002. Under the standard, transactions currently classified by the Company as extraordinary items will no longer be treated as such but instead will be reported as other nonoperating income or expenses.

Accounting for Costs Associated with Exit or Disposal Activities

In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities," which supersedes EITF 94-3. The standard affects the accounting for restructuring charges and related activities. The provisions of this statement are required to be adopted for exit or disposal activities that are initiated after December 31, 2002. The provisions of EITF 94-3 will continue to apply with regard to the Company's previously announced restructuring plans.

8. Public Offering of Common Stock

In June 2002, the Company sold 1,300,000 shares of its common stock in a public offering at $14.62 per share, for net proceeds of $17,648,000.

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

Throughout this report on Form 10-Q, we make forward-looking statements, which are statements concerning possible or assumed future results of operations. When we use words such as "believes," "expects," "anticipates," "intends," "plans," "estimates," "should," "likely," "will," or similar expressions, we are making forward-looking statements. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties, and assumptions, and are based on the beliefs and assumptions of our management, using information currently available to our management. Our future results of operations may differ materially from those expressed in the forward-looking statements. Many of the important factors that will determine these results and values are beyond our ability to control or predict. You should not put undue reliance on any forward-looking statements. For a discussion of important factors that may cause our actual results to differ materially from those suggested by the forward-looking statements, you should read carefully the section captioned "Forward-Looking Statements" in this report on Form 10-Q. We assume no obligation to update any such forward-looking statements.

Overview

Company Background

Kadant operates in two segments: the Pulp and Papermaking Equipment and Systems (Papermaking Equipment) segment and the Composite and Fiber-based Products segment. Through our Papermaking Equipment segment, we develop, manufacture, and market a range of equipment and products for the domestic and international papermaking and paper recycling industries. We have been in operation for more than 100 years and have a large, stable customer base that includes most of the world's paper manufacturers. We also have one of the largest installed bases of

Overview (continued)

equipment in the pulp and paper industry, which provides us with a higher-margin spare parts and consumables business that we believe is less susceptible than our capital equipment business to the cyclical trends in the paper industry.

Through our Composite and Fiber-based Products segment, we manufacture and sell agricultural carriers derived from cellulose fiber, and develop, manufacture, and market fiber-based composite products for the building industry.

Prior to our incorporation, we operated as a division of Thermo Electron Corporation. We were incorporated in Delaware in November 1991 as a wholly owned subsidiary of Thermo Electron. In November 1992, we completed an initial public offering of our common stock and became a majority-owned public subsidiary of Thermo Electron. On July 12, 2001, we changed our name from Thermo Fibertek Inc. to Kadant Inc., and on August 8, 2001, we were spun off from Thermo Electron and became an independent public company.

Pulp and Papermaking Equipment and Systems Segment

Our Papermaking Equipment segment consists of three primary product lines: stock-preparation equipment, paper machine accessories, and water-management systems. Principal products manufactured by this segment include:

- custom-engineered systems and equipment for the preparation of wastepaper for conversion into recycled paper;
- accessory equipment and related consumables important to the efficient operation of papermaking machines; and
- water-management systems essential for the continuous cleaning of papermaking machine fabrics and the draining, purifying, and recycling of process water for paper sheet and web formation.

Composite and Fiber-based Products Segment

Our Composite and Fiber-based Products segment consists of two product lines: our fiber-based granular products and our composite building products. We employ patented technology to produce biodegradable absorbing granules from papermaking byproducts. These granules are primarily used as agricultural carriers and for home lawn and garden applications. In our composite building products business, we develop, produce, and market fiber-based composite products, primarily for the building industry, used for applications such as decking and railing systems and roof tiles. In January 2001, we acquired the remaining 49% equity interest that we did not already own in Kadant Composites Inc., which comprises our composite building products business.

International Sales

During 2001, approximately 55% of our sales were to customers outside the United States, principally in Europe. We generally seek to charge our customers in the same currency in which our operating costs are incurred. However, our financial performance and competitive position can be affected by currency exchange rate fluctuations affecting the relationship between the U.S. dollar and foreign currencies. We seek to reduce our exposure to currency fluctuations through the use of forward currency exchange contracts. We may enter into forward contracts to hedge certain firm purchase and sale commitments denominated in currencies other than our subsidiaries' functional currencies. These contracts hedge transactions principally denominated in U.S. dollars.

Overview (continued)

Critical Accounting Policies

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

Critical accounting policies are defined as those that reflect significant judgments and uncertainties, and could potentially result in materially different results under different assumptions and conditions. We believe that our most critical accounting policies, upon which our financial condition depends and which involve the most complex or subjective decisions or assessments, are those described in "Management's Discussion and Analysis of Financial Condition and Results of Operations" under the section captioned "Critical Accounting Policies" in Exhibit 13 to our Annual Report on Form 10-K for the fiscal year ended December 29, 2001, as amended, filed with the Securities and Exchange Commission. There have been no material changes since year-end 2001 that warrant further disclosure, except with respect to the valuation of goodwill under Statement of Financial Accounting Standards (SFAS) No. 142. The Company is currently evaluating goodwill for impairment using the two-step process as prescribed in SFAS No. 142 (Note 7). The first step is an initial evaluation for potential impairment, while the second step measures the amount of the impairment. The Company completed the first step of the goodwill impairment test in the second quarter of 2002. Having completed step one, the Company expects that a portion of the goodwill related to both of its segments may be impaired. As of September 28, 2002, the Company had $113.5 million and $4.2 million of goodwill in the Papermaking Equipment segment and the Composite and Fiber-based Products segment, respectively. The Company has not yet determined the amount of the potential impairment, but plans to complete the measurement of the impairment in the fourth quarter of 2002. In accordance with SFAS No. 142 transition procedures, an impairment that is required to be recognized when adopting the standard will be reflected as the cumulative effect of a change in accounting principle in the first quarter of 2002.

Industry and Business Outlook

Our products are primarily sold to the pulp and paper industry. The paper industry has been in a prolonged downcycle, characterized by weak pulp and paper prices, decreased capital spending, and consolidation of paper companies within the industry. As paper companies continue to consolidate in response to market weakness, they frequently reduce capacity and postpone or even cancel capacity addition or expansion projects. This trend, along with paper companies' actions to quickly reduce operating rates and restrict capital spending and maintenance programs, has adversely affected our business. Over the long term, as the markets recover, we expect that consolidation in the paper industry and improved capacity management will have a positive effect on paper companies' financial performance and, in return, will be favorable to both paper companies and their suppliers, such as Kadant.

There has been a significant amount of papermaking downtime in the pulp and paper industry in 2001 and 2002. This, coupled with weakened conditions in the world economy, has produced a difficult market environment resulting in deferrals of capital projects by the paper companies and pricing pressure in some of our product lines. The combination of these factors has caused a reduction in our revenues throughout 2002, and resulted in our lower operating results in the first nine months of 2002 versus the same period last year. To mitigate the effects of these difficult market conditions, we are concentrating our efforts on several initiatives to improve our product gross margins, including focusing on the higher-margin parts and consumables business across all our product lines, sourcing the manufacture of non-proprietary components from third party suppliers, shifting more production to our lower-cost manufacturing facility in Mexico, and lowering our manufacturing overhead costs throughout the business.

Overview (continued)

In addition, we continue to focus our efforts on managing our operating costs, capital expenditures, and working capital. The modest gain in momentum we saw midyear in the pulp and paper industry has stalled, and recovery will likely be slower than expected. In the third quarter of 2002, we experienced a 17% decrease in total bookings compared to last year. This is largely due to a decrease in orders for our stock preparation equipment, which include large orders for complete custom-engineered systems. The timing of these orders is difficult to predict. Therefore, we expect earnings in the fourth quarter of 2002 to be $.15 to $.18 per diluted share on revenues of $43 to $46 million. For the fiscal year ending December 28, 2002, we expect earnings per share, excluding restructuring and unusual costs and extraordinary items (Notes 5 and 6), to be $.60 to $.63 per diluted share on revenues of $182 to $185 million. The earnings estimate for 2002 includes the favorable effect of ceasing goodwill amortization ($.19 per diluted share in 2001) resulting from the adoption of SFAS No. 142, but excludes other possible effects on earnings in 2002 resulting from the adoption of SFAS No. 142, which may include an impairment charge to be determined in the fourth quarter of 2002 in accordance with that standard (Note 7). We believe the composite building products business will generate approximately $2.0 to $3.0 million of revenues, with operating losses of $0.3 million to $0.5 million, in the fourth quarter of 2002. We expect to generate from $8 to $9 million of revenues, with operating losses (excluding restructuring and unusual costs) of $2.4 to $2.6 million, from this business in 2002.

In October 2001, we terminated for nonperformance a distributor's exclusive rights to market and sell certain of our composite building products due to failure to meet minimum purchase commitments. We are now building and expanding our distribution network for composite building products and are advertising in trade magazines, conducting in-store promotions, and exhibiting at trade and home shows. We now have numerous distribution centers throughout the U.S. for our products. We believe that the market for composite building products will grow as consumer awareness of the advantages of these products increases their acceptance as an alternative to traditional wood products, especially in light of the phase-out of widely used CCA pressure-treated lumber that contains potentially harmful chemicals.

Results of Operations

Third Quarter 2002 Compared With Third Quarter 2001

Revenues

Revenues decreased to $50.1 million in the third quarter of 2002 from $56.1 million in the third quarter of 2001. Excluding the favorable effects of currency translation in 2002 of $1.6 million due to a weaker U.S. dollar relative to the functional currencies in countries in which we operate, revenues decreased by $7.6 million, or 14%.

Pulp and Papermaking Equipment and Systems Segment. Excluding the effect of currency translation, revenues at the Papermaking Equipment segment decreased to $44.7 million in the third quarter of 2002 from $55.2 million in the third quarter of 2001. Revenues from the Papermaking Equipment segment's stock-preparation equipment product line decreased by $6.4 million in 2002 primarily as a result of a decrease in export sales to China and, to a lesser extent, a decrease in sales in North America due to adverse market conditions. Revenues from the segment's water-management and accessories product lines decreased by $3.0 million and $1.2 million in 2002, respectively, primarily due to a decrease in demand in North America as a result of machine shutdowns and mill closures caused by industry consolidation and capacity rationalization, as well as pricing pressures.

Composite and Fiber-based Products Segment. Revenues at the Composite and Fiber-based Products segment increased to $3.8 million in the third quarter of 2002 from $0.9 million in the third quarter of 2001 largely due to an increase of $2.6 million in sales of our composite building products due to increased marketing efforts resulting in higher demand and expansion of our distribution channels.

Third Quarter 2002 Compared With Third Quarter 2001 (continued)

Gross Profit Margin

Gross profit margin remained constant at 37% in the third quarters of 2002 and 2001. The gross profit margin at the Papermaking Equipment segment decreased to 38% in 2002 from 39% in 2001 primarily due to lower revenues and increased pricing pressures, offset in part by a favorable change in product mix toward higher-margin products. The gross profit margin at the Composite and Fiber-based Products segment increased to 27% in 2002 compared to negative gross margins in 2001 primarily due to positive gross profit margins from our composite building products resulting from an increase in revenues. In addition, gross profit margins from our fiber-based granular products increased primarily due to a decrease in 2002 in the cost of natural gas used in the production process and, to a lesser extent, an increase in revenues and a change to a more favorable product mix.

Other Operating Expenses

Selling, general, and administrative expenses as a percentage of revenues decreased to 25% in the third quarter of 2002 from 26% in the third quarter of 2001. Selling, general, and administrative expenses decreased to $12.5 million in 2002 from $14.6 million in 2001 primarily due to cost-reduction efforts at the Papermaking Equipment segment, as well as the absence in 2002 of $0.9 million of goodwill amortization that was recorded in 2001.

Research and development expenses as a percentage of revenues were 2% in the third quarter of 2002 compared with 3% in the third quarter of 2001. Research and development expenses decreased to $1.1 million in the third quarter of 2002 compared with $1.6 million in the third quarter of 2001, primarily at the Papermaking Equipment segment due to restructuring efforts taken in 2002 and the closure of a redundant laboratory (Note 5).

Restructuring Costs

The Company recorded additional net restructuring charges of $101,000 during the third quarter of 2002. Restructuring charges of $157,000 related to severance costs for six manufacturing and sales employees at the Company's Papermaking Equipment segment, all of whom were terminated as of September 28, 2002. Restructuring income of $56,000 resulted from the reversal of severance costs that are no longer required related to restructuring efforts taken in the first quarter of 2002 at the Papermaking Equipment segment (Note 5). During the third quarter of 2001, the Company recorded restructuring costs of $0.6 million for severance costs relating to 52 employees primarily in the manufacturing and sales functions at the Papermaking Equipment segment's domestic subsidiaries, all of whom were terminated by September 29, 2001.

Operating Income

Operating income was $4.8 million in the third quarter of 2002 compared with $3.8 million in the third quarter of 2001. Excluding restructuring and unusual costs and goodwill amortization in the 2002 and 2001 periods, operating income at the Papermaking Equipment segment decreased to $5.9 million in 2002 from $8.1 million in 2001, and operating losses at the Composite and Fiber-based Products segment decreased to $0.3 million in 2002 from $2.1 million in 2001, due to the reasons discussed above.

Interest Income and Expense

Interest income decreased to $0.7 million in the third quarter of 2002 from $1.6 million in the third quarter of 2001. Of the total decrease in interest income in 2002, approximately $0.5 million was due to lower prevailing interest rates, and $0.4 million was due to lower average invested balances. The decrease in average invested balances primarily relates to repurchases of our subordinated convertible debentures (Note 6), the redemption in September 2001 of our Thermo Fibergen subsidiary's common stock and, to a lesser extent, consideration paid to Thermo

Third Quarter 2002 Compared With Third Quarter 2001 (continued)

Fibergen shareholders for the acquisition of their minority interest. Interest expense decreased to $1.1 million in the third quarter of 2002 from $1.9 million in the third quarter of 2001 as a result of repurchases of our subordinated convertible debentures (Note 6).

Income Taxes

The effective tax rate was 38% in the third quarter of 2002 and 42% in the third quarter of 2001. The effective tax rates exceeded the statutory federal income tax rate primarily due to the impact of state income taxes and nondeductible expenses. The effective tax rate decreased in 2002 as a result of the elimination of goodwill amortization, including nondeductible goodwill, under SFAS No. 142 (Note 7) and various tax planning initiatives.

Minority Interest

Minority interest (income) expense in the third quarters of 2002 and 2001 represents the minority investors' share of earnings or losses in our majority-owned subsidiaries.

Extraordinary Item

During the third quarter of 2002, we repurchased $2.1 million principal amount of our 4 1/2% subordinated convertible debentures for $2.1 million in cash, resulting in an extraordinary gain of $5,000, net of deferred debt charges, and net of income tax provision of $3,000 (Note 6).

First Nine Months 2002 Compared With First Nine Months 2001

Revenues

Revenues decreased to $139.8 million in the first nine months of 2002 from $171.7 million in the first nine months of 2001. Excluding the favorable effects of currency translation in 2002 of $1.0 million due to a weaker U.S. dollar relative to the functional currencies in countries in which we operate, revenues decreased by $32.9 million, or 19%.

Pulp and Papermaking Equipment and Systems Segment. Excluding the effect of currency translation, revenues at the Papermaking Equipment segment decreased to $127.8 million in the first nine months of 2002 from $165.8 million in the first nine months of 2001. Revenues from the Papermaking Equipment segment's stock-preparation equipment product line decreased by $25.8 million in 2002 primarily as a result of a decrease in sales in North America and Europe due to adverse market conditions and, to a lesser extent, a decrease in export sales to China. Revenues from the segment's water-management and accessories product lines decreased by $7.6 million and $4.9 million in 2002, respectively, primarily due to a decrease in demand in North America as a result of machine shutdowns and mill closures caused by industry consolidation and capacity rationalization, as well as pricing pressures.

Composite and Fiber-based Products Segment. Revenues at the Composite and Fiber-based Products segment increased to $11.0 million in the first nine months of 2002 from $5.9 million in the first nine months of 2001, primarily as a result of an increase of $4.4 million in sales of our composite building products due to increased marketing efforts resulting in higher demand and expansion of our distribution channels. In addition, revenues from our fiber-based granular products increased by $0.7 million in 2002 primarily due to the introduction of two new applications of our agricultural carrier products.

First Nine Months 2002 Compared With First Nine Months 2001 (continued)

Gross Profit Margin

Gross profit margin increased to 38% in the first nine months of 2002 from 37% in the first nine months of 2001. The gross profit margin at the Papermaking Equipment segment was 39% in both periods. The gross profit margin at the Composite and Fiber-based Products segment increased to 26% in 2002 from negative gross margins of 6% in 2001 primarily due to the reasons discussed in the results of operations for the third quarter of 2002 compared with the third quarter of 2001.

Other Operating Expenses

Selling, general, and administrative expenses as a percentage of revenues increased to 27% in the first nine months of 2002 from 26% in the first nine months of 2001 due to lower revenues. Selling, general, and administrative expenses decreased to $37.8 million in 2002 from $45.1 million in 2001 primarily due to cost-reduction efforts at the Papermaking Equipment segment, as well as the absence in 2002 of $2.6 million of goodwill amortization that was recorded in 2001.

Research and development expenses as a percentage of revenues were 3% in both periods. Research and development expenses decreased to $3.6 million in the first nine months of 2002 compared with $5.3 million in the first nine months of 2001, primarily at the Papermaking Equipment segment due to restructuring efforts taken in 2002 and the closure of a redundant laboratory (Note 5).

Restructuring and Unusual Costs

During the first nine months of 2002, the Company recorded restructuring and unusual costs of $3.7 million. Restructuring costs of $1.1 million, which were accounted for in accordance with Emerging Issues Task Force Pronouncement No. 94-3, related to severance costs for 68 employees across all functions primarily at the Company's Papermaking Equipment segment, all of whom were terminated as of September 28, 2002. These actions were taken in an effort to improve profitability and were in response to a continued weak market environment and reduced demand for our products. Unusual costs of $2.6 million include noncash charges of $2.4 million for asset writedowns, consisting of $1.0 million for the impairment of a laboratory in Ohio held for sale at the Papermaking Equipment segment, and $1.4 million for the writedown of fixed assets held for sale at the Composite and Fiber-based Products segment; and $0.2 million for related disposal and facility-closure costs (Note 5). During the first nine months of 2001, the Company recorded restructuring costs of $0.6 million for severance costs relating to 52 employees primarily in the manufacturing and sales functions at the Papermaking Equipment segment's domestic subsidiaries, all of whom were terminated by September 29, 2001.

Operating Income

Operating income was $7.6 million in the first nine months of 2002 compared with $13.0 million in the first nine months of 2001. Excluding restructuring and unusual costs and goodwill amortization in the 2002 and 2001 periods, operating income at the Papermaking Equipment segment decreased to $14.8 million in 2002 from $23.1 million in 2001, and operating losses at the Composite and Fiber-based Products segment decreased to $1.0 million in 2002 from $4.2 million in 2001, due to the reasons discussed above.

Interest Income and Expense

Interest income decreased to $2.0 million in the first nine months of 2002 from $5.5 million in the first nine months of 2001. Of the total decrease in interest income in 2002, approximately $2.1 million was due to lower prevailing interest rates, and $1.4 million was due to lower average invested balances. The decrease in average

First Nine Months 2002 Compared With First Nine Months 2001 (continued)

invested balances primarily relates to repurchases of our subordinated convertible debentures (Note 6), the redemption in September 2001 of our Thermo Fibergen subsidiary's common stock and, to a lesser extent, consideration paid to Thermo Fibergen shareholders for the acquisition of their minority interest. Interest expense decreased to $3.7 million in the first nine months of 2002 from $5.6 million in the first nine months of 2001 as a result of the repurchases of our subordinated convertible debentures (Note 6).

Income Taxes

The effective tax rate was 38% in the first nine months of 2002 and 42% in the first nine months of 2001. The effective tax rates exceeded the statutory federal income tax rate primarily due to the impact of state income taxes and nondeductible expenses. The effective tax rate decreased in 2002 as a result of the elimination of goodwill amortization, including nondeductible goodwill, under SFAS No. 142 (Note 7) and various tax planning initiatives.

Minority Interest

Minority interest (income) expense in the first nine months of 2002 and 2001 represents the minority investors' share of earnings or losses in our majority-owned subsidiaries.

Extraordinary Item

During the first nine months of 2002, we repurchased $32.0 million principal amount of our 4 1/2% subordinated convertible debentures for $31.3 million in cash, resulting in an extraordinary gain of $291,000, net of deferred debt charges, and net of income tax provision of $178,000 (Note 6).

Liquidity and Capital Resources

Consolidated working capital was $157.2 million at September 28, 2002, compared with $159.4 million at December 29, 2001. Included in working capital are cash, cash equivalents, and available-for-sale investments of $120.7 million at September 28, 2002, compared with $119.4 million at December 29, 2001. Of the total cash, cash equivalents, and available-for-sale investments at September 28, 2002, $7.6 million was held by a majority-owned subsidiary, and the remainder was held by us and our wholly owned subsidiaries. At September 28, 2002, $57.5 million of cash, cash equivalents, and available-for-sale investments was held by our foreign subsidiaries.

During the first nine months of 2002, cash of $17.2 million was provided by operating activities compared with $9.9 million in the first nine months of 2001. A decrease in accounts receivable provided cash of $9.2 million in 2002 primarily at the Papermaking Equipment segment largely due to a decrease in revenues and improved collection efforts, offset in part by a use of cash of $3.4 million resulting from an increase in unbilled contract costs and fees at the Papermaking Equipment segment due to the timing of progress billings on large contracts. A decrease in inventories provided cash of $5.4 million in 2002 primarily at the Papermaking Equipment segment as a result of our efforts to match inventory levels with demand. In addition, an increase in accounts payable provided cash of $1.2 million in 2002 primarily at the Papermaking Equipment segment due to the timing of payments. A use of cash of $4.6 million in 2002 resulted from a decrease in other accrued liabilities, primarily accrued interest, accrued warranty costs, deferred revenues and, to a lesser extent, accrued income taxes.

Our investing activities, excluding available-for-sale investments and advances to former affiliates, used $3.6 million of cash in the first nine months of 2002, compared with $1.9 million in the first nine months of 2001. During the first nine months of 2002, we purchased property, plant, and equipment for $2.2 million, including $1.1 million at our composite building products business, the effects of which were slightly offset by our collection of $0.2 million

Liquidity and Capital Resources (continued)

from a note receivable related to the September 2000 sale of a fiber-recovery and water-clarification services plant. In addition, we paid $1.4 million in 2002 in connection with the acquisition of the minority interest of our Thermo Fibergen subsidiary.

Our financing activities used cash of $15.2 million in the first nine months of 2002, compared with $0.7 million provided in the first nine months of 2001. During the first nine months of 2002, we used $31.4 million to fund repurchases of our subordinated convertible debentures (Note 6), as well as $0.5 million to fund the payment of other long-term obligations. In addition, we paid $1.5 million in connection with the acquisition of common stock of our Thermo Fibergen subsidiary. These uses of cash were offset in part by $17.6 million of cash provided from the June 2002 issuance of 1.3 million shares of our common stock in a public offering (Note 8). In September 2001, our board of directors authorized the repurchase, through September 24, 2002, of up to $50 million of our debt and equity securities in the open market or in negotiated transactions. In April 2002, our board of directors authorized the repurchase, through April 9, 2003, of up to an additional $50 million of our debt and equity securities in the open market or in negotiated transactions. As of September 28, 2002, we had $34.6 million remaining under this authorization.

At September 28, 2002, we had $85.3 million of undistributed foreign earnings that could be subject to tax if remitted to the U.S. If we repatriate undistributed foreign earnings into the U.S., we do not expect that this will have a material adverse effect on our current liquidity.

Our net cash (calculated as cash, cash equivalents, and available-for-sale investments less total short- and long- term debt) was $33.3 million at September 28, 2002, compared with net debt of $0.4 million at December 29, 2001.

Although we currently have no material commitments for capital expenditures, during the remainder of 2002, we plan to make expenditures for property, plant, and equipment of approximately $1.6 million, including $0.7 million at our composite building products business. The expected composite expenditures largely relate to refinements and improvements we are making to optimize the production process and expand capacity at our manufacturing facility.

Our ability to use our cash and to incur additional debt is limited by financial covenants in our distribution agreement, as amended, with Thermo Electron. These financial covenants require that (1) the ratio of our net indebtedness to net capitalization not exceed 40% and (2) on a rolling four quarter basis, that the sum of our (a) operating income (excluding restructuring and other unusual items, such as gains on sales of assets, included in operating income), (b) amortization of goodwill and other intangible assets, and (c) interest income, be at least four times greater than interest expense. In instances where the ratio of our net indebtedness to net capitalization is less than or equal to 20% for any measurement date, the coverage ratio of four times greater than interest expense is lowered to three times greater than interest expense. As of September 28, 2002, we were in compliance with all the financial covenants of the agreement, as amended. If we fail to comply with the financial covenants, Thermo Electron could require us to refinance our debentures, conduct an exchange offer for the debentures, or repay in full the underlying obligation. If we were required to take any of these actions, we might not have sufficient cash or credit capacity to engage in transactions, such as a significant acquisition, that might otherwise benefit our business. These circumstances could also impair our ability to continue to engage in transactions that have been integral to our historical operations. In the future, our liquidity position will be primarily affected by the level of free cash flows from operations and the amount of cash expended on repurchases of our subordinated convertible debentures and acquisitions, if any. We believe that our existing resources, together with the cash we expect to generate from operations, are sufficient to meet the capital requirements of our existing operations for the foreseeable future.

Forward-Looking Statements

In connection with the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995, we wish to caution readers that the following important factors, among others, in some cases have affected, and in the future could affect, our actual results and could cause our actual results in 2002 and beyond to differ materially from those expressed in any forward-looking statements made by us, or on our behalf.

Our business is dependent on the condition of the pulp and paper industry, which is currently in a downcycle.

We sell products primarily to the pulp and paper industry. Generally, the financial condition of the global pulp and paper industry corresponds to the condition of the general economy, as well as to a number of other factors, including pulp and paper production capacity relative to demand. The global pulp and paper industry has been in a prolonged downcycle, with depressed pulp and paper prices, decreased spending, mill closures, consolidations, and bankruptcies. The North American pulp and paper industry has been particularly adversely affected by higher energy prices and slowing economies. As paper companies continue to consolidate in response to market weakness, they frequently reduce capacity and postpone or even cancel capacity addition or expansion projects. This cyclical downturn has adversely affected our business. Mill closures, consolidations, and bankruptcies of customers have caused our sales to decline and, if we are unable to collect from our customers, our profitability may be adversely affected. The financial condition of the pulp and paper industry may not improve in the near future, and the severity of the downturn could expand to our European and Asian businesses.

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

During 2001, approximately 55% of our sales were to customers outside the United States, principally in Europe and China. International revenues are subject to a number of risks, including the following:

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

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

An increasing portion of our international sales has and may in the future come from China. We are currently planning to establish an assembly facility in China for our stock preparation equipment and related aftermarket parts. An increase in revenues, as well as operation of an assembly facility in China, will expose us to increased risk in the event of changes in the policies of the Chinese government, political unrest or unstable economic conditions in China, or developments in China or in U.S.-China relations that are adverse to trade, including enactment of protectionist legislation or trade restrictions. In addition, orders from customers in China, particularly for large systems that have been tailored to a customer's specific requirements, involve increased risk of cancellation prior to shipment due to payment terms that are applicable to doing business in China. The timing of these orders is difficult to predict.

Forward-Looking Statements (continued)

We are subject to intense competition in all of our markets.

We encounter significant competition in each of our principal markets. We believe that the principal competitive factors affecting the markets for our products include quality, price, service, technical expertise, and product innovation. Our competitors include a number of large multinational corporations such as Voith Paper GmbH and Metso Corporation. Competition, especially in China, could increase if new companies enter the market or if existing competitors expand their product lines or intensify efforts within existing product lines. Competitors' technologies may prove to be superior to ours. Many of these competitors may have substantially greater financial, marketing, and other resources than we do. As a result, they may be able to adapt more quickly to new or emerging technologies and changes in customer requirements, or to devote greater resources to the promotion and sale of their services and products. Our current products, those under development, and our ability to develop new technologies may not be sufficient to enable us to compete effectively. In addition, our composite building products business is subject to intense competition, particularly in the decking market, from traditional wood products and other composite lumber manufacturers, many of whom have greater financial, technical, and marketing resources than we do. As a result, we may be unable to compete successfully in this market.

Our composite building products business is a new entrant into a new market. Our success will depend on our ability to manufacture and commercialize our composite building products.

In 2000, we began to develop, produce, market, and sell composite products primarily for the building industry. Development, manufacturing, and commercialization of our composite building products require significant development and testing of the products, and our efforts may not be successful. Further, our composite building products may not gain market acceptance. We expect to incur significant branding and distribution expenses to successfully market and distribute these products. Our ability to market these products successfully depends on the willingness of consumers to purchase fiber-based composite products as an alternative to traditional building products. To penetrate the market and gain market share, we need to educate consumers, including wood suppliers, distributors, contractors, and homebuilders, regarding the benefits of our fiber-based composite products over products made of wood, slate, and other traditional materials. This strategy may not be successful. We have little or no experience manufacturing these products at volume, cost, and quality levels sufficient to satisfy expected demand, and we may encounter difficulties in connection with any large-scale manufacturing or commercialization of these new products. If we were to exit this business, we would incur significant losses.

Our composite building products business may not be able to obtain effective distribution of its products and may experience seasonal fluctuation in sales and quarterly operating results.

The composite building products business is subject to intense competition, and we rely on distributors in the building products industry to market, distribute, and sell our products. We may be unable to produce our products in sufficient quantity to interest these distributors or to retain and add new distributors. If we are unable to distribute our products effectively, our revenues would decline and we would have to incur additional expenses to market these products directly.

In general, the building products industry experiences seasonal fluctuations in sales particularly in the fourth quarter, in which holidays and adverse weather conditions in some regions usually reduce the level of home improvement and new construction activity. As our business grows, we would expect our sales in the fourth quarter to reflect this seasonal variation. Operating results will tend to be lower in quarters with lower sales, which are not offset by a corresponding reduction in operating costs. In addition, we may also experience lower gross profit margins in the fourth quarter and first quarter due to seasonal incentive discounts offered to our distributors. As a result of these factors, we believe sequential period-to-period comparisons of our operating results are not reliable indicators of future performance, and the operating results for any quarterly period may not be indicative of operating results to be expected for a full year.

Forward-Looking Statements (continued)

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

Our composite building products are new, have not been on the market for long periods of time, and may be used in applications for which we may have no knowledge or limited experience. Because we have limited historical experience, we may be unable to predict the potential liabilities related to product warranty or product liability issues. If our products fail to perform over their warranty periods, we may not have the ability to protect ourselves adequately against this potential liability, which could reduce our operating results.

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

We are dependent on a single paper mill for the fiber used in the manufacture of our composite building products and fiber-based granules. This mill has the exclusive right to supply the papermaking byproducts used to manufacture the granules used in our process. Although we believe our relationship with the mill is good, the mill could decide not to renew its contract with us in 2003, or may not renew on commercially reasonable terms, and we would be forced to find an alternative supply for this raw material. We may be unable to find an alternative supply on commercially reasonable terms or could incur excessive transportation costs if an alternative supplier were found, which would increase our manufacturing costs and may prevent our products from being competitive. Our composite building products also contain recycled and off-spec plastics, which are subject to wide fluctuations in pricing and availability. We may be unable to obtain sufficient quantities at reasonable prices, which could adversely affect our ability to produce a sufficient quantity of our products or produce our products at competitive prices.

In addition, we use natural gas in the production process for our fiber-based granular products. We manage our exposure to natural gas price fluctuations by entering into short-term forward contracts to purchase specified quantities of natural gas from a supplier. There can be no assurance that we will be effective in managing our exposure to natural gas price fluctuations. High natural gas prices will have an adverse effect on our results of operations.

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

Our strategy includes the acquisition of technologies and businesses that complement or augment our existing products and services. Promising acquisitions are difficult to identify and complete for a number of reasons, including competition among prospective buyers and the need for regulatory, including antitrust, approvals. Any acquisition we may complete may be made at a substantial premium over the fair value of the net assets of the acquired company. We may not be able to complete future acquisitions, integrate any acquired businesses successfully into our existing businesses, make such businesses profitable, or realize anticipated cost savings or synergies, if any, from these acquisitions. The size and selection of suitable acquisition candidates also may be limited due to the financial covenants we have with Thermo Electron Corporation, our former parent company.

In addition, we have previously acquired several companies and businesses. As a result of these acquisitions, we have recorded significant goodwill on our balance sheet, which amounts to approximately $117.7 million as of September 28, 2002. In accordance with SFAS No. 142, we assess the carrying value of the goodwill that we have recorded at least annually or whenever events or changes in circumstances indicate that its current carrying value has diminished. These events or circumstances generally would include operating losses or a significant decline in earnings associated with the acquired business or asset. SFAS No. 142 transition procedures state that an impairment charge that is required to be recognized when adopting the standard will be reflected as the cumulative effect of a change in accounting principle in the first quarter of 2002. We are currently evaluating goodwill for impairment using the two-step process as prescribed in SFAS No. 142. The first step is an initial evaluation for potential impairment, while the second step measures the amount of the impairment. We completed the first step of the goodwill impairment test in the

Forward-Looking Statements (continued)

second quarter of 2002. Having completed step one, we expect that a portion of the goodwill related to both of our segments may be impaired. We have not yet determined the amount of the potential impairment, but plan to complete this measurement in the fourth quarter of 2002. Any future impairment losses recorded after the transition period will be recorded as a reduction to operating income, which could have a material adverse affect on our results of operations. Our ability to realize the value of the goodwill that we have recorded will depend on the future cash flows of these businesses. These cash flows in turn depend, in part, on how well we have integrated these businesses.

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

We place considerable emphasis on obtaining patent and trade secret protection for significant new technologies, products, and processes because of the length of time and expense associated with bringing new products through the development process and into the marketplace. Our success depends in part on our ability to develop patentable products and obtain and enforce patent protection for our products both in the United States and in other countries. We own numerous U.S. and foreign patents, and we intend to file additional applications, as appropriate, for patents covering our products. We have filed for a patent relating to our composite building products business. Patents may not be issued for any pending or future patent applications owned by or licensed to us, and the claims allowed under any issued patents may not be sufficiently broad to protect our technology. Any issued patents owned by or licensed to us may be challenged, invalidated, or circumvented, and the rights under these patents may not provide us with competitive advantages. In addition, competitors may design around our technology or develop competing technologies. Intellectual property rights may also be unavailable or limited in some foreign countries, which could make it easier for competitors to capture increased market position. We could incur substantial costs to defend ourselves in suits brought against us or in suits in which we may assert our patent rights against others. An unfavorable outcome of any such litigation could materially adversely affect our business and results of operations. In addition, as our patents expire, we rely on trade secrets and proprietary know-how to protect our products. We cannot be sure the steps we have taken or will take in the future will be adequate to deter misappropriation of our proprietary information and intellectual property.

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

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

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

Given the nature of the markets in which we participate and the effect of Staff Accounting Bulletin No. 101, "Revenue Recognition in Financial Statements" (SAB No. 101), which became effective as of January 2000, we cannot reliably predict future revenues and profitability, and unexpected changes may cause us to adjust our

Forward-Looking Statements (continued)

operations. A significant proportion of our costs are fixed, due in part to our significant selling, research and development, and manufacturing costs. Thus, small declines in revenues could disproportionately affect our operating results. Other factors that could affect our quarterly operating results include:

- failure of our products to pass contractually agreed upon acceptance tests, which would delay or prohibit recognition of revenues under SAB No. 101;
- demand for and market acceptance of our products;
- competitive pressures resulting in lower sales prices of our products;
- adverse changes in the pulp and paper industry;
- delays or problems in the introduction of new products by us;
- our competitors' announcements of new products, services, or technological innovations;
- contractual liabilities incurred by us related to guarantees of our equipment performance;
- increased costs of raw materials or supplies, including the cost of energy; and
- changes in the timing of product orders.

Anti-takeover provisions in our charter documents and under Delaware law and the potential tax effects of our spinoff from Thermo Electron could prevent or delay transactions that our shareholders may favor.

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

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

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

The tax treatment of the distribution of our common stock by Thermo Electron under the Internal Revenue Code and regulations thereunder could also serve to discourage an acquisition of our company. An acquisition of our company within two years following the distribution, which took place in August 2001, could result in federal tax liability being imposed on Thermo Electron and, in more limited circumstances, on shareholders of Thermo Electron who received shares of our common stock in the distribution. In addition, even acquisitions occurring more than two years after the distribution could cause the distribution to be taxable to Thermo Electron if the acquisitions were determined to be pursuant to an overall plan that existed at the time of the distribution. As part of the distribution, we have agreed to indemnify Thermo Electron, but not the shareholders of Thermo Electron, for any resulting tax liability if the tax liability is attributable to certain acts by us, including an acquisition of our company. The prospect of that tax liability and our indemnification obligation may have anti-takeover effects.

Forward-Looking Statements (continued)

A number of actions following our spinoff from Thermo Electron could cause the distribution to be fully taxable to shareholders of Thermo Electron who received shares of our common stock in the distribution and/or to Thermo Electron, and to us.

The IRS has issued a ruling that no gain or loss will be recognized by us, Thermo Electron, or its shareholders upon the distribution of our common stock as of the date of the distribution, except with respect to cash received in lieu of fractional shares of our common stock and distributions of our common stock acquired by Thermo Electron within the past five years in taxable transactions. However, the distribution could become fully taxable if we, Thermo Electron, or the shareholders of Thermo Electron who received shares of our common stock in the distribution, take any of a number of actions following the distribution. We have entered into a tax matters agreement with Thermo Electron that restricts our ability to engage in these types of actions. If any conditions of the IRS ruling are not satisfied, the distribution could become taxable to the shareholders of Thermo Electron who received shares of our common stock in the distribution and/or Thermo Electron. As part of the distribution, we have agreed to indemnify Thermo Electron, but not the shareholders of Thermo Electron, for any resulting tax liability if the tax liability is attributable to certain acts by us.

Sales of substantial amounts of our common stock may occur from time to time, which could cause our stock price to decline.

Our shares were distributed pro rata to the shareholders of Thermo Electron, and from time to time, these shareholders have sold and may in the future sell substantial amounts of our common stock in the public market if our shares no longer meet their investment criteria or other objectives. Any sales of substantial amounts of our common stock in the public market, or the perception that such sales might occur, whether as a result of the distribution or otherwise, could cause the market price of our common stock to decline.

If we are unable to comply with the financial covenants contained in our distribution agreement with Thermo Electron, we may be required to take certain actions that could compromise our ability to execute our business plan.

We have agreed to certain financial covenants contained in our distribution agreement with Thermo Electron that restrict our use of cash and our ability to incur additional debt as part of Thermo Electron's continued guarantee of our subordinated convertible debentures. If we fail to comply with these financial covenants, Thermo Electron could, among other things, require us to refinance our debentures, conduct an exchange offer for the debentures, or repay in full the underlying obligation. If we are required to take any of these actions, we might not have sufficient cash or credit capacity to engage in transactions, such as significant acquisitions, that might otherwise benefit our business.

Continuing low interest rates, coupled with declines in operating income, could cause us to no longer be in compliance with the financial covenants contained in our distribution agreement with Thermo Electron, and we may be unable to renegotiate the covenants or obtain a waiver from Thermo Electron.

The unexpected decline in interest rates in the fall of 2001, coupled with lower invested cash balances and lower operating income, resulted in our non-compliance with one of the financial covenants originally negotiated in our distribution agreement with Thermo Electron. We were able to negotiate an amendment to the agreement that resulted in our compliance with the financial covenants, as amended. If we should again fail to comply with the financial covenants, there is no assurance that Thermo Electron would either renegotiate the covenants on terms satisfactory to us or grant a waiver.

Forward-Looking Statements (continued)

We may have potential business conflicts of interest with Thermo Electron with respect to our past and ongoing relationships that could harm our business operations.

Conflicts of interest may arise between Thermo Electron and us in a number of areas relating to our past and ongoing relationships, including: labor, tax, employee benefit, indemnification, and other matters arising from our separation from Thermo Electron; and restrictions related to our use of cash and our ability to incur indebtedness in connection with Thermo Electron's continuing obligations under its guarantee of our subordinated convertible debentures. We may not be able to resolve any potential conflicts

Item 3 - Quantitative and Qualitative Disclosures About Market Risk

Our exposure to market risk from changes in interest rates, equity prices, and foreign currency exchange rates has not changed materially from our exposure at year-end 2001.

Item 4 - Controls and Procedures

Within the 90 days prior to the filing of this quarterly report, our chief executive officer (CEO) and chief financial officer (CFO) performed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, our CEO and CFO concluded that our disclosure controls and procedures are designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and are operating in an effective manner. There have been no significant changes in our internal controls or in other factors that could significantly affect these internal controls subsequent to the date of the most recent evaluation by our CEO and CFO.

PART II - OTHER INFORMATION

Item 2 - Changes in Securities and Use of Proceeds

For a description of restrictions on our working capital that may be imposed due to the financial covenants contained in our distribution agreement with Thermo Electron, refer to the section captioned "Liquidity and Capital Resources" in Item 2 of Part I in this report on Form 10-Q.

Item 6 - Exhibits and Reports on Form 8-K

(a) Exhibits

See Exhibit Index on the page immediately preceding exhibits.

(b) Reports on Form 8-K

None.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized as of the 6th day of November 2002.

KADANT INC.

/s/ Thomas M. O'Brien

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

CERTIFICATIONS

I, William A. Rainville, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Kadant Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

   b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

   c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 6, 2002 /s/ William A. Rainville

William A. Rainville
Chief Executive Officer

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

1. I have reviewed this quarterly report on Form 10-Q of Kadant Inc.;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

    a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

    b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and

    c) presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

    a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

    b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: November 6, 2002

/s/ Thomas M. O'Brien

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

KADANT INC.

EXHIBIT INDEX

Exhibit Number	Description of Exhibit
99.1	Certification of the Chief Executive Officer of the Registrant Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of Sarbanes-Oxley Act of 2002.
99.2	Certification of the Chief Financial Officer of the Registrant Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of Sarbanes-Oxley Act of 2002.

Exhibit 99.1

CERTIFICATION
Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. Section 1350, the undersigned officer of Kadant Inc., a Delaware corporation (the "Company"), does hereby certify that:

The Quarterly Report on Form 10-Q for the quarter ended September 28, 2002 of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in this Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 6, 2002

/s/ William A. Rainville

William A. Rainville
Chief Executive Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of a separate disclosure document.

Exhibit 99.2

CERTIFICATION
Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to
Section 906 of the Sarbanes-Oxley Act of 2002

Pursuant to 18 U.S.C. Section 1350, the undersigned officer of Kadant Inc., a Delaware corporation (the "Company"), does hereby certify that:

The Quarterly Report on Form 10-Q for the quarter ended September 28, 2002 of the Company fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and the information contained in this Quarterly Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: November 6, 2002

/s/ Thomas M. O'Brien

Thomas M. O'Brien
Chief Financial Officer

The foregoing certification is being furnished solely pursuant to 18 U.S.C. Section 1350 and is not being filed as part of a separate disclosure document.