

The Shaw Group Inc.

2001 ANNUAL REPORT

The Shaw Group Inc. is the world's only vertically-integrated provider of complete piping systems and comprehensive engineering, procurement and construction services to the power generation industry. Shaw is the largest supplier of fabricated piping systems in the United States and a leading supplier worldwide. The Company also engages in work for the process industries, including petrochemical, chemical and refining, and the environmental & infrastructure sector.

Founded in 1987, Shaw has expanded rapidly through internal growth and the completion and integration of a series of strategic acquisitions. The Company currently employs approximately 13,000 individuals and maintains offices and operations in North America, South America, Europe, the Middle East and the Asia-Pacific regions.



How Shaw Wins.

Letter to Our Shareholders

In 2001, The Shaw Group again demonstrated we have what it takes to win. Our operational and financial performance continued to lead the industry and reinforced our reputation as the preferred provider of world-class products and services.

We won for shareholders with a record-breaking year that saw sales and earnings more than double, and our backlog increase by more than \$2.5 billion. We won for customers by pursuing innovative strategies that deliver quality and confidence at reasonable costs. We won for communities by being there when we were needed.

There are many reasons for these successes. They include our financial strength, which enables us to execute a business plan that is right for its time. An ongoing commitment to finding better ways to provide value. The ability to align our interests with those of our customers. The unrivaled expertise of our people. These factors have enabled us to establish a record of remarkable accomplishment, and put us in a strong position to maintain our profitability in a world and an industry that continue to change.

Financial Highlights

For the year ended August 31, 2001, we realized a 101 percent increase in earnings to \$61.2 million, before extraordinary item, or \$1.46 per diluted share. This compares with earnings of \$30.4 million, before extraordinary item and cumulative effect of change in accounting principle, or \$0.99 per diluted share, last year. Sales increased 102 percent to over \$1.5 billion compared with \$763 million for fiscal year 2000.

Due primarily to the strength of the domestic power market, our backlog totaled \$4.5 billion at year-end, representing a 135 percent increase over the previous year's \$1.9 billion. Power generation projects make up 79 percent of the backlog, followed by process industries at 15 percent, environmental & infrastructure at 5 percent, and other industries at 1 percent. Domestic backlog is 83 percent of the total. We expect to work off approximately 42 percent, or \$1.9 billion, of our total backlog in fiscal year 2002.

Achievements

In addition to another year of outstanding financial performance, 2001 saw a number of noteworthy accomplishments:

Stone & Webster (S&W) Integration. We were able to quickly and successfully integrate Stone & Webster into The Shaw Group, and are moving forward without any major issues outstanding. S&W's comprehensive expertise—which includes premier engineering capabilities—is delivering added value and superior resources to customers worldwide.

Target Pricing. We introduced a new pricing concept that adds value to both Shaw and our customers. A target price is agreed to before a project is undertaken; when we come in under budget, customers receive a portion of the savings. Customers become more deeply involved in the project—which creates a new level of trust—while getting a high-quality job that is on time and at the lowest total installed cost.

Power Contract Awards. Contract activity was strong in 2001. We extended our relationship with NRG Energy, winning two projects in Mississippi and Louisiana totaling 1,520 megawatts, in addition to the contract for the expansion of the Big Cajun I site in Louisiana, which we completed during the year. Other announcements included a five-year agreement to provide maintenance and modification services for Exelon's 17 nuclear operating units; four projects with PG&E's National Energy Group that total 4,400 megawatts; two power plants in the Northwest and Southeast totaling 840 megawatts, and a 725-megawatt cogeneration power plant for FP&L Energy.



“...we believe Shaw will continue to win for many years to come.”

(In thousands, except per share data)

	Years Ended August 31,		
	2001	2000	1999
Operating Results			
Total Revenues	\$1,538,932	\$ 762,655	\$494,014
Gross Profit	246,616	127,076	93,828
Income Before Extraordinary Item and Cumulative Effect of Change in Accounting Principle	61,212	30,383	18,121
Income Per Diluted Share Before Extraordinary Item and Cumulative Effect of Change in Accounting Principle (1)	1.46	0.99	0.73

Balance Sheet Data

Total Assets	\$1,701,854	\$1,335,083	\$407,062
Working Capital	521,044	102,786	113,975
Short-Term Debt	8,587	30,251	51,618
Long-Term Debt	512,867	254,965	87,841
Shareholders' Equity	598,393	377,275	174,239
Number of Shares Outstanding at Year End (1)	41,012	35,402	23,472

(1) Fiscal year ended August 31, 2000 and 1999 have been restated to reflect the effect of the December 2000 two-for-one stock split of the Company's Common Stock.

101% increase in earnings

EntergyShaw. EntergyShaw began to take advantage of the power market build-up. Operating under the EntergyShaw arrangement, construction started on a simple cycle plant in Illinois and a combined cycle plant in Texas for two separate ventures partially owned by Entergy.

Ethylene Project in China. We were chosen to provide engineering, procurement, and construction services for a 600,000 metric ton per year ethylene plant in Nanjing, People's Republic of China. Under the contract with BASF-YPC, Stone & Webster's ethylene technology will be the cornerstone of a \$2.6 billion integrated petrochemical site. This represents a significant opportunity in a re-emerging market.

Continued Commitment to Technology. With the acquisition of Stone & Webster, we doubled our research and development budget in a clear demonstration of our commitment to grow the Company's technology base. Additionally, Shaw's proprietary systems ShawDraw™, ShawMan™, and ShawTrac™ provide a new level of value and efficiency to customers.

Looking Ahead

We expect to continue to see growth at high rates. With the demand for electricity continuing, much of the growth will be in power, and we are uniquely positioned to capitalize on a predicted rebound in both coal and nuclear.

There are also opportunities beyond power generation. Chemical plants are expected to undergo maintenance and retrofit work to meet stricter environmental regulations. We see activity in the petrochemical, refining, and general industrial markets. We will also remain an important player in the ethylene market, where S&W has supplied approximately 40 percent of the incremental capacity worldwide since 1990.

As we look to the future, we see a world that has undergone many changes over the years. There have been ups and downs in the technology sector. The economy has been strong at some points, erratic at others. New global markets have emerged, bringing with them noteworthy shifts in political, social, and economic alliances.

Shaw has successfully managed these uncertainties. We have not been afraid to adapt and evolve, and we know how to prosper in unpredictable times. That will never change. And it is why we believe Shaw will continue to win for many years to come.

J. M. Bernhard, Jr.
Chairman of the Board, President and Chief Executive Officer

The Shaw Group has demonstrated a consistent ability to win for all of our audiences, from shareholders and customers to employees and the communities where we operate. The key to this success has been an ongoing effort to align our interests with those of the people and clients we serve. The result has been a performance that is superior in every respect.

Our achievements can be attributed to a number of factors:

Financial strength; a commitment to sound customer relationships and value-added service; expertise; innovation; employees; and our civic involvement.

It is these factors that have helped shape a Company and a vision that focuses on creating relationships where everyone wins.

Financial Strength

THE RIGHT BUSINESS MODEL AT THE RIGHT TIME

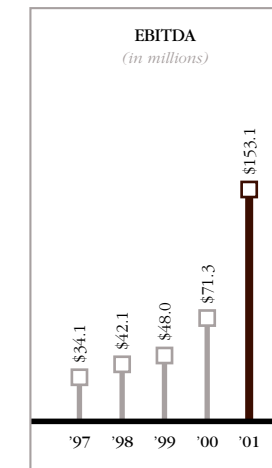
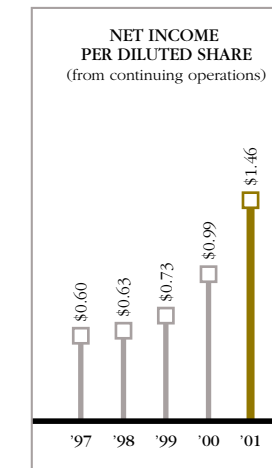
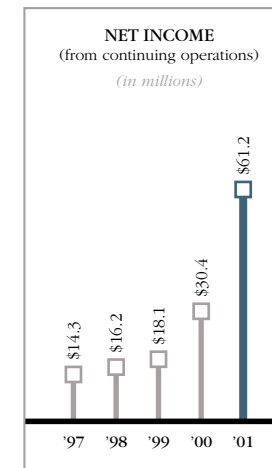
In the eight years since Shaw became a public company, we have seen a record-breaking performance. We have increased profits every year. Earnings per share and EBITDA are at an all-time high. Our backlog has soared and continues to provide clear visibility of future growth.

We have achieved this despite significant changes in the engineering and construction (E&C) industry. The continuing ability of our management team to anticipate these changes, and to evaluate and seize the opportunities they present, has contributed greatly to our profitability. We have complemented this with an across-the-board discipline in everything from business development to controlling internal and external costs. This has put us in a position of financial strength that is unusual in our industry. It is a position we believe we will not only maintain, but also build upon.

Our confidence is a product of many things. We are maximizing our profit potential during the current build-up of power generation capacity with a business model that blends intelligent risk management and comprehensive capabilities. We examine projects on a job-by-job basis. We assess risk and rewards objectively and realistically, and avoid projects that could weaken our financial position.

Effective risk-management is at the core of our business model. This model allows us to work with the customer prior to the engineering and construction of a facility. There are no high-risk premiums. Customers agree to share the risk in return for a portion of the savings that can result from our ability to deliver a job on time and within budget. This gives them an incentive to take a more active role in the project and work more closely with us, which ultimately strengthens our relationship. It also allows everyone to continually focus on price without losing sight of the ultimate objective, which is ensuring that customers get the lowest total installed cost with the highest possible quality and the quickest time to market.

Our success in managing risk is embedded in our structure and operations. While the Company began as a pipe fabricator in 1987, we have strategically added capabilities over the years, including construction, engineering, pipe erection, manufacturing, and consulting. This vertical integration has given us expertise in critical industries such as power, petrochemical, refinery, and environmental & infrastructure, while enabling us to control more facets of a given project. At the same time, it is also contributing directly to our financial strength. For example, we previously had to subcontract all of our structural steel work. But when we acquired SS&S Fabricators this year, we were able to increase its backlog virtually overnight and capture the resulting revenue stream.



The collective benefits to customers of our successful risk management—improved efficiency, lower costs, greater confidence—translate to repeat business, often in the form of longer-term, multi-project deals that are important to a steady, predictable cash flow. Our success with NRG Energy represents a good case in point. After we successfully completed the company's Big Cajun I plant this year, we were awarded two additional projects: a 1,200-megawatt combined cycle facility in Pike County, Mississippi, and a 320-megawatt peaking unit near Jennings, Louisiana. These kinds of jobs, which we have been winning from a diverse base of top-tier customers, provide us with a visibility that has a positive residual with the investment community.

Our financial strength benefits customers in other ways as well. Clients want stable partners. We provide stability. Our customers know that they can confidently share the risk and the potential reward. They also know that with a strong, viable company as a partner, they are more likely to secure the money they need to build, grow, and expand. Shaw is that kind of company.

The key to executing our model is liquidity. A strong cash position, especially in a tight credit market, ensures we have the funds to operationalize our strategy. Our performance over the years has placed us in such a position. The balance sheet is strong and net debt is low. This has contributed to a level of financial strength that will enable us to keep winning for shareholders and customers alike.



Customers

CUSTOMER RELATIONSHIPS/VALUE Shaw has recognized that in today's global marketplace, customers want partners committed to helping them become more efficient, more competitive, and more profitable. We have responded with an approach to business that aligns our interests with those of our client. We build strong and lasting relationships with customers, and are always looking for newer, better ways to bring added value to the products and services we provide. Critical to that is our ability to consistently meet our customers' criteria for success. Our vertical integration and broad capabilities eliminate traditional handoffs and third parties, bringing a new level of efficiency to any job, and helping us deliver products and projects on time. We have been able to drive down costs through innovative strategies and long-term agreements with providers that enable us to pass savings along to clients. By accomplishing all of this—and by continuing to provide superior performance—we are building win-win relationships that bring value not only to customers but to our shareholders as well.



Customer Relationships & Customer Value

ALIGNING INTERESTS FOR EFFICIENCY AND PROFITABILITY

As the global marketplace becomes more competitive, companies need partners who share their vision and are committed to helping increase their efficiency and profitability. Shaw has responded by creating win-win relationships with customers that align our interests with theirs, and deliver added value throughout the process.

The Value of Relationships

The E&C industry has been shifting from a transaction business to a relationship business. To win in this climate, companies must recognize that the importance of the customer does not begin and end with the value of the contract. It extends to the strength of the partnership.

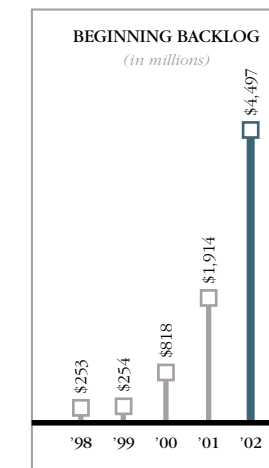
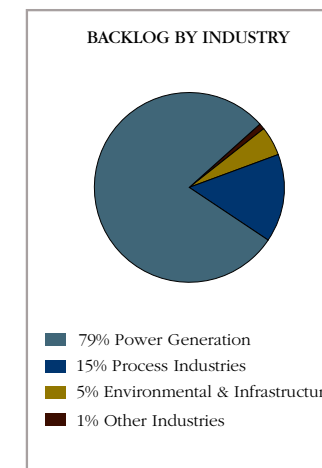
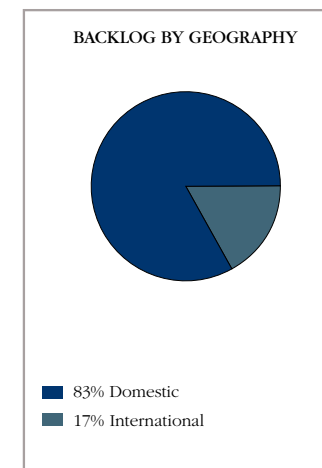
Shaw understands this. We build winning relationships from the ground up. We get involved with customers early to ensure that every aspect of a project is mapped out, critical material delivery issues are pinpointed and problems are identified and resolved before they occur. We do not do the same old thing in the same old way with the same old results. Instead, we work with customers to provide what they need before they realize they need it, and help optimize their operations to achieve superior results.

Critical to this is our willingness to look at projects from the client's perspective. We focus on whatever drives the customer, and then put the right people, plans and equipment in place to deliver maximum confidence and total satisfaction. This "in the trenches" approach enables us to combine our expertise with the customer's industry knowledge to produce an outcome in which everyone wins.

In the current power market, for example, it is critical that providers get their product to customers fast. But contractors typically have not turned systems over to operators until the plant was completed. We recognized the importance of speed-to-market, and designed a plan allowing systems turnover to begin when the facility is 70 percent complete. Customers can start providing capacity more quickly, and thus gain a competitive edge.

Stone & Webster Consultants is developing a new device that further reinforces our dedication to working from the customer's point of view. Understanding the importance of reducing costs in a deregulated market, the consulting company's subsidiary, Power Technologies, a world leader in electric systems analysis, created a monitoring instrument that enables utilities to know exactly how much electricity can flow over a transmission line. It allows customers to get more capacity on a single line and reduces the need for new installation. One Northeastern company calculated its potential annual savings at \$50 million.

We are also strengthening our customer relationships by creating value-added alliances with subcontractors. Our ability to deal with the same companies improves quality and consistency, reduces costs, and



assures a greater level of trust, knowledge, and project expertise. These benefits are apparent to customers. When they see that we share common goals with our subcontractors—to deliver a quality project on time at the best possible price—it reinforces their confidence in Shaw. That confidence generates repeat business, which supports long-term profitability and continuing shareholder value.

Meeting Customer Demand for Value

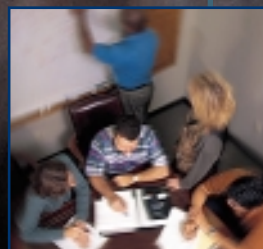
Our customers define value in three ways: efficiency, timely delivery, and the ability to assure superior quality at a reasonable cost. Shaw's success in meeting and exceeding these demands has been important to our emergence as an industry leader.

To begin with, our broad expertise has created seamless integration with one point of interface. There are none of the traditional handoffs and no third parties. Complementing this is ShawTrac, a web-based application that tracks and measures the progress of an entire project, from estimating to delivery. It keeps us apprised of where we are at every step in the process, including budget and scheduling on a day-to-day basis, and monitors essential variables at each of our facilities—a critical factor considering that 13 percent of construction costs revolve around material flow. Especially beneficial to the larger jobs we have targeted under our business model, ShawTrac enables us to manage projects more efficiently, and provides for continuing process and quality improvement.

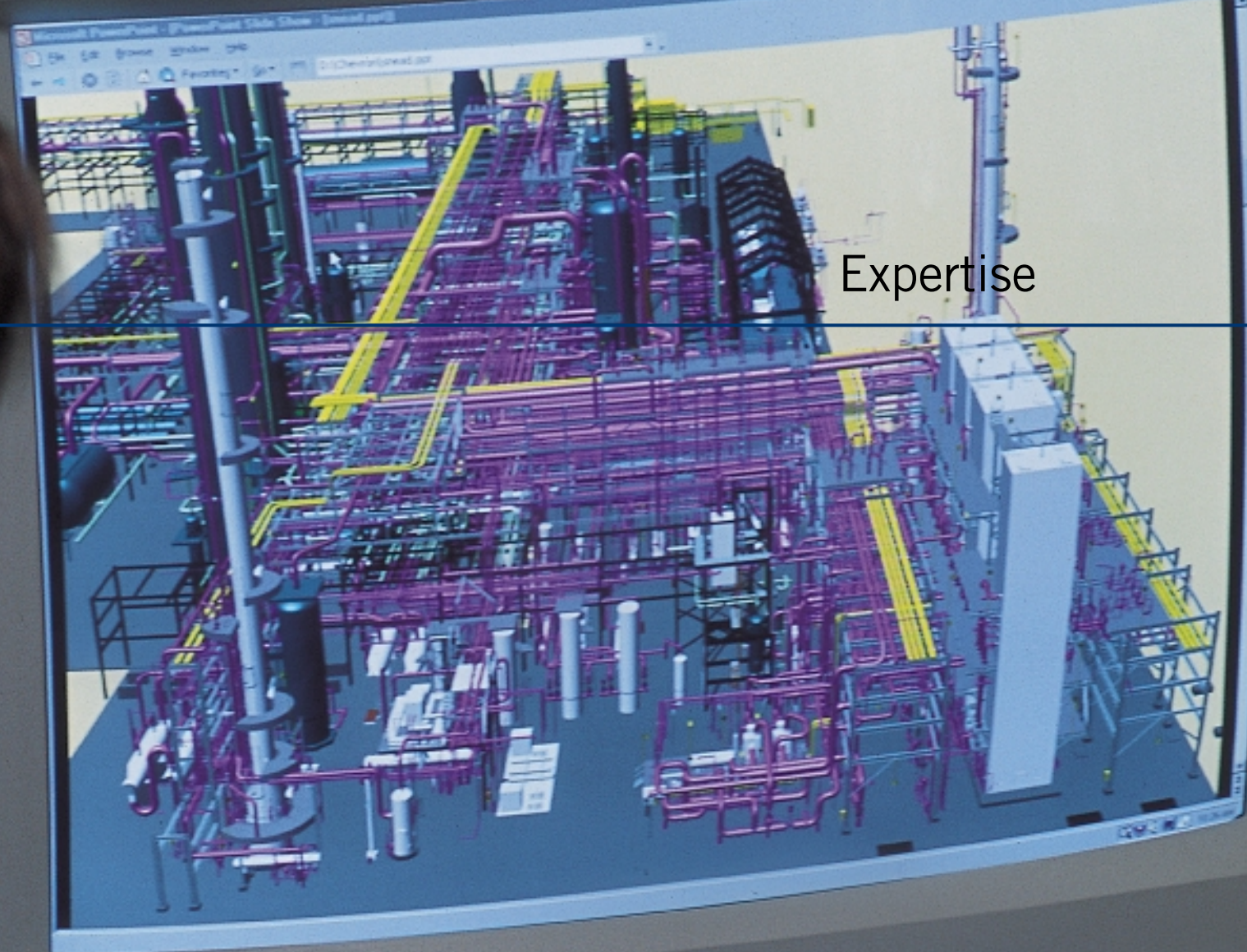
We have also been able to consistently deliver products on time, and according to the often-strict timetables that customers demand. Our record speaks for itself. We ship multiple systems of piping and components monthly under our contract with a leading turbine manufacturer, which uses them for its gas turbines. We have not been late on a delivery in over two years. We completed the 235-megawatt expansion of the Big Cajun I power plant under budget and ahead of schedule for NRG Energy. It was an achievement many thought was impossible, and helped us win contracts to build two additional NRG facilities.

We provide superior products and services while helping customers reduce costs. Because of long-term relationships with "preferred providers," we can extract value from suppliers and pass it along to customers. Finally, our experience in virtually every aspect of a project means we know where costs can be squeezed out. So when customers are seeking a better, more efficient way to build, we can deliver solutions that make everybody a winner.

EXPERTISE/INNOVATION Our comprehensive expertise, which runs the spectrum from pipe fabrication and construction to the world-class engineering and consulting services provided by Stone & Webster, ensures that we have the skill and experience to shape value-added, customer-focused solutions. It also provides us a broad perspective that is rare in our industry. This insight has enabled us to anticipate and manage any changes that might impact a project or client, and to react responsively. We have complemented this expertise with a commitment to innovation, applying the industry's most advanced technologies to everything from plant construction to project management. These innovative approaches include our state-of-the-art induction bending process, which is faster, stronger and more cost-effective; software applications that ensure efficiency in every phase of a job, and modular construction, a building process that saves customers time and money. This winning combination of expertise and innovation gives clients the confidence of knowing we can deliver whatever they need—and more—and do it better than our competitors.



Expertise



Expertise & Innovation

THE KNOWLEDGE AND SKILL TO SURPASS EXPECTATIONS

In today's marketplace, doing what is expected is not enough. Customers want more—more expertise, more innovative solutions, and more services. Shaw has the resources and capabilities to deliver on those demands, ensuring that we will continue to win for customers worldwide.

The Ability To Deliver on Any Commitment

Shaw brings customers unique experience compared to the competition. We build coal, gas-fired, and nuclear power plants, and we have installed piping systems in facilities with an aggregate generation capacity of more than 200,000 megawatts. To date, we have worked on power projects in more than 50 countries on six continents; served as design engineers for 17 U.S. nuclear plants, and provided services to over 100 nuclear plants.

The vertical integration that is essential to our business model allows us to provide these and a comprehensive range of additional services. In an industry where customers are making greater demands from fewer suppliers, we have the capabilities and expertise to meet any challenge and to deliver on any commitment.

Our 13 pipe fabrication facilities worldwide can produce 34,500 pipe spools—or 10,150 tons of product—every month. Their operations are coordinated under an integrated management system that enables us to meet the most demanding project schedules while still maximizing customer service and value. We build projects of all sizes and complexity in the power, process, and environmental & infrastructure industries. Our engineering teams utilize state-of-the-art plant management software to develop the design of power piping systems. We manufacture an extensive line of products for the power and process industries.

With the acquisition of Stone & Webster, these competencies broadened considerably to include:

Engineering. We now provide total planning, design, procurement, construction, operation and maintenance, management, and engineering services.

Consulting. Stone & Webster Consultants offers world-class services to the energy industry in the United States and abroad. This technical and commercial expertise has benefited owners, lenders, developers, and governments, and includes more than 5,000 international projects. It is a world leader in advisory services for privatizations, new private power and process industry projects, and utility asset sales.

Process Technologies. Using proprietary technology that delivers cost-effective solutions to the petrochemical and refining industries, S&W is a world leader in the process engineering and construction market.

Environmental & Infrastructure. Currently involved in more than 250 projects worldwide, S&W provides complete environmental consulting, engineering, siting, permitting, design, and remediation services.

This collective expertise gives us a rare perspective. We have a broader view of what works and does not work, and possess the ability to anticipate changes that affect customers and act quickly in response.



Providing superior
expertise from over
60 locations in
13 countries

It is an insight that has helped us execute well and consistently, and underscored our success in building a winning track record based on trust, confidence, and customer loyalty.

Innovative Solutions for Greater Value

Shaw's experience and knowledge is evident in our commitment to developing innovative solutions that add value to everything we do. Our exclusive induction bending process, which requires fewer cut-and-weld connections, is stronger, faster, less expensive, and less labor-intensive than typical pipe fabrication processes. It is a state-of-the-art technology that provides us a clear competitive and technological advantage.

We have eight induction bending machines in operation that can bend pipe up to 66 inches in diameter with walls as thick as 5 inches. Additionally, we offer a portable version of the machine that can move from job site to job site, anyplace in the world. This provides a more efficient alternative to the traditional fabrication process.

Among the other innovative products and services we provide are:

- **Reference plant designs**, which can reduce capital costs and bring new facilities on line faster. These standardized plant models are expected to reduce construction, commissioning and operating costs significantly.
- **ShawDraw**, which accepts electronically customer data files and translates the data files into working production drawings. ShawDraw can accept data files from a variety of 3-D engineering modeling systems, and generate shop details and bills of material for piping fabrication.
- **ShawMan**, a tool that tracks the flow of material through the engineering, procurement, and manufacturing processes, and provides inventory management and pricing models.
- **ShawTrac**, a web-based, customized application that enables us to monitor all aspects of a project, including estimating, enterprise resource planning, scheduling, and contract management.

We are also the industry leader in modularization, a process in which plant components are built off-site in controlled environments and then transported to the construction location for final installation. This is in sharp contrast to the traditional stick-build approach, where the entire facility is built on-site from the ground up. The process can be applied to components such as pipe racks, equipment skids, heat recovery steam generators and modular electric buildings.

The benefits of modularization to customers are significant. It reduces capital costs and takes expensive work-hours out of the field. Risks associated with weather and labor shortages, both of which can threaten on-schedule completion, are minimized considerably. By reducing these risks and their related costs, Shaw is able to negotiate more wisely—and more profitably—on a more diverse range of projects.

EMPLOYEES/COMMUNITIES Shaw recognizes that for the Company to succeed, our employees have to succeed. That's why we have created an environment that allows maximum opportunities for personal and professional advancement. We are giving our employees the tools they need to continue contributing to our growth, and they are responding with a work ethic, "nothing-is-impossible" attitude and dedication that is unrivaled in our industry. But our employees do more than help Shaw win. They help their communities win, too, by participating in a meaningful way in efforts to improve the quality of life in those areas where we have a corporate presence. As we have grown over the years, we have never forgotten that our local responsibilities extend far beyond business alone. That commitment is central to our corporate philosophy. Beyond that, it reflects an understanding that we know much is expected of us, and we are willing to do what it takes to maintain and build upon the community ties that have been an important part of our success.



Commitment



People & Local Community

WINNING EMPLOYEES WHO WIN FOR THEIR COMMUNITIES

Successful companies are built on the dedication and focus of their people. Shaw is no different. The character and commitment of our employees have played an important part not only in our success, but also in the success of those communities who depend on us in any way for their well being.

Winners

Shaw wins because our people are winners. They come to work every day committed to helping our Company grow, and making it more productive and profitable. The reason is simple: Employees see Shaw as a dynamic organization—not stagnant, not locked into old ways of doing things—and know that our successes create greater opportunities for them.

We have built a work environment that reflects the entrepreneurial spirit upon which Shaw's prosperity is founded. Our employees are encouraged to take risks if they believe customers will benefit. Good ideas are not stifled, but are allowed to flow upward and become policy if their value to clients is proved. We demand excellence and a strong work ethic, and our people deliver every day. The result is a team of employees who not only understand how Shaw's business model wins for all our stakeholders, but also how to apply it to support the Company's growth.

This approach—combining a can-do spirit with a model that provides both internal and external value—has enabled Shaw to attract and maintain world-class employees. We constantly look for opportunities for our people. In doing so, we create a perpetual cycle of reward: When people see opportunities, they work to seize them. When that happens, customers benefit. When customers benefit, Shaw continues to grow. When Shaw continues to grow, we can continue to recruit the best people.

The bottom line is that our employees understand their futures are tied to the success of our business model. They want to win for the Company, the customers, and themselves. As Shaw's performance has repeatedly shown, they are not only succeeding but also building upon that commitment every year.

Giving Back To Our Communities

We recognize that we do not exist alone. We are part of local communities whose interests go beyond the strength and success of our business. By involving ourselves in meaningful ways—through everything from civic involvement to education initiatives to disaster relief—we are doing our part to help our communities win.

We recognize that we do not exist alone.
We are part of local communities whose interests go beyond
the strength and success of our business.



The strength of this dedication runs deep, and can be found at every level in every location. Our corporate commitment to the United Way, for example, has translated into significant direct financial support to areas where Shaw has a presence. This clearly reflects our understanding that everything we do affects our communities, and that we have a duty to improve the quality of life of those who live there.

In 2001, company-wide, The Shaw Group Inc. raised over \$500,000 for our national United Way campaign, setting a record for funds raised by the Company. We also realize that unique events can make unique demands of a company—demands that go beyond the day-to-day obligations we feel as a corporate citizen. In the wake of September's devastating terrorist attacks, the Company and its employees contributed over \$250,000 to the "United Way September 11th Fund" benefiting victims of the tragedies in New York, Washington, and Pennsylvania.

But we also help communities win with locally based programs that, while less visible, are important in their own way. We have taken a leadership role in education. Our managers and employees have helped set up trade schools, and taught at high schools and vocational-technical institutions. This has created a classic win-win situation: Shaw is helping to train and educate our own potential workforce, while at the same time providing people with skills that can create job opportunities for a lifetime.

We have become an industry leader because we know how to provide value to the people we serve. In that regard, the commitment to our communities is no different. By encouraging employees at every level to give of themselves, their time and their money, we underscore our value proposition every day. And that has helped make our communities, our people, and our Company the winners we have all become.

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Selected Consolidated Financial Data

The following table presents, for the periods and as of the dates indicated, selected statement of income data and balance sheet data of the Company on a consolidated basis. The selected historical consolidated financial data for each of the three fiscal years in the period ended August 31, 2001 presented below has been derived from the Company's audited consolidated financial statements. Such data should be read in conjunction with the Consolidated Financial Statements of the Company and related notes thereto included elsewhere in this Annual Report and in "Management's Discussion and Analysis of Financial Condition and Results of Operations."

	Year Ended August 31,				
<i>(in thousands, except per share amounts)</i>	2001 (2)	2000 (3)	1999	1998 (4)	1997 (5)(6)
Consolidated Statements of Income					
Sales	\$1,538,932	\$ 762,655	\$494,014	\$501,638	\$335,734
Income from continuing operations	\$ 60,997	\$ 30,383	\$ 18,121	\$ 16,232	\$ 14,300
Basic income per common share before extraordinary item and cumulative effect of change in accounting principle (1)	\$ 1.53	\$ 1.03	\$ 0.76	\$ 0.65	\$ 0.62
Diluted income per common share before extraordinary item and cumulative effect of change in accounting principle (1)	\$ 1.46	\$ 0.99	\$ 0.73	\$ 0.63	\$ 0.60
Consolidated Balance Sheets					
Total assets	\$1,701,854	\$1,335,083	\$407,062	\$389,844	\$262,459
Long-term debt obligations, net of current maturities	\$ 512,867	\$ 254,965	\$ 87,841	\$ 91,715	\$ 39,039
Cash dividends declared per common share	\$ —	\$ —	\$ —	\$ —	\$ —

(1) Earnings per share amounts for 1997 have been restated for the adoption of Statement of Financial Standards No. 128, "Earnings per Share." Additionally, earnings per share for fiscal 2000, 1999, 1998 and 1997 have been restated to reflect the effect of the December 2000 two-for-one stock split of the Company's Common Stock.

(2) Includes the acquisition of certain assets of Scott, Sevin & Schaffer, Inc. and Technicomp, Inc. in fiscal 2001. See Note 3 of Notes to Consolidated Financial Statements.

(3) Includes the acquisitions of certain assets of Stone & Webster and PPM Contractors, Inc. in fiscal 2000. See Note 3 of Notes to Consolidated Financial Statements.

(4) Includes the acquisitions of certain assets of Prospect Industries plc, Lancas, C.A., Cojafex B.V. and Bagwell Brothers, Inc. in fiscal 1998.

(5) Includes the acquisitions of Pipe Shields Incorporated and United Crafts, Inc. and certain assets of MERIT Industrial Constructors, Inc. in fiscal 1997.

(6) Fiscal 1997 was restated to exclude the discontinued operations disposed of in fiscal 1998.

Management's Discussion and Analysis of Financial Condition and Results of Operations

The following analysis of the financial condition and results of operations of the Company should be read in conjunction with the Company's Consolidated Financial Statements, including the notes thereto.

General

The Company is the world's only vertically-integrated provider of complete piping systems and comprehensive engineering, procurement and construction ("EPC") services to the power generation industry. While approximately 79% of Shaw's backlog at August 31, 2001 was attributable to the power generation industry, the Company also does work in the process industries and the environmental and infrastructure industries. The Company's financial performance is impacted by the broader economic trends affecting its customers. All of the major industries in which Shaw operates are cyclical. Because Shaw's customers participate in a broad portfolio of industries, the Company's experience has been that downturns in one of its sectors may be mitigated by opportunities in others.

The acquisition by the Company of Stone & Webster, Incorporated ("Stone & Webster") in July 2000 more than doubled the size of the Company. This acquisition has significantly increased the Company's size and scope of its engineering, procurement and construction businesses and the Company's overall operations. For additional information regarding the Stone & Webster acquisition, see "—Recent Acquisitions," "—Liquidity and Capital Resources" and Note 3 of Notes to Consolidated Financial Statements.

As of August 31, 2001, the Company's backlog was approximately \$4.5 billion, of which 79% was attributable to power generation, 15% was attributable to process industries, 5% was attributable to its environmental and infrastructure work, and 1% was attributable to other industries. See "—Backlog" and "—Risk Factors."

Recent Acquisitions

Stone & Webster Acquisition On July 14, 2000, the Company purchased substantially all of the operating assets of Stone & Webster pursuant to a Chapter 11 bankruptcy proceeding for Stone & Webster. The purchase price included the following: (i) \$14.9 million in cash (net of \$22.8 million of funds returned from escrow), (ii) 4,463,546 shares of its no par value Common Stock ("Common Stock") (valued at approximately \$105 million at closing), and (iii) the assumption of approximately \$740 million of liabilities. For further information regarding the assumed liabilities, see Note 3 of Notes to Consolidated Financial Statements. The Company also incurred approximately \$12 million of acquisition costs. Stone & Webster is a leading global provider of engineering, procurement, construction, consulting and environmental services to the power, process, environmental and infrastructure markets. Stone & Webster was formed in 1889 and has focused on the power generation industry for most of its existence. Stone & Webster's capabilities complement and enhance Shaw's traditional strengths in project execution and pipe fabrication and enable the Company to deliver a more complete, cost-effective package of products and services to its power and process customers. Goodwill of approximately \$351 million was recorded for this acquisition, and for the years ended August 31, 2001 and 2000, this goodwill was amortized on a straight-line basis based on a 20-year estimated life. See Note 1 of Notes to Consolidated Financial Statements with respect to the impact of the Company's adoption of SFAS No. 142—"Goodwill and Other Intangibles" in fiscal 2002. This acquisition has more than doubled the size of the Company, increasing significantly the Company's engineering, procurement and construction businesses, and has significantly impacted operations and working capital requirements.

Other Acquisitions In March 2001, the Company acquired the assets and certain liabilities of Scott, Sevin & Schaffer, Inc. and Technicomp, Inc. (collectively "SS&S"). As of August 31, 2001, the Company had issued 170,683 shares (including purchase price protection reduced by purchase price adjustment settlements) of its Common Stock (valued at approximately \$6.3 million) as consideration for the transaction and 13,800 of the issued shares were escrowed to secure certain indemnities provided by the seller. The Company also incurred approximately \$0.2 million of acquisition costs. This acquisition was completed on March 23, 2001, and was accounted for under the purchase method of accounting. Approximately \$4.3 million of goodwill was recorded with respect to this acquisition. For the year ended August 31, 2001, goodwill for this acquisition was amortized on a straight-line basis based on a 20-year estimated life. See Note 1 of Notes to Consolidated Financial Statements with respect to the impact of the Company's adoption of SFAS No. 142—"Goodwill and Other Intangibles" in fiscal 2002. SS&S's primary business is structural steel, vessel and tank fabrication. The operating results of SS&S have been included in the Consolidated Statements of Income from the date of acquisition.

On July 12, 2000, the Company completed the acquisition of certain assets and liabilities of PPM Contractors, Inc. ("PPM"). Total consideration included 86,890 shares of the Company's Common Stock valued at approximately \$2 million at the closing and the assumption of certain liabilities. Acquisition costs were not material. The purchase method was used to account for the acquisition. Goodwill was approximately \$2.1 million with respect to this acquisition. For the years ended August 31, 2001 and 2000, goodwill for this acquisition was amortized on a straight-line basis based on a 20-year estimated life. See Note 1 of Notes to Consolidated Financial Statements with respect to the impact of the Company's adoption of SFAS No. 142—"Goodwill and Other Intangibles" in fiscal 2002. PPM's primary business is providing sandblasting and painting services to industrial customers. The operating results of PPM have been included in the Consolidated Statements of Income from the date of acquisition.

See Note 3 of Notes to Consolidated Financial Statements for further discussion regarding these acquisitions.

Historically, the Company has used acquisitions to pursue market opportunities and to augment or increase existing capabilities and plans to continue to do so. Any of the following comments concerning the Company's expectations for future sales and operating results are based on the Company's forecasts for its existing operations.

Results of Operations

The following table presents certain income and expense items as a percentage of sales for the years ended August 31, 2001, 2000 and 1999:

	For the Years Ended August 31,		
	2001	2000	1999
Sales	100.0%	100.0%	100.0%
Cost of sales	84.0	83.3	81.0
Gross profit	16.0	16.7	19.0
General and administrative expenses	9.1	9.8	12.2
Operating income	6.9	6.9	6.8
Interest expense	(1.0)	(1.0)	(1.8)
Other income, net	0.6	0.1	0.3
Income before income taxes	6.5	6.0	5.3
Provision for income taxes	2.5	2.2	1.8
Income before earnings (losses) from unconsolidated entities, net of taxes	4.0	3.8	3.5
Earnings (losses) from unconsolidated entities, net of taxes	—	0.2	0.2
Income before extraordinary item and cumulative effect of change in accounting principle	4.0	4.0	3.7
Extraordinary item for early extinguishment of debt, net of taxes	—	(0.1)	—
Cumulative effect on prior years of change in accounting for start-up costs, net of taxes	—	—	—
Net income	4.0%	3.9%	3.7%

Fiscal 2001 Compared to Fiscal 2000 Revenues increased 102% to \$1,538.9 million in fiscal 2001 from \$762.7 million in fiscal 2000. Revenues from both of the Company's business segments increased in fiscal year 2001, when compared to fiscal 2000, with the integrated EPC services segment increasing by \$761.1 million or 108% over the prior fiscal year. This revenue increase was attributable to revenue from Stone & Webster businesses, which were acquired in July 2000 (see Note 3 of Notes to Consolidated Financial Statements). Revenues from the manufacturing and distribution segment increased \$15.1 million, or 25%, from fiscal 2000 levels to \$76.1 million for fiscal 2001. Gross profit increased 94% to \$246.6 million in fiscal 2001 from \$127.1 million in fiscal 2000 due to increased revenues.

The Company's sales to customers in the following geographic regions approximated the following amounts and percentages:

Geographic Region	Fiscal 2001		Fiscal 2000	
	(in millions)	%	(in millions)	%
United States	\$1,285.4	83.5%	\$591.8	77.6%
Asia/Pacific Rim	117.1	7.6	51.0	6.7
Europe	86.4	5.6	65.2	8.5
Other	23.9	1.6	20.5	2.7
South America	23.1	1.5	29.8	3.9
Middle East	3.0	0.2	4.4	0.6
	\$1,538.9	100.0%	\$762.7	100.0%

Revenues from domestic projects increased \$693.6 million, or 117%, from \$591.8 million for fiscal 2000 to \$1,285.4 million for fiscal 2001. The power generation market continues to be robust in the U.S., accounting for approximately \$550.1 million (79%) of the increase in domestic sales for fiscal 2001. These increases were made possible primarily by the Stone & Webster acquisition. Further, as a result of the acquisition of Stone & Webster, the Company now conducts business in the environmental and infrastructure industry sector. Domestic sales to this industry sector increased by \$163.4 million for the year ended August 31, 2001. The increases in the domestic power generation and environmental and infrastructure domestic sectors were partially offset by decreases in domestic process work. Domestic process industries sector sales decreased \$52.8 million primarily due to decreases of sales to the refining industry. The Company's domestic power generation customers continue to express interest in new orders for gas power plants and also for coal and nuclear projects. No significant increases are expected in the process markets in fiscal 2002 due to reduced capital expenditures by the Company's customers in these markets.

Sales for international projects increased \$82.6 million, or 48%, to \$253.5 million from fiscal 2000 to fiscal 2001. Sales in the Asia/Pacific Rim Region and Europe increased from prior year's levels primarily due to work performed by the acquired Stone & Webster businesses. Additionally, in fiscal 2001, the Company finalized an agreement for the construction of a 600,000 metric tons-per-year ethylene plant in China, which will significantly impact sales in this area through fiscal 2004. Even though sales for South America and the Middle East regions have remained sluggish, the Company continues to believe that these markets present long-term opportunities to the Company.

The Company's sales to customers in the following industries approximated the following amounts and percentages:

Industry Sector	Fiscal 2001		Fiscal 2000	
	(in millions)	%	(in millions)	%
Power Generation	\$ 915.7	59.5%	\$329.8	43.2%
Process Industries	305.5	19.9	324.0	42.5
Environmental and Infrastructure	186.2	12.1	22.8	3.0
Other Industries	131.5	8.5	86.1	11.3
	\$1,538.9	100.0%	\$762.7	100.0%

Revenues from both domestic and international power generation projects increased by a total of \$585.9 million in fiscal 2001 from fiscal 2000. Demand in the United States for power generation projects remained high, and was responsible for 94% of the power generation revenue increase. The acquisition of Stone & Webster has enabled the Company to capitalize on the increase in demand to construct power generation plants. The decrease in process industries sales in fiscal 2001 from fiscal 2000 resulted primarily from reductions in domestic refining work. Additionally, the Stone & Webster acquisition resulted in the addition of the environmental and infrastructure industry sector to the Company's capabilities.

Gross profit increased 94%, or \$119.5 million, to \$246.6 million in fiscal 2001 from \$127.1 million in fiscal 2000 due to the growth in revenue volume during the year. The Company's gross profit in fiscal 2001 was increased (cost of sales decreased) by approximately \$99.3 million by the utilization of reserves which were established to record the fair value of (primarily) fixed-price contracts acquired in the Stone & Webster acquisition (see Note 3 of Notes to Consolidated Financial Statements).

In fiscal 2001, the Company increased the gross margin reserve and its reserve for contract losses for contracts acquired from Stone & Webster by \$38.1 million and \$5.4 million, respectively. These increases were made to finalize the Company's purchase accounting fair value assessment of the related acquired contracts in progress and primarily reflected a customer's decision to recommence a large foreign nuclear project which had been suspended and to adjust the reserves of certain other contracts based on a current evaluation of their status as of the acquisition date. These reserve adjustments increased goodwill recorded for the acquisition.

The gross profit margin percentage for the year ended August 31, 2001 decreased to 16.0% from 16.7% from the prior year. The Company is involved in numerous projects, and, as a result, the Company's consolidated gross profit margin can be affected by many factors. These include matters, such as product mix (e.g., engineering and consulting versus construction and procurement), pricing strategies, foreign versus domestic work (profit margins differ, sometimes substantially, depending on the location of the work) and adjustments to project profit estimates during the project term.

During fiscal 2001, Stone & Webster's operating results were included in the Company's consolidated financial statements for the entire year as compared to only one and one-half months in fiscal 2000. EPC contracts, such as those that Stone & Webster worked on during fiscal 2001, typically have lower gross profit margin percentages than the Company's historical gross profit margin percentages. These contracts were a contributing factor to the lower gross profit margin percentage in fiscal 2001 as compared with fiscal 2000.

Additionally, during fiscal 2001, as compared with prior periods, the Company entered into more cost reimbursable contracts as opposed to fixed-price projects. Cost reimbursable contracts generally allow the Company to recover any cost overruns. Accordingly, cost reimbursable contracts are frequently priced with lower gross margins than fixed-price contracts, because fixed-priced contracts are usually bid with higher margins to compensate for cost overrun risks. The Company expects that a substantial portion of its work in fiscal 2002 and fiscal 2003 will be performed pursuant to cost reimbursable contracts.

The Company expects that gross profit margin percentages will be lower in fiscal 2002, compared with fiscal 2001, due, in large part, to the following factors: (a) increase in engineering, procurement and construction work, which carries lower margin percentages than pipe fabrication work; (b) additional EPC contracts requiring the procurement of large pieces of equipment; and (c) increase in the amount of work to be performed pursuant to cost reimbursable contracts, which contracts generally carry lower margins than fixed-price contracts (such as some of the contracts assumed in the Stone & Webster acquisition).

In fiscal 2001, general and administrative expenses, which include goodwill amortization, increased to \$139.7 million from \$74.3 million in fiscal 2000. The increase in fiscal 2001 general and administrative expenses resulted primarily from (i) expenses associated with the Stone & Webster businesses and (ii) an approximate \$15.8 million increase in goodwill amortization, also resulting primarily from the Stone & Webster acquisition. However, as a result of economies realized with the integration of Stone & Webster into Shaw, general and administrative expenses in fiscal 2001 decreased as a percentage of sales to 9.1% from 9.8% compared with fiscal 2000. The Company expects general and administrative expenses, excluding goodwill amortization, to increase in fiscal 2002, but at a substantially lesser rate than its percentage growth in revenues. Additionally, the Company adopted SFAS No. 142 ("Goodwill and Other Intangible Assets") effective at September 1, 2001 (see Note 1 of Notes to the Consolidated Financial Statements), and will cease amortizing goodwill for fiscal 2002 and future periods as required by this new accounting standard. The Company's goodwill amortization for fiscal 2001 was approximately \$18.9 million.

In May 2001, the Company realized approximately \$490 million net proceeds (after offering expenses) from the issuance and sale of \$790 million of 20-year, zero-coupon, unsecured, convertible debt Liquid Yield Option™ Notes (the "LYONs") due 2021. The LYONs were issued on an original discount basis of \$639.23 per LYON, providing the holders with a yield-to-maturity of 2.25% (see Note 7 of Notes to Consolidated Financial Statements). The Company used these proceeds to retire the majority of its outstanding borrowings and to invest surplus funds in investments with yields higher than the interest on the debt. Interest expense for the year increased to \$15.7 million from \$8.0 million in fiscal year 2000. This increase was largely attributable to higher borrowing levels and higher interest rates on the Company's primary revolving line of credit facility during fiscal 2001 prior to the sale of the LYONs in May 2001. Interest expense was favorably impacted in fiscal 2001 and 2000 by excluding approximately \$2.4 million and \$1 million, respectively, of interest expense attributable to the operations of a cold storage operation reported as an asset held for sale. The Company's interest expense for fiscal 2001, and for future periods, includes the amortization of loan origination costs for both its revolving credit facility and its LYONs debt, and therefore, its reported interest expense is and will be higher than expected, based on its borrowing levels.

Other income was \$8.6 million for fiscal 2001 compared with \$0.8 million for fiscal 2000. This increase is primarily attributable to interest income realized from investments in high quality, short-term debt instruments. The funds for these investments were primarily provided from the net proceeds (after retiring other outstanding debt) from the sale of the Company's convertible debt instruments in May 2001 (see Note 7 of Notes to Consolidated Financial Statements). During fiscal 2001, the yields from these investments were greater than the interest costs associated with the convertible debt.

The Company's interest expense will increase in fiscal 2002 from fiscal 2001 as a result of having convertible debt outstanding for the full fiscal year. Interest income should increase in fiscal 2002 over fiscal 2001 levels due to the Company's investment of a substantial portion of the funds received from the sale of its convertible debt. However, the Company anticipates that, based on its current cash flow and yield projections, interest income will be less than its interest expense in fiscal 2002.

The Company's effective tax rates for the years ended August 31, 2001 and 2000 were 38.4% and 35.9%, respectively. The Company's tax rates for each period during each year represent the Company's estimate of its effective tax rates for each entire year based primarily on the Company's estimate of pretax income for the year and the mix of domestic and foreign sourced (including foreign export sales) income. The Company updates its effective tax rate each quarter based on actual results to date and revised budgeted amounts for the remainder of the year. The increase in the tax rates in fiscal 2001 versus fiscal 2000 is due primarily to the increase in domestic sales and an increase in nondeductible expenses, such as a portion of the goodwill recognized from the Stone & Webster acquisition. However, because the Company has adopted SFAS No. 142 in fiscal 2002 (see Note 1 of Notes to Consolidated Financial Statements), it will cease to amortize goodwill. Accordingly, the Company anticipates that its effective tax rate will decrease in fiscal 2002 because it will no longer recognize goodwill amortization expense (which is only partially deductible for tax purposes) in its financial statements. This decrease is expected to be partially offset by increased domestic income in fiscal 2002 that has a higher tax rate than most foreign income.

Fiscal 2000 Compared to Fiscal 1999 Revenues increased 54.4% to \$762.7 million in fiscal 2000 from \$494.0 million in fiscal 1999. Fiscal 2000 revenues from both of the Company's business segments increased from fiscal 1999 levels with the integrated EPC services (formerly named pipe services) segment reflecting a \$255.0 million increase or 57%. Approximately \$111 million of the revenue increase was provided from the newly acquired Stone & Webster businesses (see Note 3 of Notes to Consolidated Financial Statements). Revenues in fiscal 2000 from the manufacturing and distribution segment increased \$13.6 million or a 29% increase over prior year levels. Gross profit increased 35.4% to \$127.1 million in fiscal 2000 from \$93.8 million in fiscal 1999 due to the growth in revenue volume during the year.

The Company's sales to customers in the following geographic regions approximated the following amounts and percentages:

Geographic Region	Fiscal 2000		Fiscal 1999	
	(in millions)	%	(in millions)	%
United States	\$591.8	77.6%	\$366.2	74.1%
Europe	65.2	8.5	49.7	10.1
Asia/Pacific Rim	51.0	6.7	41.1	8.3
South America	29.8	3.9	18.7	3.8
Other	20.5	2.7	8.1	1.6
Middle East	4.4	0.6	10.2	2.1
	\$762.7	100.0%	\$494.0	100.0%

Revenues from domestic projects increased \$225.6 million, or 62%, from \$366.2 million for fiscal 1999 to \$591.8 million for fiscal 2000. Increases were experienced in all domestic industry sectors, with power generation sales accounting for the majority of the increase. Revenues from international projects increased \$43.1 million, or 34%, from \$127.8 million for fiscal 1999 to \$170.9 million for fiscal 2000. All international industry sectors reflected sales increases over fiscal 1999 amounts, with the primary increases being in crude oil refining revenues (part of the process industries sector) and the power generation sector. For the year ended August 31, 2000, virtually all European sector sales were to the United Kingdom. Sales increased in the Asia/Pacific Rim region due to work performed by the acquired Stone & Webster businesses. Additionally, in August 2000, the Company executed a letter of intent for the construction of a 600,000 metric tons-per-year ethylene plant in China.

The Company's sales to customers in the following industries approximated the following amounts and percentages:

Industry Sector	Fiscal 2000		Fiscal 1999	
	(in millions)	%	(in millions)	%
Power Generation	\$329.8	43.2%	\$161.8	32.8%
Process Industries	324.0	42.5	271.1	54.9
Other Industries	86.1	11.3	61.1	12.3
Environmental and Infrastructure	22.8	3.0	—	—
	\$762.7	100.0%	\$494.0	100.0%

Process industries sector sales include revenues from the chemical and petrochemical and crude oil refining industries, which in prior years were reported separately. Other industries sales include revenues from the oil and gas exploration and production industry, which in prior years was reported separately.

Revenues from power generation projects increased both domestically and internationally. Sales related to domestic power projects increased due to additional work performed for United States customers, including a \$300 million, five-year contract with a major manufacturer of gas turbines. International power generation revenue increases resulted from work performed by the newly acquired Stone & Webster businesses. Process industries sector sales also increased both domestically and internationally over 1999 revenues, principally due to sales to the crude oil refining industry. Environmental and infrastructure sales were primarily domestic and were generated by the newly acquired Stone & Webster businesses.

The gross profit margin for the year ended August 31, 2000, decreased to 16.7% from 19.0% for the same period the prior year. The Company is involved in numerous projects, all of which affect gross profit in various ways, such as product mix, pricing strategies, foreign versus domestic work (profit margins differ, sometimes substantially, depending on where the work is performed), and constant monitoring of percentage of completion calculations. The Company's gross profit margin has been declining due to the Company's increase in revenues related to its erection and maintenance services and the inclusion of Stone & Webster's procurement and construction activities, which generally carry lower margins than fabrication work.

General and administrative expenses were \$74.3 million for fiscal 2000, up 24% from \$60.1 million for fiscal 1999. Approximately \$5.3 million of the increase resulted from Stone & Webster activity since the acquisition. The remaining increase resulted primarily from higher sales levels and other normal business expenses. As a percentage of sales, however, general and administrative expenses decreased to 9.8% for the year ended August 31, 2000 from 12.2% for the year ended August 31, 1999.

Interest expense for the year ended August 31, 2000 was \$8.0 million, compared to \$8.6 million for the prior fiscal year. Interest expense varies from year to year due to the level of borrowings and interest rate fluctuations on variable rate loans. Prior to the Stone & Webster acquisition and a new primary credit facility obtained in July 2000 (see Note 8 of Notes to Consolidated Financial Statements), interest expense on the Company's previous line of credit had decreased approximately \$1.3 million in fiscal year 2000, compared to the same period in fiscal 1999, due to lower borrowings partially offset by higher interest rates. Borrowings after the Stone & Webster acquisition on the new credit facility added approximately \$1.1 million of additional interest costs in fiscal 2000. The remaining \$0.4 million decrease relates to paydowns of debt, offset by interest on assumed Stone & Webster debt.

The Company's effective tax rates for the years ended August 31, 2000 and 1999 were 35.9% and 33.1%, respectively. The increase in the tax rates was primarily a result of the change in the mix of foreign (including foreign export sales) versus domestic work.

Liquidity and Capital Resources

Net cash provided by operations was \$11.4 million in fiscal 2001, compared to net cash used in operations of \$69.9 million in fiscal 2000. For fiscal 2001, net cash provided by operations was favorably impacted primarily by: (i) net income of \$61 million, (ii) an increase in advanced billings and billings in excess of cost and estimated earnings on uncompleted contracts of \$66.8 million, (iii) depreciation and amortization of \$39.7 million, and (iv) deferred taxes of \$37.7 million. Offsetting these positive influences were decreases of \$62.9 million in accrued liabilities, \$42.4 million in accounts payable, and \$99.3 million in accrued contract losses and reserves.

The increase in advanced billings and billings in excess of cost and estimated earnings on uncompleted contracts resulted from accelerated or advanced billing provisions in more contracts, increased revenue and construction activity. The increase in depreciation and amortization over fiscal 2000 levels resulted primarily from the amortization of goodwill and other intangibles related to the Stone & Webster acquisition. The increase in deferred taxes over fiscal 2000 levels was substantially attributable to timing differences for certain assumed obligations associated with the Stone & Webster acquisition. The decreases in accrued liabilities and accounts payable were primarily the result of payment of liabilities assumed in the Stone & Webster acquisition.

Additionally, the Company acquired a large number of contracts in the Stone & Webster acquisition with either inherent losses or lower than market rate margins due to the effect of the financial difficulties experienced by Stone & Webster on negotiating and executing contracts prior to the acquisition. These contracts were adjusted to their fair value at acquisition date by establishing a gross margin reserve that reduces costs of sales for contracts as they are completed. Costs of sales was reduced by approximately \$70.1 million during fiscal 2001 through the utilization of this reserve, which is a non-cash component of income. Costs of sales was also reduced by approximately \$29.2 million due to the utilization of the reserve which represents net cash losses on contracts acquired in the Stone & Webster acquisition. The utilization of these reserves resulted in a corresponding increase in gross profit during fiscal 2001. See Note 3 of Notes to Consolidated Financial Statements.

Net cash provided by investing activities was \$54.3 million in fiscal 2001, compared with net cash used in investing activities of \$15.8 million for fiscal 2000. Asset sales provided approximately \$120.9 million in net cash, comprised primarily of proceeds from the sale of assets acquired in the Stone & Webster acquisition for \$112.5 million, and the sale of other property and equipment for \$8.4 million. Additionally, \$22.8 million of escrow funds that had been deposited as retainer for the Stone & Webster acquisition in fiscal 2000 were returned to the Company. The Company invested approximately \$45.6 million of the proceeds received from the sale of its LYONs in high quality short-term marketable debt securities being held to maturity. The Company purchased \$38.1 million of property and equipment during fiscal 2001, an increase of approximately \$15 million to \$20 million over the Company's historical levels; this increase was largely attributable to upgrading various corporate information systems which have assisted in the integration of the Stone & Webster acquisition. During fiscal 2001, the Company also invested approximately \$2 million in its EntergyShaw joint venture, \$1.9 million in an unconsolidated cold storage and frozen food handling operation and made additional advances of \$0.3 million to its Shaw Nass joint venture (see Note 5 of Notes to Consolidated Financial Statements). The Company also made an investment of \$1.2 million in securities held for sale and paid \$0.2 million of acquisition costs related to the acquisition of the assets of Scott, Sevin & Schaffer, Inc. and Technicomp, Inc. (see Note 3 of Notes to Consolidated Financial Statements).

Net cash provided by financing activities totaled approximately \$356.7 million for the fiscal year ended August 31, 2001, as compared with \$101.2 million in the prior year. On May 1, 2001, the Company realized net proceeds (after offering expenses) of approximately \$490 million from the sale of \$790 million face value LYONs debt (see Note 7 of Notes to Consolidated Financial Statements). Approximately \$67 million of the proceeds from the sale of the LYONs were used to pay off existing debt, including approximately \$58 million on the Company's primary credit facility ("Credit Facility"). The remaining amount of approximately \$423 million was invested in short-term, high quality cash equivalents and debt securities all with maturities of less than four months. The Company also had other normal course of business borrowings of approximately \$3 million.

The holders of the LYONs have the right to require the Company to repurchase the debt on the third, fifth, tenth, and fifteenth anniversaries at the accreted value. The Company has the right to fund such repurchases with shares of its Common Stock, cash, or a combination of Common Stock and cash. The LYONs holders also have the right to require the Company to repurchase the debt for cash, at the accreted value, if there is a change in control of the Company, as defined, occurring on or before May 1, 2006. The Company may redeem all or a portion of the LYONs at the accreted value, through cash payments, at any time after May 1, 2006.

In October 2000, the Company completed the sale of 4,837,338 shares (including 1,200,000 shares for over-allotments) of its Common Stock, no par value per share (the "Common Stock"), in an underwritten public offering at a price of \$31.75 per share, less underwriting discounts and commissions. The net proceeds to the Company, less underwriting discounts and commissions and other offering expenses, totaled approximately \$144.8 million. The Company also received approximately \$3.3 million from employees upon the exercise of stock options during fiscal 2001. In fiscal 2000, the Company realized approximately \$69.7 million in proceeds from the sale of its Common Stock.

During the course of fiscal 2001, the Company utilized the funds obtained from the sales of the Company's Common Stock, LYONs and assets acquired in the Stone & Webster acquisition to pay off the Credit Facility, which had a balance of approximately \$235 million as of August 31, 2001. Although the Company had no borrowings outstanding under the Credit Facility as of August 31, 2001, the Credit Facility is still fully available to the Company. As of August 31, 2001, the Credit Facility was being used to provide letters of credit of approximately \$61.5 million to satisfy various project guarantee requirements (see Note 8 of Notes to Consolidated Financial Statements). The Company has also used this Credit Facility to provide working capital and to fund fixed asset purchases and subsidiary acquisitions, including the acquisition of substantially all of the operating assets of Stone & Webster and continues to be available for these purposes.

In fiscal 2001, the Company's repayment of debt and leases of \$49.2 million (excluding payments on the Company's Credit Facility balances) included \$23.9 million related to the sale of certain Stone & Webster assets and the Company's corporate headquarters office building in Baton Rouge, Louisiana; \$23.3 million of other debt and leases (most of which were secured by facilities or equipment); and the prepayment of a \$2 million debt related to the acquisition of a subsidiary in 1998, which resulted in an extraordinary loss after taxes of approximately \$0.2 million.

On August 30, 2000, the Company and Entergy Corporation ("Entergy") formed EntergyShaw, L.L.C. ("EntergyShaw"), an equally-owned and equally-managed company (see Note 5 of Notes to Consolidated Financial Statements). During fiscal 2001, the Company invested \$2 million in EntergyShaw, as required under the terms of the agreement with EntergyShaw. The Company does not believe that work performed for EntergyShaw will require a significant working capital investment due to the terms of its agreement with EntergyShaw. At August 31, 2001, EntergyShaw had begun construction on two projects for Entergy, involving a total of six turbines.

The Company's primary credit facility is a three-year term, \$300 million credit facility ("Credit Facility") dated July 14, 2000 that permits both revolving credit loans and letters of credit, which letters of credit cannot exceed an aggregate of \$150 million. The Company has the option to increase the Credit Facility under existing terms to \$400 million, if certain conditions are satisfied, including the successful solicitation of additional lenders or increased participation of existing lenders. The Credit Facility allows the Company to borrow at interest rates in a range of 1.50% to 2.75% over the London Interbank Offered Rate ("LIBOR") or from the prime rate to 1.25% over the prime rate. The Company selects the interest rate index and the spread over the index is dependent upon certain financial ratios of the Company. The Credit Facility is secured by, among other things: (i) guarantees by the Company's domestic subsidiaries; (ii) a pledge of all of the capital stock in the Company's domestic subsidiaries and 66% of the capital stock in certain of the Company's foreign subsidiaries; and (iii) a security interest in all property of the Company and its domestic subsidiaries (except real estate and equipment). The Credit Facility also contains restrictive covenants, including ratios, minimum capital levels, limits on other borrowings and other restrictions. As of August 31, 2001, the Company was in compliance with these covenants or had obtained the necessary waivers, had no outstanding revolving credit loans, and had letters of credit of approximately \$61.5 million outstanding under the Credit Facility. The Company's total availability under the Credit Facility at August 31, 2001, was approximately \$238.5 million, which includes availability for additional letters of credit of approximately \$88.5 million.

In September 2001, the Company announced that its Board of Directors had authorized the Company to repurchase shares of its Common Stock, depending on market conditions, up to a limit of \$100 million. As of November 19, 2001, the Company had purchased a total of 333,000 shares at a cost of approximately \$10.1 million.

The Company's working capital balance was approximately \$521 million at August 31, 2001. The Company's future requirements for working capital are likely to fluctuate due to such factors as the timing and negotiated payment terms of its projects. The Company believes that its working capital position and its availability of funds under its Credit Facility are sufficient to fund the working capital needs of its business, its fixed asset expenditures and its normal operations for the next twelve months.

Backlog

The Company defines its backlog as a "working backlog" that includes projects for which Shaw has received a commitment from its customers. This commitment typically takes the form of a written contract for a specific project, a purchase order, or a specific indication of the amount of time or material the Company needs to make available for a customer's anticipated project. In certain instances the engagement is for a particular product or project for which the Company estimates anticipated revenue, often based on engineering and design specifications that have not been finalized and may be revised over time. Shaw's backlog for maintenance work is derived from maintenance contracts and Shaw's customers' historic maintenance requirements. The Company estimates that its backlog was approximately \$4.5 billion at August 31, 2001. The Company estimates that approximately 42% of its backlog at August 31, 2001 will be completed in fiscal 2002.

The following table breaks out the Company's backlog in the following industry sectors and geographic regions for the periods indicated.

	At August 31,			
	Fiscal 2001		Fiscal 2000	
	(in millions)	%	(in millions)	%
Industry Sector				
Power Generation	\$3,540.1	79%	\$1,276.3	67%
Process Industries	666.4	15	335.5	18
Environmental and Infrastructure	231.9	5	253.9	13
Other Industries	58.8	1	47.9	2
	\$4,497.2	100%	\$1,913.6	100%
Geographic Region				
Domestic	\$3,743.0	83%	\$1,527.4	80%
International	754.2	17	386.2	20
	\$4,497.2	100%	\$1,913.6	100%

The Company's backlog is largely a reflection of the broader economic trends being experienced by its customers and is important to Shaw in anticipating its operational needs. Backlog is not a measure defined in generally accepted accounting principles and the Company's backlog may not be comparable to backlog of other companies. The Company cannot provide any assurance that revenues projected in its backlog will be realized, or if realized, will result in profits.

Effects of Inflation

The Company has determined it will focus its operations on cost-reimbursable or negotiated lump-sum contracts. To the extent that a significant portion of the Company's revenues are earned under cost-reimbursable type contracts, the effects of inflation on the Company's financial condition and results of operations should generally be low. However, if the Company expands its business into markets and geographical areas where fixed-price and lump-sum work is more prevalent, inflation may begin to have a larger impact on the Company's results of operations. To the extent permitted by competition, the Company intends to continue to emphasize contracts which are either cost-reimbursable or negotiated fixed-price. For contracts the Company accepts with fixed-price or lump-sum terms, the Company monitors closely the actual costs on the project as they compare to the budget estimates. On these projects, the Company also attempts to secure fixed-price commitments from key subcontractors and vendors. However, due to the competitive nature of the Company's industry, combined with the fluctuating demands and prices associated with personnel, equipment and materials the Company traditionally needs in order to perform on its contracts, there can be no guarantee that inflation will not affect the Company's results of operations in the future.

Recent Accounting Pronouncements

In early 1998, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position 98-5, "Reporting on the Costs of Start-Up Activities" ("SOP"). The SOP is effective for fiscal years beginning after December 15, 1998, and requires costs of start-up activities and organization costs to be expensed as incurred. Any such unamortized costs on the date of adoption of this SOP were to be written off and reflected as a cumulative effect of a change in accounting principle. The Company adopted this new SOP in fiscal 2000, and in accordance therewith, on September 1, 1999, the Company wrote off deferred organizational costs of approximately \$0.3 million, net of taxes.

In fiscal 2000, the Securities and Exchange Commission issued Staff Accounting Bulletin No. 101 which establishes guidance in applying generally accepted accounting principles to revenue recognition in financial statements and is effective for fiscal 2001. The Company has determined that its existing revenue recognition practices comply with the guidance in the bulletin.

Effective September 1, 2000, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 133—"Accounting for Derivative Instruments and Hedging Activities" which requires that all derivative instruments be recorded on the balance sheet at fair value. On the date derivative contracts are executed, the Company designates the derivative as one of the following: (i) the hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment (fair value hedge), (ii) the hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge), or (iii) the hedge of a net investment in a foreign operation (net investment hedge).

Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income, depending on whether the derivative is designated as part of a hedge transaction and, if it is, depending on the type of hedge transaction. For fair value hedge transactions, changes in fair value of the derivative instrument are generally offset in the income statement by changes in the fair value of the item being hedged. For cash flow hedge transactions, changes in the fair value of the derivative instrument are reported in other comprehensive income. For net investment hedge transactions, changes in the fair value are recorded as a component of the foreign currency translation account that is also included in other comprehensive income. The gains and losses on cash flow hedge transactions that are reported in other comprehensive income are reclassified to earnings in the periods in which earnings are affected by the variability of the cash flows of the hedged item. The ineffective portions of all hedges are recognized in current period earnings.

The Company utilizes forward foreign exchange contracts to reduce its risk from foreign currency price fluctuations related to firm and anticipated commitments to purchase or sell equipment, materials and/or services. These investments are designated as cash flow hedging instruments. The Company normally does not use any other type of derivative instrument or participate in any other hedging activities.

Upon initial application of SFAS No. 133, the Company recorded the fair value of the existing hedge contracts on the balance sheet and a corresponding unrecognized loss of \$23,000 as a cumulative effect adjustment of accumulated other comprehensive income, which was transferred to earnings during fiscal 2001.

In July 2001, the Financial Accounting Standards Board (FASB) issued SFAS No. 141—"Business Combinations," and SFAS No. 142—"Goodwill and Other Intangible Assets." The standards significantly changed the Company's prior practices by: (i) terminating the use of the pooling-of-interests method of accounting for future business combinations, (ii) ceasing goodwill amortization, and (iii) requiring impairment testing of goodwill based on a fair value concept. SFAS No. 142 requires that impairment testing of the opening goodwill balances be performed within six months from the start of the fiscal year in which the standard is adopted and that any impairment be written off and reported as a cumulative effect of a change in accounting principle. It also requires that another impairment test be performed during the fiscal year of adoption of the standard and that impairment tests be performed at least annually thereafter, with interim testing required if circumstances warrant. The standards must be implemented for fiscal years beginning after December 31, 2001, but early adoption is permitted. The Company has decided to adopt the new standards for its fiscal year beginning September 1, 2001. Accordingly, the Company will cease to amortize goodwill in fiscal 2002. Goodwill amortization was approximately \$18.9 million, \$3.1 million and \$1.8 million for the years ended August 31, 2001, 2000 and 1999, respectively. The Company has not completed its initial evaluation of goodwill impairment that is required with the adoption of the SFAS No. 142. However, based on the preliminary evaluation procedures it has performed, the Company does not believe that its existing goodwill balances will be impaired under the new standards; however, no assurances can be given. The initial transition evaluation is required to be and will be completed by February 28, 2002 which is within the six month transition period allowed by the new standard upon adoption.

The FASB also recently issued SFAS No. 143, "Accounting for Asset Retirement Obligations." This statement, which is first effective in 2003, covers the accounting for closure or removal-type costs that are incurred with respect to long-lived assets. The nature of the Company's business and long-lived assets is such that adoption of this new standard should have no significant impact on the Company's financial position or results of operations.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which supersedes SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of." The new statement also supersedes certain aspects of APB 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," with regard to reporting the effects of a disposal of a segment of a business and will require expected future operating losses from discontinued operations to be reported in discontinued operations in the period incurred rather than as of the measurement date as presently required by APB 30. Additionally, certain dispositions may now qualify for discontinued operations treatment. The provisions of the statement are required to be applied for fiscal years beginning after December 15, 2001 and interim periods within those fiscal years. The Company has not yet determined what effect this statement will have on its financial statements.

Risk Factors

Investing in the Company's Common Stock will provide an investor with an equity ownership interest in the Company. Shareholders will be subject to risks inherent in the Company's business. The performance of Shaw's shares will reflect the performance of the Company's business relative to, among other things, general economic and industry conditions, market conditions and competition. The value of the investment in the Company may increase or decrease and could result in a loss. An investor should carefully consider the following factors as well as other information contained in this Annual Report before deciding to invest in shares of the Company's Common Stock.

This Annual Report also contains forward-looking statements that involve risks and uncertainties. The Company's actual results could differ materially from those anticipated in the forward-looking statements as a result of many factors, including the risk factors described below and the other factors described elsewhere in this Annual Report.

Demand for the Company's products and services is cyclical and vulnerable to downturns in the power generation and other industries to which the Company markets its products and services.

The demand for Shaw's products and services depends on the existence of engineering, construction and maintenance projects, particularly in the power generation industry which accounted for 79% of the Company's backlog as of August 31, 2001. The Company also depends, to a lesser extent, on conditions in the petrochemical, chemical, environmental, infrastructure and refining industries. These industries historically have been, and will likely continue to be, cyclical in nature and vulnerable to general downturns in the domestic and international economies. The Company's results of operations have varied and may continue to vary depending on the demand for future projects from these industries.

The dollar amount of the Company's backlog, as stated at any given time, is not necessarily indicative of its future earnings.

Shaw cannot provide assurance that the revenues projected in its backlog will be realized, or if realized, will result in profits. To the extent that Shaw experiences significant terminations, suspensions or adjustments in the scope of its projects as reflected in its backlog contracts, the Company could be materially adversely affected.

The Company defines its backlog as a “working backlog” which includes projects for which Shaw has received a commitment from its customers. This commitment may be in the form of a written contract for a specific project, a purchase order or an indication of the amount of time or material Shaw needs to make available for a customer’s anticipated project. In certain instances, the engagement is for a particular product or project for which Shaw estimates anticipated revenue, often based on engineering and design specifications that have not been finalized and may be revised over time. The Company’s backlog for maintenance work is derived from maintenance contracts and customers’ historic maintenance requirements.

The Company also includes in backlog commitments from certain individual customers who have committed to more than one significant EPC project and other customers who have committed to multi-year orders for piping or maintenance services. The Company cannot be assured that the customers will complete all of these projects or that the projects will be performed in the currently anticipated time-frame.

On occasion, customers will cancel or delay projects for reasons beyond the Company’s control. In the event of project cancellation, Shaw may be reimbursed for certain costs but typically has no contractual right to the total revenues reflected in the Company’s backlog. In addition, projects may remain in the Company’s backlog for extended periods of time. If Shaw were to experience significant cancellations or delays of projects in its backlog, the Company’s financial condition would be significantly adversely affected.

Difficulties integrating acquisitions could adversely affect Shaw. The Company has and may continue to acquire new businesses. As a result, the Company may encounter difficulties integrating acquisitions and successfully managing the growth the Company expects to experience from the acquisitions. To the extent the Company encounters problems in integrating one or more acquisitions, the Company could be materially adversely affected. The Company plans to pursue select acquisitions in the future. Because the Company may pursue acquisitions around the world and may actively pursue a number of opportunities simultaneously, the Company may encounter unforeseen expenses, complications and delays, including difficulties in employing sufficient staff and operational and management oversight.

The Company may not receive the economic benefits expected from EntergyShaw. On September 18, 2000, the Company executed a definitive agreement with Entergy Corporation (“Entergy”) governing the parties’ relationship with respect to EntergyShaw, the equally-owned and equally-managed company formed by the parties on August 30, 2000. Subsequent to the execution of the letter of intent relating to this joint venture on June 2, 2000, Entergy and FPL Group, Inc., the parent of Florida Power & Light, announced a merger, but on August 2, 2001, these parties announced that they were abandoning their merger plans. EntergyShaw’s initial focus is the construction of power plants in North America and Europe for Entergy’s unregulated wholesale operations relating to the installation of turbines that Entergy has previously ordered for these plants. While the Company believes that EntergyShaw will manage the construction of most of such power plants, the Company can provide no assurances regarding the number of future power plant construction projects that Entergy will actually commence, or the number of turbines (specifically those previously ordered by Entergy) that Entergy will actually dedicate to any such future projects. During fiscal 2001, EntergyShaw and the Company began work on two projects for Entergy which will have a total of six turbines. The Company expects to provide the engineering, procurement, construction and pipe fabrication services for substantially all of EntergyShaw’s power generation projects. Under the terms of the joint venture, the Company must offer EntergyShaw a right of first refusal on opportunities to provide fully bundled engineering, procurement and construction opportunities that it receives after December 31, 2000.

The nature of Shaw’s contracts could adversely affect the Company. Shaw enters into fixed-price, lump-sum or unit price contracts on a significant number of domestic piping contracts and substantially all international piping projects. In addition, a number of the contracts the Company assumed in the Stone & Webster acquisition were fixed-price or lump-sum contracts and the Company may continue to enter into these types of contracts in the future. Under fixed, maximum or unit price contracts, the Company agrees to perform the contract for a fixed-price, and as a result, benefits from costs savings, but is unable to recover any cost overruns. Under fixed-price incentive contracts, the Company shares with the customer any savings up to a negotiated or target ceiling. When costs exceed the negotiated ceiling price, the Company may be required to reduce its fee or to absorb some or all of the cost overruns. Contract prices are established based in part on cost estimates that are subject to a number of assumptions, including assumptions regarding future economic conditions. If these estimates prove inaccurate or circumstances change, cost overruns having a material adverse effect on the Company’s business and results of its operations could occur. Shaw’s profit for these projects could decrease or the Company could experience losses, if the Company is unable to secure fixed pricing commitments from its suppliers at the time the contracts are entered into or if the Company experiences cost increases for material or labor during the performance of the contracts.

Shaw enters into contractual agreements with customers for many of its engineering, procurement and construction services based on agreed upon reimbursable costs and labor rates. Some of these contracts provide for the customer's review of the Company's accounting and cost control systems to verify the completeness and accuracy of the reimbursable costs invoiced. These reviews could result in proposed reductions in reimbursable costs and labor rates previously billed to the customer.

In addition, the Company has several significant projects for agencies of the U.S. Government. Generally, U.S. Government contracts are subject to oversight audits by government representatives, profit and cost controls and limitations and provisions permitting modification or termination, in whole or in part, without prior notice, at the government's convenience and with payment of compensation only for work done and commitments made at the time of termination. In the event of termination, the Company generally receives some allowance for profit on the work performed. In some cases, government contracts are subject to the uncertainties surrounding congressional appropriations or agency funding. Government contracts are subject to specific procurement regulations and a variety of socio-economic and other requirements. Failure to comply with such regulations and requirements could lead to suspension or debarment, for cause, from future government contracting or subcontracting for a period of time. Among the causes for debarment are violations of various statutes, including those related to employment practices, the protection of the environment, the accuracy of records and the recording of costs.

Actual results could differ from the estimates and assumptions used to prepare the Company's financial statements.

In order to prepare financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions as of the date of the financial statements which affect the reported values of assets and liabilities and revenues and expenses, and disclosures of contingent assets and liabilities. Areas requiring significant estimates by the Company's management, include (i) contract expenses and profits and application of percentage of completion accounting; (ii) recoverability of inventory and application of lower of cost or market accounting; (iii) provisions for uncollectable receivables and customer claims; (iv) provisions for income taxes and related valuation allowances; (v) recoverability of net goodwill; (vi) recoverability of other intangibles and related amortization; and (vii) accruals for estimated liabilities, including litigation and insurance reserves. Actual results could differ from those estimates.

The Company's results of operations depend on Shaw's ability to obtain future contracts. In the case of large-scale domestic and international projects where timing is often uncertain, it is particularly difficult to predict whether and when Shaw will receive a contract award. In addition, timing of receipt of revenues from the Company's projects can be affected by a number of factors beyond the Company's control, including unavoidable delays from weather conditions, unavailability of material and equipment from vendors, changes in the scope of services requested by clients, or labor disruptions. The uncertainty of the Company's contract award timing can also present difficulties in matching workforce size with contract needs. In some cases, Shaw maintains and bears the cost of a ready workforce that is larger than called for under existing contracts in anticipation of future workforce needs under expected contract awards. If an expected contract award is delayed or not received, the Company would incur costs that could have a material adverse effect on it.

Projects in the industries in which the Company provides products and services frequently involve a lengthy and complex bidding and selection process. Because a significant portion of the Company's sales are generated from large projects, the Company's results of operations can fluctuate from quarter to quarter. Shaw's significant customers vary between years. The loss of any one or more of the Company's key customers could have a material adverse impact on it.

Political and economic conditions in foreign countries in which Shaw operates could adversely affect the Company.

A significant portion of the Company's sales is attributable to projects in international markets. Shaw expects international sales and operations to continue to contribute materially to the Company's growth and earnings for the foreseeable future. International contracts, operations and expansion expose the Company to risks inherent in doing business outside the United States, including:

- uncertain economic conditions in the foreign countries in which Shaw makes capital investments, operates and sells products and services;
- the lack of well-developed legal systems in some countries in which Shaw operates and sells products and services, which could make it difficult for it to enforce the Company's contractual rights;
- expropriation of property;
- restrictions on the right to convert or repatriate currency; and
- political risks, including risks of loss due to civil strife, acts of war, guerrilla activities and insurrection.

Foreign exchange risks may affect the Company's ability to realize a profit from certain projects. While Shaw attempts to denominate its contracts in United States dollars, from time to time the Company enters into contracts denominated in a foreign currency without escalation provisions. This practice subjects the Company to foreign exchange risks. In addition, to the extent contract revenues are denominated in a currency different than the contract costs, the Company increases its foreign exchange risks. The Company attempts to minimize its exposure from foreign exchange risks by obtaining escalation provisions or matching the contract revenue currency with the contract costs currency. Foreign exchange controls may also adversely affect the Company. For instance, prior to the lifting of foreign exchange controls in Venezuela in November 1995, foreign exchange controls adversely affected the Company's ability to repatriate profits from Shaw's Venezuelan subsidiary or otherwise convert local currency into United States dollars. Shaw generally does not obtain insurance for or hedge against foreign exchange risks for a material portion of its contracts. In addition, the Company's ability to obtain international contracts is impacted by the relative strength or weakness of the United States dollar relative to foreign currencies.

Failure to meet schedule or performance requirements of Shaw's contracts could adversely affect the Company. In certain circumstances, the Company guarantees facility completion by a scheduled acceptance date or achievement of certain acceptance and performance testing levels. Failure to meet any such schedule or performance requirements could result in additional costs and the amount of such additional costs could exceed project profit margins. Performance problems for existing and future contracts, whether fixed, maximum or unit priced, could cause actual results of operations to differ materially from those anticipated by the Company.

A dependence on one or a few clients could adversely affect the Company. Due to the size of many engineering and construction projects, one or a few clients have in the past and may in the future contribute a substantial portion of the Company's consolidated revenues in any one year, or over a period of several consecutive years. For example, the Company's backlog frequently reflects multi-projects for individual clients and therefore, one major customer may comprise a significant percentage of backlog at a point in time.

The Company has a contract with a major manufacturer of gas turbines to fabricate at least 90% of the pipe necessary to install the combined-cycle gas turbines to be built by this manufacturer domestically through 2004, and the relationship with the turbine manufacturer has assisted the Company in obtaining other work scopes, such as engineering, procurement, or construction associated with the projects for which the turbines are being manufactured.

Additionally, the Company has long-standing relationships with many significant customers, including customers with whom the Company has alliance agreements, that have preferred pricing arrangements; however, the Company's contracts with them are on a project by project basis and they may unilaterally reduce or discontinue their purchases at any time.

The loss of business from any one of such customers could have a material adverse effect on the Company's business or results of operations.

Shaw's dependence on a few suppliers and subcontractors could adversely affect the Company. The principal raw materials in the Company's piping systems business are carbon steel, stainless steel and other alloy piping, which Shaw obtains from a number of domestic and foreign primary steel producers. In the Company's engineering, procurement and construction services Shaw relies on third-party equipment manufacturers or materials suppliers as well as third-party sub-contractors, to complete its projects. To the extent that the Company cannot engage sub-contractors or acquire equipment or materials, Shaw's ability to complete a project in a timely fashion or at a profit may be impaired. To the extent the amount the Company is required to pay for these goods and services exceeds the amount the Company has estimated in bidding for lump-sum work, Shaw could experience losses in the performance of these contracts. In addition, if a manufacturer is unable to deliver the materials according to the negotiated terms, the Company may be required to purchase the materials from another source at a higher price. This may reduce the profit to be realized or result in a loss on a project for which the materials were needed.

The Company's projects expose it to potential professional liability, product liability, or warranty and other claims. Shaw engineers and constructs (and the Company's products typically are installed in) large industrial facilities in which system failures can be disastrous. Any catastrophic occurrences in excess of insurance limits at locations engineered or constructed by the Company or where Shaw's products are installed could result in significant professional liability, product liability or warranty and other claims against it. In addition, under some of the Company's contracts, Shaw must use new metals or processes for producing or fabricating pipe for its customers. The failure of any of these metals or processes could result in warranty claims against the Company for significant replacement or reworking costs.

Further, the engineering and construction projects Shaw is performing expose it to additional risks including cost overruns, equipment failures, personal injuries, property damage, shortages of materials and labor, work stoppages, labor disputes, weather problems and unforeseen engineering, architectural, environmental and geological problems. In addition, once the Company's construction is complete, Shaw may face claims with respect to the performance of these facilities.

The indemnification provisions of the Company's acquisition agreements may not fully protect it and may result in unexpected liabilities. Some of the former owners of companies Shaw has acquired are contractually required to indemnify the Company against liabilities related to the operation of their companies before Shaw acquired them and for misrepresentations made by them in connection with the acquisitions. In some cases, these former owners may not have the financial ability to meet their indemnification responsibilities. If this occurs, the Company may incur unexpected liabilities.

The Company's competitors may have greater resources and experience than Shaw does. In the Company's engineering, procurement and construction business, Shaw has numerous regional, national, and international competitors, many of which have greater financial and other resources than Shaw does. The Company's competitors include well-established, well-financed concerns, both privately and publicly held, including many major power equipment manufacturers and engineering and construction companies, some engineering companies, internal engineering departments at utilities and certain of its customers. Because the Company is primarily a service organization, Shaw competes by providing services of the highest quality. The markets that Shaw serves require substantial resources and particularly highly skilled and experienced technical personnel.

In pipe engineering and fabrication, competition on a domestic and international level is substantial. In the United States, there are a number of smaller pipe fabricators. Internationally, the Company's principal competitors are divisions of large industrial firms. Some of the Company's competitors, primarily in the international sector, have greater financial and other resources than Shaw does.

A failure to attract and retain qualified personnel could have an adverse effect on the Company. The Company's ability to attract and retain qualified engineers, scientists and other professional personnel, either through direct hiring or acquisition of other firms employing such professionals, will be an important factor in determining the Company's future success. The market for these professionals is competitive, and there can be no assurance that the Company will be successful in its efforts to attract and retain such professionals. In addition, Shaw's ability to be successful depends in part on its ability to attract and retain skilled laborers in its pipe fabrication business. Demand for these workers can at times be high and the supply extremely limited.

Terrorists' actions have and could negatively impact the U.S. economy and the Company's markets. Terrorist attacks, such as those that occurred on September 11, 2001, have contributed to economic instability in the United States and further acts of terrorism, violence or war could affect the markets in which the Company operates, its business operations, and expectations, and other forward-looking statements in this Annual Report.

The terrorist attacks on September 11, 2001 have also caused instability in the world's markets. There can be no assurance that the current armed hostilities will not increase or that these terrorist attacks, or responses from the United States, will not lead to further acts of terrorism and civil disturbances in the United States or elsewhere, which may further contribute to economic instability in the United States. These attacks or armed conflicts may directly impact the Company's physical facilities or those of its suppliers or customers and could impact the Company's domestic or international sales, its supply chain, its production capability, and its ability to deliver its products and services to its customers. Political and economic instability in some regions of the world may also result and could negatively impact the Company's business.

Environmental factors and changes in laws and regulations could increase the Company's costs and liabilities. The Company is subject to environmental laws and regulations, including those concerning:

- emissions into the air;
- discharges into waterways;
- generation, storage, handling, treatment and disposal of waste materials; and
- health and safety.

The Company's projects often involve nuclear, hazardous and other highly regulated materials, the improper characterization, handling or disposal of which could constitute violations of federal, state or local statutes, and result in criminal and/or civil liabilities. Environmental laws and regulations generally impose limitations and standards for certain pollutants or waste materials and require Shaw to obtain a permit and comply with various other requirements. Governmental authorities may seek to impose fines and penalties on the Company, or revoke or deny the issuance or renewal of operating permits, for failure to comply with applicable laws and regulations.

In addition, under the Comprehensive Environmental Response, Compensation and Liability Act of 1980 ("CERCLA"), as amended and comparable state laws, the Company may be required to investigate and remediate hazardous substances. CERCLA and these comparable state laws typically impose liability without regard to whether a company knew of or caused the release, and liability has been interpreted to be joint and several unless the harm is divisible and there is a reasonable basis of allocation. The principal federal environmental legislation affecting the Company's environmental and infrastructure division of its principal engineering subsidiary and its clients include: the National Environmental Policy Act of 1969 ("NEPA"), the Resource Conservation and Recovery Act of 1976 ("RCRA"), the Clean Air Act, the Federal Water Pollution Control Act and the Superfund Amendments and Reauthorization Act of 1986 ("SARA"). The Company's foreign operations are also subject to various requirements governing environmental protection.

The environmental health and safety laws and regulations to which Shaw is subject are constantly changing, and it is impossible to predict the effect of such laws and regulations on the Company in the future. Shaw has not conducted environmental audits of many of its properties, including the assets the Company acquired from Stone & Webster. The Company cannot give any assurance that its operations will continue to comply with future laws and regulations or that these laws and regulations will not significantly adversely affect the Company.

If Shaw has to write-off a significant amount of intangible assets, the Company's earnings will be negatively impacted.

Because the Company has grown in part through acquisitions, goodwill and other acquired intangible assets represent a substantial portion of its assets. Goodwill was approximately \$369 million as of August 31, 2001. If the Company makes additional acquisitions, it is likely that additional intangible assets will be recorded on its books. A determination that a significant impairment in value of the Company's unamortized intangible assets has occurred would require the Company to write-off a substantial portion of its assets. This write-off would negatively affect the Company's earnings. See Note 1 of Notes to Consolidated Financial Statements.

The Company is and will continue to be involved in litigation. The Company has been and may from time to time be named as a defendant in legal actions claiming damages in connection with engineering and construction projects and other matters. These are typically actions that arise in the normal course of business, including employment-related claims and contractual disputes or claims for personal injury or property damage which occur in connection with services performed relating to project or construction sites. Such contractual disputes normally involve claims relating to the performance of equipment design or other engineering services or project construction services provided by the Company's subsidiaries.

While the Company did not assume possible liabilities relating to environmental pollution in connection with Stone & Webster's acquisition, a federal, state or local governmental authority may seek redress from Shaw or its subsidiaries and the Company may be named as a Potentially Responsible Party in an action by such governmental authority. While the Company would vigorously contest any attempt to make the Company responsible for unassumed environmental liabilities, there can be no assurance that the Company would not be held liable in connection with such matters in amounts that would have a material adverse effect on its business and results of operations.

Adverse events could negatively affect the Company's liquidity position. The Company operates in an environment in which the Company could be required to utilize large sums of working capital, sometimes on short notice and sometimes without the ability to recover the expenditures (as has been the experience of certain of the Company's competitors). Circumstances or events which could create large cash outflows include loss contracts, environmental liabilities, litigation risks, unexpected costs or losses resulting from acquisitions, contract initiation or completion delays, political conditions, customer payment problems, foreign exchange risks, professional and product liability claims, cash repurchases of the LYONs, etc. Although the Company attempts to mitigate its risks, it cannot provide assurance that it will have sufficient liquidity or the credit capacity to meet all its cash needs if it encounters significant unforeseen working capital requirements which could result from these or other factors.

Insufficient liquidity could have important consequences to the Company. For example, the Company could:

- experience difficulty in financing future acquisitions and/or its continuing operations;
- be required to dedicate a substantial portion of its cash flows from operations to the repayment of its debt and the interest associated with its debt;
- have less operating flexibility due to restrictions which could be imposed by its creditors, including restrictions on incurring additional debt, creating liens on its properties and paying dividends;
- have less success in obtaining new work if its sureties and/or its lenders were to limit its ability to provide new performance bonds or letters of credit for its projects; and
- incur increased lending fees, costs and interest rates.

All or any of these matters could place the Company at a competitive disadvantage compared with competitors with more liquidity and could have a negative impact upon the Company's financial condition and results of operations.

Work stoppages and other labor problems could adversely affect the Company. Some of the Company's employees in the United States and abroad may be represented by labor unions. Shaw experienced a strike, without material impact on pipe production, by union members in February 1997 relating to the termination of collective bargaining agreements covering its pipe facilities in Walker and Prairieville, Louisiana. A lengthy strike or other work stoppage at any of the Company's facilities could have a material adverse effect on the Company. From time to time Shaw has also experienced attempts to unionize the Company's non-union shops. While these efforts have achieved limited success to date, the Company cannot give any assurance that it will not experience additional union activity in the future.

Changes in technology could adversely affect the Company and its competitors may develop or otherwise acquire equivalent or superior technology. The Company believes its Stone & Webster subsidiary has a leading position in technologies for the design and construction of ethylene plants. The Company protects its position through patent registrations, license restrictions, and a research and development program; however, it is possible that others may develop competing processes which could negatively affect the Company's market position.

Additionally, the Company has developed construction and power generation software, which it feels provide competitive advantages. The advantages currently provided by this software could be at risk if competitors were to develop superior or comparable technologies.

The Company's induction pipe bending technology and capabilities favorably influence the Company's ability to compete successfully. Currently this technology and its proprietary software are not patented. While the Company has some legal protections against the dissemination of this know-how, (including non-disclosure and confidentiality agreements), the Company's efforts to prevent others from using its technology could be time-consuming, expensive and ultimately may be unsuccessful or only partially successful. Finally, there is nothing to prevent the Company's competitors from independently attempting to develop or obtain access to technologies that are similar or superior to Shaw's technology.

The Company's success depends on key members of its management, including J. M. Bernhard, Jr. The Company's success is dependent upon the continued services of J. M. Bernhard, Jr., its founder, Chairman, President and Chief Executive Officer, and other key officers. The loss of Mr. Bernhard or other key officers could adversely affect the Company. The Company does not maintain key employee insurance on any of its executive officers.

Market prices of the Company's equity securities could change significantly. The market prices of the Company's Common Stock may change significantly in response to various factors and events, including the following:

- the other risk factors described in this Annual Report, including changing demand for its products and services;
- a shortfall in operating revenue or net income from that expected by securities analysts and investors;
- changes in securities analysts' estimates of the financial performance of Shaw or its competitors or the financial performance of companies in its industry generally;
- general conditions in its industry;
- general conditions in the securities markets;
- issuance of a significant number of shares upon exercise of employee stock options or upon conversion of the LYONs; and
- issuance of shares of Common Stock to fund repurchases by the Company of the LYONs.

Many of these factors are beyond the Company's control.

Provisions in the Company's charter documents and rights agreement could make it more difficult to acquire the Company and may reduce the market price of the Common Stock. The Company's articles of incorporation and by-laws contain certain provisions, such as a provision establishing a classified board of directors (in the event the entire board of directors is increased to twelve or more members), provisions entitling holders of shares of Common Stock that have been beneficially owned for four years or more to five votes per share, a provision prohibiting shareholders from calling special meetings, a provision requiring super majority voting (75% of the outstanding voting power) to approve certain business combinations and provisions authorizing the Board of Directors to issue up to 20 million shares of preferred stock without approval of the Company's shareholders. Also, the Company has adopted a rights plan which limits the ability of any person to acquire more than 15% of the Company's Common Stock. These provisions could have the effect of delaying or preventing a change in control of the Company or the removal of management, of deterring potential acquirers from making an offer to the Company's shareholders and of limiting any opportunity to realize premiums over prevailing market prices for the Common Stock. Provisions of the Company's shareholder rights agreement could also have the effect of deterring changes of control of the Company.

Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

The Company is exposed to interest rate risk due to changes in interest rates, primarily in the United States. The Company's policy is to manage interest rates through the use of a combination of fixed and floating rate debt and short-term fixed rate investments. The Company currently does not use any derivative financial instruments to manage its exposure to interest rate risk. The table below provides information about the Company's future maturities of principal for outstanding debt instruments and fair value at August 31, 2001.

<i>(Dollars in millions)</i>	2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
Long-term debt								
Fixed rate	\$4.8	\$2.8	\$510.3	\$0.3	—	—	\$518.2	\$422.0
Average interest rate	7.4%	8.0%	2.25%	7.2%	—	—	2.3%	—
Short-term line of credit								
Variable rate	\$3.9	—	—	—	—	—	\$ 3.9	\$ 3.9
Average interest rate	6.0%	—	—	—	—	—	6.0%	—

As discussed in Note 7 of Notes to Consolidated Financial Statements, on May 1, 2001, the Company issued \$790 million (face value), 20-year, 2.25% zero coupon unsecured convertible debt Liquid Yield Option™ Notes (the "LYONs") for which it received net proceeds of approximately \$490 million. After paying off approximately \$67 million of outstanding debt, the remaining proceeds were invested in high quality short-term cash equivalents and marketable securities held to maturity. During fiscal 2001, the income realized from these investments was greater than the interest costs associated with the LYONs debt. However, the Company anticipates that based on its current cash flow and yield projections that interest income will be less than its interest expense in fiscal 2002.

The holders of the LYONs have the right to require the Company to repurchase the debt on the third, fifth, tenth and fifteenth anniversaries at the accreted value. Therefore, the debt is presented above as maturing on the third anniversary date because of the potential for repurchase requests by the debt holders at that time.

Also during fiscal 2001, the Company used the proceeds from the sales of the LYONs, the Company's Common Stock (see Note 2 of Notes to Consolidated Financial Statements) and various assets to pay off its borrowings under its primary Credit Facility (\$235.2 million at August 31, 2000). At August 31, 2001, the interest rate on this line of credit was either 6.5% (if the prime rate index had been chosen) or 5.26% (if the LIBOR rate index had been chosen) with an availability of \$238.5 million. See Note 8 of Notes to Consolidated Financial Statements for further discussion of this line of credit.

The estimated fair value of long-term debt as of August 31, 2001 and 2000 was approximately \$422 million and \$46.7 million, respectively. The fair value of the convertible debt as of August 31, 2001 was based on recent sales of such debt as of August 31, 2001. The fair value of the Company's other long-term debt at August 31, 2001 and August 31, 2000 were based on borrowing rates currently available to the Company for notes with similar terms and average maturities.

Foreign Currency Risks

The majority of the Company's transactions are in U.S. dollars; however, certain of the Company's subsidiaries conduct their operations in various foreign currencies. Currently, the Company, when considered appropriate, uses hedging instruments to manage its risks associated with its operating activities when an operation enters into a transaction in a currency that is different from its local currency. In these circumstances, the Company will frequently utilize forward exchange contracts to hedge the anticipated purchases and/or sales. The Company attempts to minimize its exposure to foreign currency fluctuations by matching its revenues and expenses in the same currency for its contracts. As of August 31, 2001, the Company had a minimal number of forward exchange contracts outstanding that were hedges of certain commitments of foreign subsidiaries. The exposure from the commitments is not material to the Company's results of operations or financial position. See Notes 1 and 17 of Notes to Consolidated Financial Statements.

The Shaw Group Inc. and Subsidiaries
Consolidated Balance Sheets
As of August 31, 2001 and 2000

<i>(Dollars in thousands)</i>	2001	2000
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 443,304	\$ 21,768
Marketable securities, held to maturity	45,630	—
Accounts receivable, including retainage, net	341,833	311,285
Accounts receivable from unconsolidated entity	4,848	—
Inventories	91,155	96,283
Cost and estimated earnings in excess of billings on uncompleted contracts	95,012	143,250
Prepaid expenses	10,660	13,555
Deferred income taxes	54,351	63,858
Assets held for sale	3,491	116,501
Other current assets	5,757	18,335
Total current assets	1,096,041	784,835
Investment in and advances to unconsolidated entities, joint ventures and limited partnerships	24,314	20,361
Investment in securities available for sale	10,490	16,361
Property and equipment:		
Transportation equipment	4,433	4,710
Furniture and fixtures	49,550	38,629
Machinery and equipment	79,536	94,533
Buildings and improvements	33,127	37,922
Assets acquired under capital leases	1,554	1,554
Land	7,302	10,520
Construction in progress	21,659	2,766
	197,161	190,634
Less: Accumulated depreciation	(61,959)	(46,087)
	135,202	144,547
Goodwill, net of accumulated amortization of \$25,234 and \$6,375 at August 31, 2001 and 2000, respectively	368,872	282,238
Other assets	66,935	86,741
	\$1,701,854	\$1,335,083

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

(Continued)

The Shaw Group Inc. and Subsidiaries
Consolidated Balance Sheets
As of August 31, 2001 and 2000

(Dollars in thousands, except share amounts)

	2001	2000
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 181,936	\$ 225,230
Accrued liabilities	81,660	147,887
Current maturities of long-term debt	2,365	26,654
Short-term revolving lines of credit	3,909	2,893
Current portion of obligations under capital leases	2,313	704
Deferred revenue—prebilled	7,976	6,045
Advanced billings and billings in excess of cost and estimated earnings on uncompleted contracts	244,131	166,147
Accrued contract losses and reserves	50,707	106,489
Total current liabilities	574,997	682,049
Long-term revolving line of credit	—	235,187
Long-term debt, less current maturities	509,684	19,127
Obligations under capital leases, less current obligation	3,183	651
Deferred income taxes	8,247	6,098
Other liabilities	7,350	14,696
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, no par value, 20,000,000 shares authorized; no shares issued and outstanding	—	—
Common stock, no par value, 200,000,000 shares authorized; 41,012,292 and 51,802,324 shares issued, respectively; 41,012,292 and 35,402,408 shares outstanding, respectively	437,015	298,005
Retained earnings	167,578	106,581
Accumulated other comprehensive income	(6,200)	(5,209)
Unearned restricted stock compensation	—	(59)
Treasury stock, 16,399,916 shares at August 31, 2000	—	(22,043)
Total shareholders' equity	598,393	377,275
	\$1,701,854	\$1,335,083

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

Consolidated Statements of Income

For the Years Ended August 31, 2001, 2000 and 1999

<i>(Dollars in thousands, except per share amounts)</i>	2001	2000	1999
Sales	\$1,538,932	\$762,655	\$494,014
Cost of sales	1,292,316	635,579	400,186
Gross profit	246,616	127,076	93,828
General and administrative expenses	139,660	74,297	60,082
Operating income	106,956	52,779	33,746
Interest income	8,746	682	465
Interest expense	(15,680)	(8,003)	(8,649)
Other, net	(128)	90	513
	(7,062)	(7,231)	(7,671)
Income before income taxes	99,894	45,548	26,075
Provision for income taxes	38,366	16,359	8,635
Income before earnings (losses) from unconsolidated entities	61,528	29,189	17,440
Earnings (losses) from unconsolidated entities, net of tax benefit of \$354	(316)	1,194	681
Income before extraordinary item and cumulative effect of change in accounting principle	61,212	30,383	18,121
Extraordinary item for early extinguishment of debt, net of taxes of \$134 and \$340	(215)	(553)	—
Cumulative effect on prior years of change in accounting for start-up costs, net of taxes of \$196	—	(320)	—
Net income	\$ 60,997	\$ 29,510	\$ 18,121
Basic income per common share:			
Income per common share:			
Income before extraordinary item and cumulative effect of change in accounting principle	\$ 1.53	\$ 1.03	\$ 0.76
Extraordinary item, net of taxes	(0.01)	(0.02)	—
Cumulative effect of change in accounting principle, net of taxes	—	(0.01)	—
Net income per common share	\$ 1.52	\$ 1.00	\$ 0.76
Diluted income per common share:			
Income per common share:			
Income before extraordinary item and cumulative effect of change in accounting principle	\$ 1.46	\$ 0.99	\$ 0.73
Extraordinary item, net of taxes	—	(0.02)	—
Cumulative effect of change in accounting principle, net of taxes	—	(0.01)	—
Net income per common share	\$ 1.46	\$ 0.96	\$ 0.73

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

Consolidated Statements of Shareholders' Equity

	Common Stock		Unearned Restricted Stock Compensation	Treasury Stock		Accumulated Other Comprehensive Income	Retained Earnings	Total Shareholders' Equity
	Shares	Amount		Shares	Amount			
<i>(Dollars in thousands, except share amounts)</i>								
Balance, September 1, 1998	39,885,564	\$119,360	\$(367)	13,325,832	\$ (6,828)	\$ (420)	\$ 58,950	\$170,695
Comprehensive income:								
Net income	—	—	—	—	—	—	18,121	18,121
Other comprehensive income:								
Foreign translation adjustments	—	—	—	—	—	(1,115)	—	(1,115)
Comprehensive income								17,006
Restricted stock cancellation	(30,000)	(255)	145	—	—	—	—	(110)
Amortization of restricted stock compensation	—	—	97	—	—	—	—	97
Exercise of options	65,000	248	—	—	—	—	—	248
Purchases of treasury stock	—	—	—	3,122,640	(13,697)	—	—	(13,697)
Balance, August 31, 1999	39,920,564	119,353	(125)	16,448,472	(20,525)	(1,535)	77,071	174,239
Comprehensive income:								
Net income	—	—	—	—	—	—	29,510	29,510
Other comprehensive income:								
Foreign translation adjustments	—	—	—	—	—	(3,674)	—	(3,674)
Comprehensive income								25,836
Shares issued in public offering	6,900,000	67,487	—	—	—	—	—	67,487
Amortization of restricted stock compensation	—	—	66	—	—	—	—	66
Shares issued to acquire PPM	86,890	2,012	—	—	—	—	—	2,012
Shares issued to acquire Stone & Webster	4,463,546	105,033	—	—	—	—	—	105,033
Exercise of options	580,764	2,255	—	—	—	—	—	2,255
Tax benefit on exercise of options	—	2,739	—	—	—	—	—	2,739
Purchases of treasury stock	—	—	—	100,884	(2,392)	—	—	(2,392)
Retirement of treasury stock	(149,440)	(874)	—	(149,440)	874	—	—	—
Balance, August 31, 2000	51,802,324	298,005	(59)	16,399,916	(22,043)	(5,209)	106,581	377,275
Comprehensive income:								
Net income	—	—	—	—	—	—	60,997	60,997
Other comprehensive income:								
Foreign translation adjustments	—	—	—	—	—	(1,099)	—	(1,099)
Unrealized net gain on hedging activities, net of taxes of \$72	—	—	—	—	—	115	—	115
Unrealized net losses on securities available for sale, net of tax benefit of \$5	—	—	—	—	—	(7)	—	(7)
Comprehensive income								60,006
Shares issued in public offering	4,837,338	144,809	—	—	—	—	—	144,809
Amortization of restricted stock compensation	—	—	59	—	—	—	—	59
Shares issued to acquire SS&S	170,683	6,274	—	—	—	—	—	6,274
Exercise of options	606,863	3,271	—	—	—	—	—	3,271
Tax benefit on exercise of options	—	6,699	—	—	—	—	—	6,699
Return of Naptech acquisition escrow shares	—	—	—	5,000	—	—	—	—
Retirement of treasury stock	(16,404,916)	(22,043)	—	(16,404,916)	22,043	—	—	—
Balance, August 31, 2001	41,012,292	\$437,015	\$ 0	0	\$ 0	\$(6,200)	\$167,578	\$598,393

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

Consolidated Statements of Cash Flows

For the Years Ended August 31, 2001, 2000 and 1999

<i>(Dollars in thousands)</i>	2001	2000	1999
Cash flows from operating activities:			
Net income	\$ 60,997	\$ 29,510	\$ 18,121
Adjustments to reconcile net income to net cash provided by (used in) operating activities:			
Depreciation and amortization	39,740	16,808	13,271
Provision for deferred income taxes	37,724	2,110	3,697
(Earnings) losses from unconsolidated entities	316	(1,194)	(681)
Foreign currency transaction losses	41	1,805	533
Utilization of gross margin reserve	(70,081)	(7,933)	—
Amortization of deferred debt issue costs	5,515	1,004	198
Accretion of interest on discounted convertible long-term debt	3,787	—	—
Other	(335)	(4,700)	(1,792)
Changes in assets and liabilities, net of effects of acquisitions:			
(Increase) decrease in receivables	(24,627)	(51,775)	18,192
(Increase) decrease in cost and estimated earnings in excess of billings on uncompleted contracts	12,064	(33,833)	(4,485)
(Increase) decrease in inventories	5,173	(17,941)	(12,243)
(Increase) in assets held for sale	(1,397)	(332)	—
(Increase) decrease in other current assets	12,722	(5,343)	(471)
(Increase) decrease in prepaid expenses	(760)	(787)	564
(Increase) decrease in other assets	3,894	(749)	(1,018)
(Decrease) in accounts payable	(42,437)	(37,886)	(7,688)
Increase in deferred revenue—prebilled	1,760	2,469	1,763
Increase (decrease) in accrued liabilities	(62,871)	21,445	4,326
Increase (decrease) in advanced billings and billings in excess of cost and estimated earnings on uncompleted contracts	66,813	21,823	(4,046)
(Decrease) in accrued contract losses and adjustments	(29,219)	(5,575)	—
Increase (decrease) in other long-term liabilities	(7,414)	1,198	—
Net cash provided by (used in) operating activities	11,405	(69,876)	28,241
Cash flows from investing activities:			
Proceeds from sale of assets	120,920	8,715	1,530
Acquisition, return of funds	22,750	—	—
Purchase of marketable securities, held to maturity	(45,630)	—	—
Purchase of property and equipment	(38,121)	(20,619)	(17,967)
Investment in and advances to unconsolidated entities and joint ventures	(4,237)	(1,561)	(2,552)
Purchase of securities available for sale	(1,241)	—	(12,500)
Investment in subsidiaries, net of cash received	(160)	(2,342)	—
Net cash provided by (used in) investing activities	\$ 54,281	\$ (15,807)	\$(31,489)

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

(Continued)

<i>(Dollars in thousands)</i>	2001	2000	1999
Cash flows from financing activities:			
Proceeds from issuance of debt, net of deferred debt issue costs	\$ 492,851	\$ 2,443	\$ 5,475
Issuance of Common Stock	148,080	69,742	248
Net proceeds (repayments) from revolving credit agreements, including payments for deferred debt issue costs	(235,024)	150,536	22,682
Repayment of debt and leases	(49,247)	(112,555)	(10,690)
Increase (decrease) in outstanding checks in excess of bank balance	—	(6,610)	2,614
Purchase of treasury stock	—	(2,392)	(13,697)
Net cash provided by financing activities	356,660	101,164	6,632
Effects of foreign exchange rate changes on cash	(810)	(614)	(226)
Net increase in cash	421,536	14,867	3,158
Cash and cash equivalents—beginning of year	21,768	6,901	3,743
Cash and cash equivalents—end of year	\$ 443,304	\$ 21,768	\$ 6,901
Supplemental disclosures:			
Cash payments for:			
Interest (net of capitalized interest)	\$ 5,931	\$ 9,329	\$ 8,530
Income taxes	\$ 2,268	\$ 11,286	\$ 5,592
Noncash investing and financing activities:			
Payment of liability with securities available for sale	\$ 7,000	\$ —	\$ —
Property and equipment acquired through issuance of debt	\$ 6,379	\$ 1,467	\$ —
Investment in subsidiaries acquired through issuance of Common Stock	\$ 6,274	\$ 107,045	\$ —
Investment in securities available for sale acquired in lieu of interest payment	\$ 843	\$ 1,406	\$ 1,330
Sale of property financed through issuance of note receivable	\$ —	\$ 3,960	\$ 1,400

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

Notes to Consolidated Financial Statements

Note 1—Summary of Significant Accounting Policies

Principles of Consolidation The consolidated financial statements include the accounts of The Shaw Group Inc. (a Louisiana corporation) and its wholly-owned subsidiaries (collectively, the “Company”). All material intercompany accounts and transactions have been eliminated in these financial statements.

In order to prepare financial statements in conformity with generally accepted accounting principles, management is required to make estimates and assumptions as of the date of the financial statements which affect the reported values of assets and liabilities and revenues and expenses, and disclosures of contingent assets and liabilities. Areas requiring significant estimates by the Company’s management, include (i) contract expenses and profits and application of percentage of completion accounting; (ii) recoverability of inventory and application of lower of cost or market accounting; (iii) provisions for uncollectable receivables and customer claims; (iv) provisions for income taxes and related valuation allowances; (v) recoverability of net goodwill; (vi) recoverability of other intangibles and related amortization; and (vii) accruals for estimated liabilities, including litigation and insurance reserves. Actual results could differ from those estimates.

Nature of Operations The Company is a vertically-integrated provider of comprehensive engineering, procurement and construction services and complete piping services. The Company operates primarily in the United States, the Asia/Pacific Rim, Europe, South America and the Middle East for customers in the power generation, process (including petrochemical, chemical and refining) and other industries as well as the environmental and infrastructure sector. The Company’s services and products include consulting, project design, engineering and procurement, piping system fabrication, industrial construction and maintenance, manufacture and distribution of specialty pipe fittings and design and fabrication of pipe support systems. The Company’s operations are conducted primarily through wholly-owned subsidiaries and joint ventures.

Cash and Cash Equivalents Highly liquid investments are classified as cash equivalents if they mature within three months of the purchase date. At August 31, 2000, the Company included in cash and cash equivalents approximately \$1,300,000 which resulted from industrial development bond financing. The Company was required to invest these funds, which were released in fiscal 2001 in AAA rated, short-term marketable securities until used for other capital improvements.

Accounts Receivable and Credit Risk The Company’s principal customers are major multi-national industrial corporations, independent and merchant power providers, governmental agencies and equipment manufacturers. Work is performed under contract and the Company believes that in most cases its credit risk is minimal. The Company grants short-term credit to its customers.

At August 31, 2001, the Company had an outstanding receivable from one customer totaling approximately 33% of total accounts receivable. Approximately 95% of that outstanding receivable balance represented billings in excess of costs.

Allowance for Uncollectable Receivables and Contract Adjustments The allowance for uncollectable receivables and contract adjustments was approximately \$12,650,000 and \$5,850,000 at August 31, 2001 and 2000, respectively. The Company estimates the amount of uncollectable receivables based on historical experience and management’s understanding of the financial condition of its customers. Contract adjustment allowances represent management’s estimates of the net amounts to be realized with respect to matters disputed or questioned by customers. Increases to the allowance for the year ended August 31, 2001 were approximately \$10,600,000 and total reductions were approximately \$3,800,000. The net increase to this allowance was approximately \$100,000 in fiscal 2000. The Company increases or reduces sales for contract adjustments.

At August 31, 2001 and 2000, accounts receivable included approximately \$14,200,000 and \$17,900,000, respectively, of receivables and claims, recorded at net realizable value, due under contracts which are subject to contract renegotiations or legal proceedings. At August 31, 2001, contracts with 16 customers made up the \$14,200,000 balance discussed above. Management believes that the ultimate resolution of these disputes will not have a significant impact on future results of operations.

Inventories Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out (“FIFO”) or weighted average cost methods.

Property and Equipment Property and equipment are recorded at cost. Additions and improvements (including interest costs for construction of certain long-lived assets) are capitalized. Maintenance and repair expenses are charged to income as incurred. The cost of property and equipment sold or otherwise disposed of and the accumulated depreciation thereon, are eliminated from the property and related accumulated depreciation accounts, and any gain or loss is credited or charged to income.

For financial reporting purposes, depreciation is provided by utilizing the straight-line method over the following estimated useful service lives:

Transportation equipment	5–15 Years
Furniture and fixtures	3– 7 Years
Machinery and equipment	3–18 Years
Buildings and improvements	8–40 Years

During the year ended August 31, 2001, interest costs of approximately \$363,000 were capitalized.

Income Taxes The Company provides for deferred taxes in accordance with Statement of Financial Accounting Standards (“SFAS”) No. 109—“Accounting for Income Taxes,” which requires an asset and liability approach for measuring deferred tax assets and liabilities due to temporary differences existing at year end using currently enacted tax rates.

Revenues For project management, engineering, procurement, and construction services, the Company recognizes revenues under the percentage of completion method measured primarily on contract costs incurred to date, excluding the costs of any purchased but uninstalled materials, compared with total estimated contract costs. Revenues from cost-plus-fee contracts are recognized on the basis of costs incurred during the period plus the fee earned. Profit incentives are included in revenues when their realization is reasonably assured.

For unit-priced pipe fabrication contracts, the Company recognizes revenues upon completion of individual spools of production. A spool consists of piping materials and associated shop labor to form a prefabricated unit according to contract specifications. Spools are generally shipped to job site locations when complete. During the fabrication process, all direct and indirect costs related to the fabrication process are capitalized as work in progress. For lump-sum fabrication contracts, the Company recognizes revenues based on the percentage of completion method, measured primarily by the cost of materials for which production is complete compared with the total estimated material costs of the contract.

Revenue is recognized from consulting services as the work is performed.

The Company recognizes revenues for pipe fittings, manufacturing operations and other services primarily at the time of shipment or upon completion of the services.

Provisions for estimated losses for uncompleted contracts are made in the period in which such losses are identified. The cumulative effect of other changes, including those arising from contract penalty provisions, final contract settlements and reviews performed by customers, are recognized in the period in which the revisions are identified. To the extent that these adjustments result in a reduction or elimination of previously reported profits, the Company would report such a change by recognizing a charge against current earnings, which might be significant depending on the size of the project or the adjustment. An amount equal to the costs attributable to unapproved change orders and claims is included in the total estimated revenue when realization is probable. Profit from unapproved change orders and claims is recorded in the year such amounts are resolved.

Goodwill and Other Intangibles Goodwill represents the excess of the purchase price of acquisitions over the fair value of the net assets acquired. The Company’s practice has been to amortize goodwill and most other intangibles over a 20-year period on a straight-line basis. However, effective fiscal 2002, the Company will cease to amortize goodwill pursuant to SFAS No. 142 issued in July 2001 (see *New Accounting Standards* below).

The Company also has recorded in other assets intangible assets with respect to various licenses, patents, technology and related processes pertaining to the design and construction of ethylene plants (see Note 3 of Notes to Consolidated Financial Statements) which are being amortized over a 15-year period on a straight-line basis.

Goodwill represents the excess of the purchase price of acquisitions over the fair value of the net assets acquired. Such excess costs and intangible assets of various licenses, patents, technology and related processes pertaining to the design and construction of plants which produce ethylene (see Note 3) are being amortized on a straight-line basis over a 20-year period. The Company periodically assesses the recoverability of the unamortized balance based on expected future profitability and undiscounted future cash flows of the acquisitions and their contribution to the overall operation of the Company. Should the review indicate that the carrying value is not recoverable, the excess of the carrying value over the undiscounted cash flows would be recognized as an impairment loss.

Through August 31, 2001, the Company has historically conducted impairment reviews of its goodwill and other intangibles, however, to date the Company has not identified any impairment losses. The review of goodwill assessed the recoverability of the unamortized balance based on expected future profitability, undiscounted future cash flows of the acquisitions and their contribution to the overall operation of the Company. An impairment loss would have been recognized for the amount identified in the review by which the goodwill balance exceeded the recoverable goodwill balance. Subsequent to August 31, 2001, the Company will perform impairment reviews in accordance with SFAS No. 142 (see *New Accounting Standards* below).

Financial Instruments, Forward Contracts—Non-Trading Activities The majority of the Company's transactions are in U.S. dollars; however, certain of the Company's foreign subsidiaries conduct their operations in their local currency. Accordingly, there are situations when the Company believes it is appropriate to use off-balance sheet financial hedging instruments (generally foreign currency forward contracts) to manage foreign currency risks when it enters into a transaction denominated in a currency other than its local currency.

Prior to September 1, 2000, at the inception of a hedging contract, the Company designated a contract as a hedge if there was a direct relationship to the price risk associated with the Company's future sales and purchases. Recognition of the gains and losses on the early termination or maturity of forward contracts designated as hedges were deferred until the period the hedged transaction was recorded. However, gains or losses on the hedge transaction were recognized when the direct relationship between the hedge and the Company's price risk ceased to exist. Future changes in the fair value of the forward contracts were then recognized as gains or losses in revenues or expenses in the period of change.

Effective September 1, 2000, the Company adopted SFAS No. 133—"Accounting for Derivative Instruments and Hedging Activities," which requires that all derivative instruments be recorded on the balance sheet at fair value. The Company designates each derivative contract as one of the following on the day the contract is executed: (a) hedge of the fair value of a recognized asset or liability or of an unrecognized firm commitment (fair value hedge), (b) hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (cash flow hedge), or (c) hedge of a net investment in a foreign operation (net investment hedge). Changes in the fair value of derivatives are recorded each period in current earnings or other comprehensive income, depending on whether the derivative is designated as part of a hedge transaction and, if so, depending on the type of hedge transaction. For fair value hedge transactions, changes in fair value of the derivative instrument are generally offset in the income statement by changes in the fair value of the item being hedged. For cash flow hedge transactions, changes in the fair value of the derivative instrument are reported in other comprehensive income. For net investment hedge transactions, changes in the fair value are recorded as a component of the foreign currency translation account that is also included in other comprehensive income. The gains and losses on cash flow hedge transactions that are reported in other comprehensive income are reclassified to earnings in the periods in which earnings are effected by the variability of the cash flows of the hedged item. The ineffective portions of all hedges are recognized in current period earnings. Upon initial application of SFAS No. 133, the Company recorded the fair value of the existing hedge contracts on the balance sheet and a corresponding unrecognized loss of \$23,000 as a cumulative effect adjustment of accumulated other comprehensive income, which was transferred to earnings during fiscal 2001. The Company's hedging activities during fiscal 2001 were not material.

The Company utilizes forward foreign exchange contracts to reduce its risk from foreign currency price fluctuations related to firm or anticipated commitments to purchase or sell equipment, materials and or services. These investments are designated as cash flow hedging instruments. The Company normally does not use any other type of derivative instrument or participate in any other hedging activities.

Comprehensive Income In the first quarter of fiscal 1999, the Company adopted SFAS No. 130—"Reporting Comprehensive Income," which establishes standards for the reporting and display of comprehensive income as part of a full set of financial statements. Comprehensive income for a period encompasses net income and all other changes in a company's equity other than from transactions with the company's owners.

The foreign currency translation adjustments relate to the varying strength of the U.S. dollar in relation to the British pound, Australian and Canadian dollar and Dutch guilder. The Company's statement of comprehensive income is included in the Consolidated Statements of Shareholders' Equity.

Reclassifications Certain reclassifications have been made to the prior years' financial statements in order to conform to the current year's presentation.

Stock-Based Compensation Stock-based compensation is accounted for using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations. It is the Company's general practice to issue stock options at the market value of the underlying stock; and therefore, no compensation expense is recorded for these stock options.

New Accounting Standards In early 1998, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position 98-5, "Reporting on the Costs of Start-Up Activities" ("SOP") which became effective for fiscal years beginning after December 15, 1998. The SOP requires that costs of start-up activities and organization costs be expensed as incurred and that upon adoption of the SOP that any previously unamortized costs be written off and reported as a cumulative effect of a change in accounting principle. Accordingly, the Company wrote off deferred organizational costs of approximately \$320,000, net of taxes, at the start of fiscal 2000 (September 1999).

In July 2001, the Financial Accounting Standards Board (FASB) issued two new accounting standards SFAS No. 141—"Business Combinations" and SFAS No. 142—"Goodwill and Other Intangible Assets." The new standards have significantly changed prior practices by: (i) terminating the use of the pooling-of-interests method of accounting for future business combinations, (ii) ceasing goodwill amortization, and (iii) requiring impairment testing of goodwill based on a fair value concept. SFAS No. 142 requires that impairment testing of the opening goodwill balances be performed within six months from the start of the fiscal year in which the standard is adopted and that any impairment be written off and reported as a cumulative effect of a change in accounting principle. It also requires that another impairment test be performed during the fiscal year of adoption of the standard and, that impairment tests should be performed at least annually thereafter, with interim testing required if circumstances warrant. The standards must be implemented for fiscal years beginning after December 31, 2001, but early adoption is permitted. The Company has decided to adopt the new standards for its fiscal year beginning September 1, 2001. Accordingly, the Company will cease to amortize goodwill in fiscal 2002. Goodwill amortization was approximately \$18,859,000, \$3,099,000 and \$1,846,000 for the years ended August 31, 2001, 2000 and 1999, respectively. The Company has not completed its initial evaluation of goodwill impairment that is required with the adoption of the SFAS No. 142. However, based on the preliminary evaluation procedures it has performed, the Company does not believe that its existing goodwill balances will be impaired under the new standards; however, no assurances can be given. The initial transition evaluation is required to be and will be completed by February 28, 2002 which is within the six month transition period allowed by the new standard upon adoption.

The FASB also recently issued SFAS No. 143, "Accounting for Asset Retirement Obligations." This statement, which is first effective in 2003, covers the accounting for closure or removal-type costs that are incurred with respect to long-lived assets. The nature of the Company's business and long-lived assets is such that adoption of this new standard should have no significant impact on the Company's financial position or results of operations.

In August 2001, the FASB issued SFAS No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," which supersedes FASB No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed of." The new statement also supersedes certain aspects of APB 30, "Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions," with regard to reporting the effects of a disposal of a segment of a business and will require expected future operating losses from discontinued operations to be reported in discontinued operations in the period incurred rather than as of the measurement date as presently required by APB 30. Additionally, certain dispositions may now qualify for discontinued operations treatment. The provisions of the statement are required to be applied for fiscal years beginning after December 15, 2001 and interim periods within those fiscal years. The Company has not yet determined what effect this statement will have on its financial statements.

Note 2—Capital Stock Transactions

In September 2001, the Company announced that its Board of Directors had authorized the Company to repurchase shares of its Common Stock, depending on market conditions, up to a limit of \$100,000,000. As of October 5, 2001, the Company had purchased 203,000 shares at a cost of approximately \$5,900,000 under this program.

On July 31, 2001, the Company issued a dividend distribution of one Preferred Share Purchase Right (a "Right") for each outstanding share of the Company's Common Stock (see Note 10 of Notes to Consolidated Financial Statements).

Effective May 1, 2001, the Company issued and sold \$790,000,000 (including \$200,000,000 to cover over-allotments) of 20-year, zero-coupon, unsecured, convertible debt, Liquid Yield Option™ Notes ("LYONs," "debt" or "the securities"). The debt was issued at an original discount price of \$639.23 per \$1,000 maturity value and has a yield to maturity of 2.25%. The debt is senior unsecured obligations of the Company and is convertible into the Company's Common Stock at a fixed ratio of 8.2988 per \$1,000 maturity value or an effective conversion price of \$77.03 at the date of issuance. Under the terms of the issue, the conversion rate may be adjusted for certain reasons, but will not be adjusted for accrued original issue discount.

In January 2001, the Company's shareholders approved increases in (i) the number of the Company's authorized Common Stock from 50,000,000 shares to 200,000,000 shares and (ii) the number of shares of the Company's authorized no par value preferred stock from 5,000,000 shares to 20,000,000 shares.

The Company effected a two-for-one stock split of its Common Stock on December 15, 2000. Unless otherwise indicated, all references to the number of shares and to per-share information in the financial statements and related notes have been adjusted to reflect this stock split on a retroactive basis.

In October 2000, the Company completed the sale of 4,837,338 shares (including 1,200,000 shares to cover over-allotments) of its Common Stock in an underwritten public offering at a price of \$31.75 per share, less underwriting discounts and commissions. The net proceeds to the Company, less underwriting discounts and commissions and other offering expenses, totaled approximately \$144,800,000 and were used to pay amounts outstanding under the Company's primary revolving line of credit facility. The Company's primary revolving line of credit facility has been used to provide working capital and to fund fixed asset purchases and subsidiary acquisitions, including the Stone & Webster Incorporated ("Stone & Webster") acquisition (see Note 3 of Notes to Consolidated Financial Statements).

In September 2000, the Company retired 16,404,916 shares of treasury stock recorded at \$22,043,000.

In November 1999, the Company sold 6,900,000 shares (including over-allotments) of its Common Stock, no par value (the "Common Stock"), in an underwritten public offering at a price of \$10.50 per share, less underwriting discounts and commissions. The net proceeds to the Company, less underwriting discounts and commissions and other expenses of the offering, totaled approximately \$67,500,000 and were used to pay down amounts outstanding under the Company's primary revolving line of credit facility and certain other long-term debt.

Note 3—Acquisitions

Acquisitions completed by the Company and discussed below have been accounted for under the purchase method of accounting. Under the purchase method, the cost of each acquired operation is allocated to the assets acquired and liabilities assumed based on their estimated fair values. These estimates are revised during the allocation period as necessary when, and if, information becomes available to further define and quantify the value of the assets acquired and liabilities assumed. The allocation period does not exceed beyond one year from the date of the acquisition. To the extent additional information to refine the original allocation becomes available during the allocation period, the allocation of the purchase price is adjusted. Likewise, to the extent such information becomes available after the allocation period, such items are included in the Company's operating results in the period that the settlement occurs or information is available to adjust the original allocation to a better estimate. These future adjustments, if any, that may arise from these acquisitions may materially impact the Company's future consolidated financial position or results of operations.

In connection with potential acquisitions, the Company incurs and capitalizes certain transaction costs, which include legal, accounting, consulting and other direct costs. When an acquisition is completed these costs are capitalized as part of the acquisition price. The Company routinely evaluates capitalized transaction costs and expenses those costs related to acquisitions that are not likely to occur. Indirect acquisition costs, such as salaries, corporate overhead and other corporate services are expensed as incurred.

The operating results of the acquisitions accounted for as a purchase are included in the Company's consolidated financial statements from the applicable date of the transaction.

Stone & Webster Acquisition On July 14, 2000, the Company purchased substantially all of the operating assets of Stone & Webster, a global provider of engineering, procurement, construction, consulting and environmental services to the power, process, environmental and infrastructure markets. The Company funded this acquisition with \$14,850,000 in cash (net of \$22,750,000 of funds returned from escrow) and 4,463,546 shares of Common Stock (valued at approximately \$105,000,000 at closing). The Company also assumed approximately \$740,000,000 of liabilities. The Company incurred approximately \$12,000,000 of acquisition costs. The purchase price was subject to various adjustments, and the final allocation is discussed below. Any future adjustments will be reflected in operating results.

The excess of the initial aggregate purchase price over the estimated fair market value of net tangible assets acquired was approximately \$300,000,000. During the allocation period following the acquisition, changes in the initial estimated purchase price allocation were appropriately adjusted through goodwill. The more significant changes in estimates are discussed below. The final allocation of cost resulted in an excess of the aggregate adjusted purchase price over the estimated fair market value of net tangible assets acquired of approximately \$381,000,000 (recorded as patents, licenses, other tangibles and goodwill). The following reflects the final allocation of the purchase price to the acquired assets and liabilities (in thousands):

Accounts receivable	\$ 150,720
Cost and estimated earnings in excess of billings on uncompleted contracts	37,406
Inventories	11,480
Assets held for sale	112,652
Patents, licenses and other intangible assets	28,600
Property and equipment	19,606
Deferred income taxes	87,451
Other assets	28,935
Goodwill	352,557
Accounts payable and accrued liabilities	(326,456)
Billings in excess of cost and estimated earnings on uncompleted contracts	(143,612)
Accrued contract losses and adjustments	(163,515)
Debt and bank loans	(92,497)
Other liabilities	(13,498)
<hr/>	
Purchase price (net of cash received of \$42,194)	\$ 89,829

For the year ended August 31, 2001 and 2000, goodwill amortization was approximately \$16,800,000 and \$1,800,000, respectively, and was amortized on a straight-line basis based on a 20-year estimated life. See Note 1 of Notes to Consolidated Financial Statements with respect to the impact of the Company's adoption of SFAS No. 142—"Goodwill and Other Intangibles" for the year ending August 31, 2002.

The acquisition was concluded as part of a proceeding under Chapter 11 of the U.S. Bankruptcy Code for Stone & Webster, Inc. In December 2000, the parties entered into an amendment to the initial acquisition agreement that: (i) returned approximately \$22,750,000 to the Company from escrow, (ii) waived the purchase price adjustment provision of the agreement, (iii) excluded four completed contracts from the transaction, and (iv) required the Company to assume three previously excluded items. This amendment was approved by the bankruptcy court and decreased the Company's purchase price and goodwill.

The Company believes that, pursuant to the terms of the acquisition agreement, it assumed only certain specified liabilities. The Company believes that liabilities excluded from this acquisition include liabilities associated with certain contracts in progress, completed contracts, claims or litigation that relate to acts or events occurring prior to the acquisition date, and certain employee benefit obligations, including Stone & Webster's U.S. defined benefit plan (collectively, the excluded items). The Company, however, cannot provide assurance that it has no exposure with respect to the excluded items because, among other things, the bankruptcy court has not finalized its validation of claims filed with the court. The final amount of assumed liabilities may change as a result of the validation of claims process; however, the Company believes, based on its review of claims filed, that any such adjustment to the assumed liabilities will not be material.

The Company acquired a large number of contracts with either inherent losses or lower than market rate margins primarily because Stone & Webster's previous financial difficulties had negatively affected the negotiation and execution of the contracts. These contracts were adjusted to their estimated fair value at acquisition date (July 14, 2000) and a liability (gross margin reserve) of \$121,815,000 was established, including adjustments of \$38,118,000 recorded during the one-year allocation period. The adjustment during the allocation period resulted from a more accurate determination of the actual contract status at acquisition date. The amount of the accrued future cash losses on assumed contracts with inherent losses (contract loss reserve) was estimated to be approximately \$41,700,000 (including adjustments totaling approximately \$5,400,000 recorded during the allocation period), and a liability of such amount was established. Both reserves are reduced as work is performed on the contracts and such reduction in the reserves results in a reduction in cost of sales and a corresponding increase in gross profit. Goodwill and deferred tax assets for the Stone & Webster acquisition were adjusted by \$43,518,000 due to the revisions to the original reserve estimates identified during the allocation period. These reserves and adjustments during the allocation period, as well as the decreases in the cost of sales for the periods indicated, are as follows (in thousands):

	July 14, 2000 Balance	Reserve Increase	Cost of Sales (Decrease)	August 31, 2000 Balance
Year ended August 31, 2000				
Gross margin reserves	\$ 83,697	\$ —	\$ (7,933)	\$ 75,764
Contract loss reserves	36,300	—	(5,575)	30,725
Total	\$119,997	\$ —	\$(13,508)	\$106,489
	September 1, 2000 Balance	Reserve Increase	Cost of Sales (Decrease)	August 31, 2001 Balance
Year ended August 31, 2001				
Gross margin reserves	\$ 75,764	\$38,118	\$(70,081)	\$ 43,801
Contract loss reserves	30,725	5,400	(29,219)	6,906
Total	\$106,489	\$43,518	\$(99,300)	\$ 50,707

The Company acquired several contracts under which Stone & Webster was contractually obligated to pay liquidated damages or for which the scheduled project completion date was beyond the contract completion date agreed to with the customer, which would require the Company to pay liquidated damages upon completion of the project. In addition, several acquired contracts contain warranty provisions requiring achievement of acceptance and performance testing levels or payment of filed liens or claims on the project. The Company recorded reserves of approximately \$42,000,000 at acquisition date related to these contracts. No payments have been made on these amounts as the contracts are still in progress. Payments are anticipated upon completion of the contract or during the warranty periods. The ultimate amount of these payments may vary depending upon the actual completion date compared to the current scheduled completion date, the amount needed to resolve the performance requirements, and final negotiations with the customers or lien holders. To the extent the final settlement or payment amount is different than the reserve established, the difference will be reflected in results of operations in the period the difference is known.

Property and equipment acquired in the Stone & Webster acquisition included software and other assets that required a reassessment of their fair value. During the one-year allocation period, this assessment was completed and the purchase price allocated to property and equipment was reduced from Stone & Webster's net book value of \$48,779,000 to \$19,606,000. A corresponding adjustment was made that increased goodwill by \$29,173,000.

The Company also acquired various licenses, patents, technology and related processes pertaining to the design and construction of ethylene plants. The Company assigned an estimated value of \$50,000,000 in its preliminary allocation as of the date of acquisition pending completion of an appraisal of these assets. During the allocation period, the appraisal was completed which valued these assets at \$28,600,000 based on estimates of the discounted cash flows to be generated from the existing acquired technology. An adjustment has been made to increase goodwill by \$21,400,000, representing the difference between the original estimated value of the technology at the time of the Stone & Webster acquisition and the above appraised value. The estimated useful lives of these intangible assets are 15 years.

The Company also assumed certain liabilities pursuant to severance and change in control agreements for certain former Stone & Webster executives, and the Company recorded an acquisition liability of approximately \$22,400,000 for amounts due to executives who were not retained. During the year ended August 31, 2001, the Company settled all of the Stone & Webster executive severance liabilities and reduced this reserve by approximately \$5,000,000. Goodwill and deferred taxes were adjusted to reflect the difference between the Company's initial estimated liability for executive severance payments and its final payment requirements.

Included in this acquisition was a cold storage and frozen food handling operation which Stone & Webster had previously reported as a discontinued operation. The Company classified the operation as assets held for sale until the Company sold all of these assets (other than cash) for \$69,364,000 (net of various purchase price adjustments) in December 2000. Losses, net of taxes, of approximately \$1,397,000 and \$332,000 from this operation's results, which includes allocated interest expense of approximately \$2,387,000 and \$1,000,000, have been excluded from the Company's Statements of Income for the years ended August 31, 2001 and 2000, respectively. These losses were included in the Company's allocation of purchase price to the acquired assets and liabilities. In connection with the sale of these assets, the Company also acquired an approximate 19.5% equity interest in the purchaser of the assets for an investment of \$1,930,000, which is accounted for under the cost method. Additionally, in December 2000, the Company completed the sale of an office building located in Houston, Texas which was acquired in the Stone & Webster acquisition and realized net proceeds of approximately \$21,100,000 after paying off the mortgage of approximately \$19,700,000. The proceeds from these asset disposals were used to pay down the Company's primary credit facility.

The following summarized unaudited pro forma income statement data reflects the impact the Stone & Webster acquisition would have had on fiscal 2000, had the acquisition taken place at the beginning of the fiscal year (in thousands, except per share data):

	Unaudited Pro Forma Results for the Year Ended August 31, 2000
Gross revenue	\$1,643,000
Loss from continuing operations	\$ (10,000)
Basic earnings from continuing operations per common share	\$ (0.61)
Diluted earnings from continuing operations per common share	\$ (0.61)

The unaudited pro forma results for the year ended August 31, 2000 has been prepared for comparative purposes only and does not purport to be indicative of the amounts which actually would have resulted had the acquisition occurred on September 1, 1999, or which may result in the future.

Other Acquisitions In March 2001, the Company acquired the assets and certain liabilities of Scott, Sevin & Schaffer, Inc. and Technicomp, Inc. (collectively "SS&S"). As of August 31, 2001, the Company had issued 170,683 shares (including purchase price protection reduced by purchase price adjustment settlements) of its Common Stock (valued at approximately \$6,300,000) as consideration for the transaction and 13,800 of the issued shares were escrowed to secure certain indemnities provided by the seller. The Company also incurred approximately \$160,000 of acquisition costs. This acquisition was accounted for under the purchase method of accounting and approximately \$4,300,000 of goodwill was recorded. For the year ended August 31, 2001, goodwill for this acquisition was amortized on a straight-line basis based on a 20-year estimated life. See Note 1 of Notes to Consolidated Financial Statements with respect to the impact of the Company's adoption of SFAS No. 142—"Goodwill and Other Intangibles" on September 1, 2001. SS&S's primary business is structural steel, vessel, and tank fabrication.

On July 12, 2000, the Company completed the acquisition of certain assets and assumption of liabilities of PPM Contractors, Inc. ("PPM"). Total consideration paid was 86,890 shares of the Company's Common Stock valued at \$2,012,000 and the assumption of certain liabilities. Acquisition costs were not material. The purchase method was used to account for the acquisition and goodwill of approximately \$2,100,000 was recorded. For the years ended August 31, 2001 and 2000, goodwill for this acquisition was amortized on a straight-line basis based on a 20-year estimated life. See Note 1 of Notes to Consolidated Financial Statements with respect to the impact of the Company's adoption of SFAS No. 142—"Goodwill and Other Intangibles" on September 1, 2001. PPM's primary business is providing sandblasting and painting services to industrial customers.

The pro forma effects of these other acquisitions as though they had occurred as of the beginning of the immediate preceding fiscal year is not material to the operations of the Company.

Note 4—Inventories

The major components of inventories consist of the following (in thousands):

	August 31,					
	2001			2000		
	Weighted Average	FIFO	Total	Weighted Average	FIFO	Total
Finished Goods	\$33,126	\$ —	\$33,126	\$36,158	\$ —	\$36,158
Raw Materials	2,380	46,511	48,891	2,270	45,175	47,445
Work In Process	948	8,190	9,138	1,626	11,054	12,680
	\$36,454	\$54,701	\$91,155	\$40,054	\$56,229	\$96,283

Note 5—Investment in Unconsolidated Entities

The Company owns 49% of Shaw Nass Middle East, W.L.L., a joint venture in Bahrain (“Shaw Nass”) which is accounted for on the equity basis. During the years ended August 31, 2001, 2000 and 1999, the Company recognized earnings of \$250,000, \$1,194,000 and \$681,000, respectively, from Shaw Nass. No distributions have been made through August 31, 2001 by Shaw Nass. At August 31, 2001, undistributed earnings of Shaw Nass included in the consolidated retained earnings of the Company amounted to approximately \$2,419,000. As of August 31, 2001 and 2000, the Company’s investment in Shaw Nass was approximately \$6,090,000 and \$5,840,000, respectively, and the Company had outstanding receivables from Shaw Nass totaling \$6,178,000 and \$5,871,000, respectively. These receivables relate primarily to inventory and equipment sold and net advances and are recorded as long-term advances to Shaw Nass. The Company did not make any equity contributions during the fiscal years ended August 31, 2001 and 2000.

During the years ended August 31, 2001, 2000 and 1999, revenues of \$230,000, \$19,000 and \$1,188,000, were recognized on sales of products from the Company to Shaw Nass. The Company’s 49% share of profit on these sales was eliminated.

In fiscal 2001, the Company and Entergy Corporation (“Entergy”) formed EntergyShaw, L.L.C. (“EntergyShaw”), an equally-owned and equally-managed company. EntergyShaw’s initial focus is the construction of power plants in North America and Europe for Entergy’s wholesale operations. The Company believes that EntergyShaw, subject to the approval of its joint-management committee, will manage the construction of most of these power plants. Additionally, under the terms of the arrangement, the Company will offer EntergyShaw a right of first refusal to contract for bundled engineering, procurement, and construction (“EPC”) services. This right of first refusal does not apply to project inquiries related to services other than fully bundled EPC projects. In any event, the Company expects to provide EPC services and pipe fabrication for substantially all of EntergyShaw’s power generation projects.

During the year ended August 31, 2001, the Company made an initial investment in EntergyShaw of \$2,000,000. The Company has recognized losses of \$566,000 (net of a tax benefit of \$354,000) from EntergyShaw during the year ended August 31, 2001. During fiscal 2001, the Company had sales to EntergyShaw of approximately \$17,080,000. In addition, as of August 31, 2001, the Company’s investment in EntergyShaw was \$1,080,000 and it had outstanding trade accounts receivable from EntergyShaw totaling approximately \$4,848,000. Other than its initial \$2,000,000 investment, the Company has no further capital contribution commitments to EntergyShaw.

In connection with the December 2000 sale of a cold storage and frozen food handling operation that was included in the Stone & Webster acquisition, the Company acquired an approximate 19.5% equity interest in the purchaser of the assets for an investment of \$1,930,000. Since this equity interest is less than 20% and the Company does not exert any significant influence over the management of the operations, the Company will not recognize any income from this operation other than cash distributions. No such distributions have been made since its acquisition.

As is common in the engineering, procurement and construction industries, the Company executed certain contracts jointly with third parties through joint ventures, limited partnerships and limited liability companies. The investments are included on the accompanying consolidated balance sheet as of August 31, 2001 and 2000 are \$10,966,000 and \$8,650,000, respectively, which generally represents the Company's cash contributions and earnings from these investments.

Note 6—Investment In Securities Available for Sale

In December 1998, the Company participated in a customer's project financing by acquiring \$12,500,000 of 15% Senior Secured Notes due December 1, 2003 (the "15% Notes"), and preferred stock related thereto issued by the customer for the face value of the notes. The 15% Notes were originally secured by a first priority security interest in certain assets of the customer's Norco, Louisiana refinery where the Company provided construction services.

In November 1999, the Company exchanged its 15% Notes for (i) \$14,294,535 (representing the principal and accrued interest on the Company's 15% Notes) of 10% Senior Secured Notes due November 15, 2004 (the "New Notes"), and (ii) shares of the customer's Class A Convertible Preferred Stock. This exchange was made pursuant to an offer initiated by the customer to all holders of the 15% Notes (aggregating approximately \$254,000,000 in principal and interest). The 10% interest rate on the New Notes will increase to 14% on November 16, 2003 until maturity. Through November 15, 2003, the Company expects to receive additional New Notes in lieu of interest payments. The New Notes have little market liquidity.

The Company participated in the New Notes exchange offer because, upon receipt of the requisite approval by the holders of the 15% Notes, the collateral securing the 15% Notes would be released. All holders of the 15% Notes participated in the New Notes exchange offer.

Prior to the exchange offer, the Company's customer issued additional Common Stock, raising \$50,000,000 in additional equity, and obtained additional secured indebtedness of approximately \$150,000,000, which ranked senior to both the 15% Notes and the New Notes. As such, the security interest in the refinery assets securing the New Notes is subordinate to the security interest securing such additional indebtedness.

During fiscal 2001, the Company used \$7,000,000 of the New Notes to satisfy certain liabilities related to the acquisition of Stone & Webster. The Company has classified the New Notes as available for sale and, therefore, the New Notes are measured at fair value, which the Company believes approximates the face value of the New Notes. The New Notes had an aggregate value of \$9,079,000 and \$15,236,000 at August 31, 2001 and 2000, respectively. The financing arrangement was related to construction services that were completed prior to the end of the first quarter of fiscal 2001. Accordingly, during the years ended August 31, 2001, 2000 and 1999, interest income of approximately \$312,000, \$1,406,000 and \$1,330,000, respectively, from these securities were included in sales, and imputed interest costs associated with carrying the securities of approximately \$381,000, \$1,106,000 and \$621,000, respectively, were included in cost of sales. The remaining interest income earned during fiscal 2001 from these securities, amounting to \$531,000, is included in other income. The interest cost was calculated at the Company's effective borrowing rate, which approximated 9.8% for the three month period ended November 30, 2000, and 7.6% and 7.0% for the twelve months ended August 31, 2000 and 1999, respectively.

In November 1999, the Company also exchanged the related preferred stock for shares of new Class C Convertible Preferred Stock, the amount and value of which are not material.

The Company also had equity securities available for sale aggregating \$1,411,000 and \$1,125,000 at August 31, 2001 and 2000, respectively. At August 31, 2001, the Company reflected a \$12,000 unrealized loss (\$7,000, net of related taxes) on certain of these securities as a component of other comprehensive income in stockholders' equity. The unrealized loss relates to a temporary decrease in the value of these securities from their historical cost. The Company also reclassified a loss of \$942,000 (\$576,000, net of related taxes) to net income during the year ended August 31, 2001, due to an impairment loss on securities acquired in the Stone & Webster acquisition. As of August 31, 2000, no unrealized or realized gains or losses had been recorded on the securities held for sale.

Note 7—Long-Term Debt

Long-term debt consisted of (dollars in thousands):

	August 31,	
	2001	2000
Convertible Liquid Yield Option™ Notes, unsecured, zero coupon, 2.25% interest, due May 1, 2021, with early redemption options by the holder	\$508,780	\$ —
Note payable to a finance company, interest payable monthly at 6.15% and 7.52%; monthly payments of \$311 and \$175, through January 2002 and May 2001, respectively; unsecured (annual renewal)	1,530	1,530
Note payable to a bank; interest payable quarterly at 7.23%; quarterly payments of \$52 through April 2005; secured by equipment with an approximate net book value of \$519 as of August 31, 2001	677	828
Note payable to a former employee relating to a non-competition agreement; interest payable monthly at 7.125%; monthly payments of \$21 until April 2004; unsecured; see Note 16—Related Party Transactions	605	804
Note payable to an insurance company, interest payable at 6.44%; secured by assets held for sale with an approximate net book value of \$42,000 at August 31, 2000	—	19,728
Notes payable to a finance company; variable interest rates based on 30-day commercial paper rates plus 190 to 235 basis points ranging from 7.41% to 8.38% as of August 31, 2000; payable in monthly installments based on amortization over the respective note lives; maturing from 2001 to 2006; secured by property and equipment with an approximate net book value of \$10,645 as of August 31, 2000 and guaranties by the Company and certain subsidiaries of the Company	—	5,816
Note payable to a mortgage company, interest payable monthly at 7.20%; monthly payments of \$35 through June 2019 secured by land, buildings and equipment with an approximate net book value of \$7,251 at August 31, 2000	—	4,280
South Carolina Revenue Bonds payable; principal due in 2005; interest paid monthly accruing at a variable rate of 3.60% as of August 31, 2000; secured by a \$4,000 letter of credit	—	4,000
Note payable to a bank; interest payable quarterly based upon London Interbank Offering Rate (“LIBOR”) plus 1.6%; payable in quarterly principal installments of \$264 with remaining balance due in June 2003; secured by equipment with an approximate net book value of \$8,591 as of August 31, 2000	—	3,171
Notes payable to former owners of Cojafex in conjunction with an acquisition; payable in annual installments of \$750 (including interest imputed at 6.56%) through December 31, 2003; secured by the stock of the acquired subsidiary	—	2,566
Note payable to a bank; variable interest rate based upon London Interbank Offering Rate (“LIBOR”) plus 1.4%; payable in quarterly principal installments of \$143 through July 2004 plus interest; secured by equipment with an approximate net book value of \$1,515 as of August 31, 2000	—	2,143
Notes payable to a bank and finance company; interest rates ranging from 7.82% to 9.25%; payable in monthly installments based on amortization over the respective note lives; maturing from 2000 to 2009; secured by property and equipment with an approximate net book value of \$661 as of August 31, 2000	—	730
Other notes payable; interest rates ranging from 0% to 7.0%; payable in monthly installments based on amortization over the respective note lives; maturing in 2002 and 2003	457	185
Total debt	512,049	45,781
Less: current maturities	(2,365)	(26,654)
Total long-term portion of debt	\$509,684	\$ 19,127

Annual maturities of long-term debt during each year ending August 31 are as follows (in thousands):

	Total
2002	\$ 2,365
2003	404
2004	509,130
2005	150
2006 and thereafter	—
Total	\$512,049

Effective May 1, 2001, the Company issued and sold \$790,000,000 (including \$200,000,000 to cover over-allotments) of 20-year, zero-coupon, unsecured, convertible debt, Liquid Yield Option™ Notes (“LYONs,” “debt” or “the securities”). The debt was issued at an original discount price of \$639.23 per \$1,000 maturity value and has a yield to maturity of 2.25%. The debt is senior unsecured obligations of the Company and is convertible into the Company’s Common Stock at a fixed ratio of 8.2988 per \$1,000 maturity value or an effective conversion price of \$77.03 at the date of issuance. Under the terms of the issue, the conversion rate may be adjusted for certain factors as defined in the agreement including but not limited to dividends or distributions payable on Common Stock, but will not be adjusted for accrued original issue discount. The Company realized net proceeds, after expenses, from the issuance of these securities of approximately \$490,000,000. The Company used these proceeds to retire outstanding indebtedness and for general corporate purposes, including investment in AAA rated, short-term marketable securities held until maturity and cash equivalents.

The holders of the debt have the right to require the Company to repurchase the debt on the third, fifth, tenth and fifteenth anniversaries at the then accreted value. The debt is reflected in the preceding maturity table as maturing at the first repurchase date. The Company has the right to fund such repurchases with shares of its Common Stock, cash, or a combination of Common Stock, at the current market value, and cash. The debt holders also have the right to require the Company to repurchase the debt for cash, at the accreted value, if there is a change in control of the Company, as defined, occurring on or before May 1, 2006. The Company may redeem all or a portion of the debt at the accreted value, through cash payments, at any time after May 1, 2006.

The estimated fair value of long-term debt as of August 31, 2001 and 2000 was approximately \$422,000,000 and \$46,700,000, respectively. The fair value of the convertible debt as of August 31, 2001 was based on recent sales of such debt as of August 31, 2001. The fair value of the Company’s other long-term debt at August 31, 2001 and August 31, 2000 were based on borrowing rates currently available to the Company for notes with similar terms and average maturities.

During fiscal 2001 and 2000, the Company recognized, as interest expense, \$5,808,000 and \$411,000, respectively, of costs associated with the amortization of financing fees which were incurred with respect to initiation of the Company’s LYONs and Credit Facility. The LYONs costs are being amortized to the first repurchase date of the debt. As of August 31, 2001 and 2000, unamortized deferred financing fees of the Company’s LYONs debt and Credit Facility were approximately \$20,923,000 and \$10,112,000, respectively.

Note 8—Revolving Lines of Credit

The Company’s primary credit facility is a three-year term, \$300,000,000 credit facility (“Credit Facility”) dated July 2000 that permits both revolving credit loans and letters of credit, which letters of credit cannot exceed \$150,000,000. The Company has the option to increase the Credit Facility under existing terms to \$400,000,000, if certain conditions are satisfied, including the successful solicitation of additional lenders or increased participation of existing lenders. The Credit Facility allows the Company to borrow either at interest rates in a range of 1.50% to 2.75% over the London Interbank Offered Rate (“LIBOR”) or from the prime rate to 1.25% over the prime rate. The Company selects the interest rate index and the spread over the index is dependent upon certain financial ratios of the Company. The Credit Facility is secured by, among other things, (i) guarantees by the Company’s domestic subsidiaries; (ii) a pledge of all of the capital stock in the Company’s domestic subsidiaries and 66% of the capital stock in certain of the Company’s foreign subsidiaries; and (iii) a security interest in all property of the Company and its domestic subsidiaries (except real estate and equipment). The Credit Facility also contains restrictive covenants, which include ratios, minimum capital levels, limits on other borrowings and other restrictions. As of August 31, 2001, the Company was in compliance with these covenants or had obtained the necessary waivers, had no outstanding revolving credit loans, and letters of credit of approximately \$61,500,000 were outstanding under the Credit Facility. The Company’s total availability under the Credit Facility at August 31, 2001 was approximately \$238,500,000, which included availability for letters of credit of approximately \$88,500,000. At August 31, 2001, the interest rate on this line of credit was either 6.5% (if the prime rate index had been chosen) or 5.26% (if the LIBOR rate index had been chosen).

As of August 31, 2001, the Company’s foreign subsidiaries had short-term revolving lines of credit permitting borrowings totaling approximately \$16,200,000. These subsidiaries had outstanding borrowings under these lines of credit of approximately \$3,900,000 at a weighted average interest rate of 6.0% at August 31, 2001.

Note 9—Income Taxes

The significant components of deferred tax assets and liabilities are as follows (in thousands):

	August 31,	
	2001	2000
Assets:		
Tax basis of inventory in excess of book basis	\$ 125	\$ 535
Receivables	6,442	8,824
Self-insurance reserves	—	238
Net operating loss and tax credit carryforwards	26,853	1,976
Accrued severance	205	8,978
Contract reserves	20,868	40,306
State tax credits	—	150
Other expenses not currently deductible	6,613	6,826
Less: valuation allowance	—	(670)
Total assets	61,106	67,163
Liabilities:		
Property, plant and equipment	(7,736)	(7,636)
Employee benefits	(7,266)	(1,767)
Total liabilities	(15,002)	(9,403)
Net deferred tax assets	\$ 46,104	\$57,760

Income (loss) before provision for income taxes for the years ended August 31 was as follows (in thousands):

	2001	2000	1999
Domestic	\$104,361	\$ 45,532	\$27,663
Foreign	(4,467)	16	(1,588)
Total	\$ 99,894	\$ 45,548	\$26,075

The provision for income taxes for the years ended August 31 was as follows (in thousands):

	2001	2000	1999
Current—Federal	\$ —	\$ 13,549	\$ 4,534
Deferred	36,863	1,805	3,697
State	1,503	1,005	404
Total	\$ 38,366	\$ 16,359	\$ 8,635

A reconciliation of Federal statutory and effective income tax rates for the years ended August 31 was as follows:

	2001	2000	1999
Statutory rate	35%	35%	35%
State taxes provided	(1)	2	1
Foreign income taxed at different rates	(3)	(3)	(2)
Non-deductible goodwill	7	—	—
Other	—	2	1
State tax credits	—	—	(2)
	38%	36%	33%

As of August 31, 2001, for Federal income tax return purposes, the Company had approximately \$66,657,000 of U.S. net operating loss carryforwards available to offset future taxable income. The carryforwards expire beginning in 2011 through 2020. As of August 31, 2001, the Company's United Kingdom ("U.K.") operations had net operating loss carryforwards of approximately £1,066,000 (\$1,554,000), which can be used to reduce future taxable income in the U.K. As of August 31, 2001, a benefit of \$466,200 had been given to these losses in the accompanying financial statements.

Unremitted foreign earnings reinvested abroad upon which deferred income taxes have not been provided aggregated approximately \$6,296,000 at August 31, 2001. Due to the timing and circumstances of repatriation of such earnings, if any, it is not practicable to determine the unrecognized deferred tax liability relating to such amounts. Withholding taxes, if any, upon repatriation would not be significant.

Note 10—Common Stock

The Company has one class of Common Stock. Each outstanding share of Common Stock, which has been held for four consecutive years without an intervening change in beneficial ownership, entitles its holder to five votes on each matter properly submitted to the Company's shareholders for their vote, waiver, release or other action. Each outstanding share of Common Stock which has been held for less than four consecutive years entitles its holder to only one vote.

On July 31, 2001, the Company distributed a dividend distribution of one Preferred Share Purchase Right (a "Right") for each outstanding share of the Company's Common Stock outstanding on that date. The Rights, which expire on July 9, 2011, will not prevent a takeover, but are designed to deter coercive or unfair takeover tactics, and are, therefore, intended to enable all Company shareholders to realize the long-term value of their investment in the Company. It is anticipated that the Rights will encourage anyone seeking to acquire the Company to negotiate with the Board of Directors prior to attempting a takeover.

The Rights, which are governed by a Rights Agreement dated July 9, 2001, between the Company and First Union National Bank, as Rights Agent, should not interfere with a merger or other business combination approved by the Company's Board of Directors.

The Rights are attached to the Company's Common Stock and are exercisable only if a person or group (an "Acquiring Person") either (i) acquires 15% or more of the Company's Common Stock or (ii) commences a tender offer, the consummation of which would result in ownership by the Acquiring Person of 15% or more of the Common Stock. The Board of Directors is authorized to reduce the 15% threshold to not less than 10% of the Common Stock.

In the event the Rights become exercisable, each Right will entitle shareholders (other than the Acquiring Person) to buy one one-hundredth of a share of a new series of junior participating preferred stock ("Preferred Shares") at an exercise price of \$170.00 (the "Exercise Price"). The Exercise Price is subject to certain anti-dilution adjustments. Each one one-hundredth of a Preferred Share will give the stockholder approximately the same dividend, voting and liquidation rights as would one share of Common Stock.

In lieu of Preferred Shares, each Right holder (other than the Acquiring Person) will be entitled to purchase from the Company at the Right's then-current Exercise Price, shares of the Company's Common Stock having a market value of twice such Exercise Price. In addition, if the Company is acquired in a merger or other business combination transaction after a person has acquired 15% or more of the Company's outstanding Common Stock, each Right will entitle its holder to purchase at the Right's then-current Exercise Price, a number of the acquiring company's common shares having a market value of twice such Exercise Price, in lieu of acquiring Preferred Shares.

Further, after a group or person becomes an Acquiring Person, but prior to acquisition by such person of 50% or more of the Company's Common Stock, the Board of Directors may exchange all or part of the Rights (other than the Rights held by the Acquiring Person) for shares of Common Stock at an exchange ratio of one share of Common Stock for each Right.

Prior to the acquisition by an Acquiring Person of 15% or more of the Company's Common Stock, the Rights are redeemable for \$0.01 per Right at the option of the Board of Directors.

Note 11—Leases

Capital Leases The Company leases furniture and fixtures and transportation equipment under various non-cancelable lease agreements. Minimum lease rentals have been capitalized and the related assets and obligations recorded utilizing various interest rates. The assets are amortized using the straight-line method over either the estimated useful lives of the assets or the lease terms, and interest expense is accrued on the basis of the outstanding lease obligations.

Assets acquired under capital leases—net of accumulated amortization are as follows (in thousands):

	August 31,	
	2001	2000
Transportation equipment	\$ 61	\$ 61
Furniture and fixtures	1,366	1,366
Machinery and equipment	127	127
Construction in progress	6,251	—
	7,805	1,554
Less accumulated depreciation	(744)	(251)
	\$7,061	\$1,303

The following is a summary of future obligations under capital leases (in thousands):

	Minimum Lease Payments
For the year ending August 31:	
2002	\$2,710
2003	2,450
2004	1,005
2005	—
2006 and thereafter	—
Total payments	6,165
Less: amount representing interest	(669)
Total debt	5,496
Less: current portion	2,313
Total long-term portion of debt	\$3,183

The Company leases certain offices, fabrication shops, warehouse facilities, office equipment and machinery under non-cancelable operating lease agreements which expire at various times and which require various minimum rentals. The non-cancelable operating leases that were in effect as of August 31, 2001 require the Company to make the following estimated future minimum lease payments:

For the year ending August 31 (in thousands):	
2002	\$ 27,595
2003	30,200
2004	28,435
2005	25,889
2006	23,747
2007 and thereafter	106,176
Total future minimum lease payments	\$242,042

The Company has included in the table above the estimated lease payments on the Company's new corporate facilities. The final rental amounts, classification as operating or capital lease and certain other terms of the lease are not finalized; therefore, certain adjustments to the rental amounts may be made upon completion of the facilities which is expected to be finalized during the third quarter of fiscal 2002.

The Company enters into short-term lease agreements for equipment needed to fulfill the requirements of specific jobs. Any payments owed or committed under these lease arrangements as of August 31, 2001 are not included as part of total minimum lease payments. Rent expense for the fiscal years ended August 31, 2001, 2000 and 1999 was \$35,579,000, \$16,391,000 and \$8,297,000, respectively.

Note 12—Commitments and Contingencies

In the normal course of business activities, the Company enters into contractual agreements with customers for certain construction services to be performed based on agreed upon reimbursable costs and labor rates. In some instances, the terms of these contracts provide for the customer's review of the accounting and cost control systems to verify the completeness and accuracy of the reimbursable costs invoiced. These reviews could result in proposed reductions in reimbursable costs and labor rates previously billed to the customer. Additionally, the Company performs work for the U.S. Government that is subject to continuing financial and operating reviews by governmental agencies. The Company does not believe that any such reviews will result in a material change to the Company's financial position or results of operations.

The Company is self-insured for workers' compensation claims for individual claims up to \$250,000 and maintains insurance coverage for the excess. The Company has accrued a liability for its estimated workers' compensation claims totaling approximately \$1,200,000 and \$1,040,000 at August 31, 2001 and 2000, respectively. Additionally, the Company self-insures its employee health coverage up to certain annual individual and plan limits and maintains insurance coverage for the excess. The Company has accrued a liability of \$3,982,000 and \$1,381,000 at August 31, 2001 and 2000, respectively, for outstanding and incurred, but not reported, health claims.

In the normal course of its business, the Company becomes involved in various litigation matters including, claims by third parties for alleged property damages, personal injuries, and other matters. The Company has estimated its potential exposure, net of insurance coverage, and has recorded reserves in its financial statements as appropriate. The Company does not anticipate that the differences between its estimated outcome of these claims and future actual settlements could have a material effect on the Company's financial position or results of operations. See Note 3 of Notes to Consolidated Financial Statements with respect to certain contingencies relating to the Stone & Webster acquisition.

Note 13—Business Segments, Operations by Geographic Region and Major Customers

Business Segments The Company adopted SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information," as of August 31, 1999. SFAS No. 131 establishes standards for the way public business enterprises report information about operating segments in annual financial statements and requires those enterprises to report selected information about operating segments in interim financial reports issued to shareholders. It also establishes standards for related disclosures about products and services, geographic areas and major customers. SFAS No. 131 defined operating segments as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Company has aggregated its business activities into two operating segments: the integrated EPC services segment and the manufacturing and distribution segment.

The integrated EPC services segment is a vertically integrated provider of piping systems and comprehensive engineering, procurement, and construction services to the power generation, process, and environmental and infrastructure industries. These services include piping systems fabrication, engineering and design, construction, procurement and maintenance, and consulting.

The manufacturing and distribution segment manufactures and distributes specialty stainless, alloy and carbon steel pipe fittings. These fittings include elbows, tees, reducers and stub ends. The Company has one manufacturing facility that provides products for the Company's pipe services operations, as well as to third parties. The Company also has several distribution centers in the United States, which distribute its products primarily to third parties.

Business Segment Data The following table presents information about segment profit and assets (in thousands):

	Integrated EPC Services	Manufacturing and Distribution	Corporate	Total
Fiscal 2001				
Sales to external customers	\$1,462,876	\$76,056	\$ —	\$1,538,932
Intersegment sales	2,139	18,259	—	20,398
Corporate overhead allocations	26,681	4,399	(31,080)	—
Interest income	1,758	—	6,988	8,746
Interest expense	—	—	15,680	15,680
Depreciation and amortization	34,754	2,183	2,803	39,740
Earnings from unconsolidated entity	250	—	(566)	(316)
Income tax expense	40,081	2,947	(4,662)	38,366
Net income	64,117	5,687	(8,807)	60,997
Total assets	1,094,962	55,149	551,743	1,701,854
Investment in and advances to unconsolidated entities	12,268	—	1,080	13,348
Purchases of property and equipment	9,882	934	27,305	38,121
Other increases in long-lived assets, net	517	—	15,064	15,581
Fiscal 2000				
Sales to external customers	\$ 701,700	\$60,955	\$ —	\$ 762,655
Intersegment sales	23	15,343	—	15,366
Corporate overhead allocations	20,360	4,244	(24,604)	—
Interest income	185	—	497	682
Interest expense	203	—	7,800	8,003
Depreciation and amortization	13,354	2,192	1,262	16,808
Earnings from unconsolidated entity	1,194	—	—	1,194
Income tax expense	12,733	1,230	2,396	16,359
Net income	22,760	2,361	4,389	29,510
Total assets	1,209,792	64,612	60,679	1,335,083
Investment in and advances to unconsolidated entities	11,711	—	—	11,711
Purchases of property and equipment	11,383	737	8,499	20,619
Other increases in long-lived assets, net	—	288	10,950	11,238

	Integrated EPC Services	Manufacturing and Distribution	Corporate	Total
Fiscal 1999				
Sales to external customers	\$446,708	\$47,306	\$ —	\$494,014
Intersegment sales	—	19,914	566	20,480
Corporate overhead allocations	9,214	1,586	(10,800)	—
Interest income	234	4	227	465
Interest expense	3,906	1,323	3,420	8,649
Depreciation and amortization	10,431	2,028	812	13,271
Earnings from unconsolidated entity	681	—	—	681
Income tax expense	10,196	(64)	(1,497)	8,635
Net income	20,449	(165)	(2,163)	18,121
Total assets	319,904	54,833	32,325	407,062
Investment in and advances to unconsolidated entities	8,956	—	—	8,956
Purchases of property and equipment	9,441	869	7,657	17,967
Other increases in long-lived assets, net	66	—	48	114

Operations by Geographic Region The following tables present geographic sales and long-lived assets (in thousands):

	For the Years Ended August 31,		
	2001	2000	1999
Sales:			
United States	\$1,285,412	\$591,812	\$365,942
China	41,767	11,436	30,795
Other Asia/Pacific Rim countries	75,368	39,546	10,257
United Kingdom	71,598	63,886	49,822
Other European countries	14,799	1,288	160
South America	23,071	29,788	18,736
Middle East	3,039	4,382	10,181
Other	23,878	20,517	8,121
	\$1,538,932	\$762,655	\$494,014
Long-lived assets:			
United States	\$ 528,723	\$469,163	\$111,716
United Kingdom	33,791	38,778	12,639
Other foreign countries	32,809	25,946	21,117
	\$ 595,323	\$533,887	\$145,472

Sales are attributed to geographic regions based on location of the project or the ultimate destination of the product sold. Long-lived assets include all long-term assets, except those specifically excluded under SFAS No. 131, such as deferred income taxes and securities available for sale.

Information about Major Customers The Company's customers are principally major multi-national industrial corporations, independent and merchant power providers, governmental agencies and equipment manufacturers. For the year ended August 31, 2001, sales to U.S. Government agencies or corporations owned by the U.S. government totaled approximately \$183,000,000, or 12% of sales. For the year ended August 31, 2000, sales to a customer were \$85,000,000, or 11% of sales. Additionally, for the years ended August 31, 2000 and 1999, sales to a different customer amounted to \$83,400,000 (11% of sales) and \$67,700,000 (14% of sales), respectively.

Export Sales For the years ended August 31, 2001, 2000 and 1999, the Company has included as part of its international sales approximately \$167,000,000, \$49,000,000 and \$58,000,000, respectively, of exports from its domestic facilities.

Note 14—Earnings Per Common Share

The following table sets forth the computation of basic and diluted earnings per share (in thousands, except per share data):

	For the Years Ended August 31,		
	2001	2000	1999
Basic and Dilutive:			
Income available to common shareholders before extraordinary item and cumulative effect of change in accounting principle	\$61,212	\$30,383	\$18,121
Extraordinary item, net of taxes	(215)	(553)	—
Cumulative effect on prior years of change in accounting principle, net of taxes	—	(320)	—
Net income for basic and diluted computation	\$60,997	\$29,510	\$18,121
Weighted average common shares (basic)	40,127	29,636	23,869
Effect of dilutive securities:			
Stock options	1,595	1,002	842
Escrow shares	106	133	—
Adjusted weighted average common shares and assumed conversions (diluted)	41,828	30,771	24,711
Basic earnings per common share:			
Income before extraordinary item and cumulative effect of change in accounting principle	\$ 1.53	\$ 1.03	\$ 0.76
Extraordinary item, net of taxes	(0.01)	(0.02)	—
Cumulative effect on prior years of change in accounting principle, net of taxes	—	(0.01)	—
Net income per common share	\$ 1.52	\$ 1.00	\$ 0.76
Diluted earnings per common share:			
Income before extraordinary item and cumulative effect of change in accounting principle	\$ 1.46	\$ 0.99	\$ 0.73
Extraordinary item, net of taxes	—	(0.02)	—
Cumulative effect on prior years of change in accounting principle, net of taxes	—	(0.01)	—
Net income per common share	\$ 1.46	\$ 0.96	\$ 0.73

At August 31, 2001, approximately 2,209,000 incremental shares related to convertible debt were excluded from the calculation of diluted income per share because they were antidilutive. Additionally, the Company had approximately 7,500, 12,000 and 53,000 of stock options at August 31, 2001, 2000 and 1999, respectively, which were excluded from the calculation of diluted income per share because they were antidilutive.

Note 15—Employee Benefit Plans

The Company has a 1993 Employee Stock Option Plan (“1993 Plan”) under which both qualified and non-qualified options and restricted stock may be granted. As of August 31, 2001, approximately 3,844,000 shares of Common Stock were authorized for issuance under the 1993 Plan. The 1993 Plan is administered by a committee of the Board of Directors (the “Board”), which selects persons eligible to receive options and determines the number of shares subject to each option, the vesting schedule, the exercise price, and the duration of the option. Generally, the exercise price of any option granted under the 1993 Plan cannot be less than 100% of the fair market value on the date of grant and its duration cannot exceed 10 years. Both qualified options and non-qualified options have been granted under the 1993 Plan. The options awarded vest in 25% annual increments beginning one year from the date of award.

Shares of restricted stock are subject to risk of forfeiture during the vesting period. Restrictions related to these shares and the restriction terms are determined by the committee. Holders of restricted stock have the right to vote the shares. At August 31, 2000, there were 30,000 shares of restricted stock outstanding. During the fiscal year 2001, the stock restrictions were released or shares were forfeited. At August 31, 2001, there were no restricted shares of stock.

In conjunction with the Stone & Webster acquisition (see Note 3 of Notes to Consolidated Financial Statements), the Company established the Stone & Webster Acquisition Stock Option Plan ("Stone & Webster Plan"). The purpose of this plan was to award options to Company employees who were not officers of the Company, as defined in the plan documents, and who were either (a) employed by the Company as a result of the Stone & Webster acquisition or (b) instrumental to the Stone & Webster acquisition. At August 31, 2001, 1,071,000 shares of Common Stock were authorized for issuance under this plan. The Stone & Webster Plan is administered by a committee of the Board, which selects persons eligible to receive options and determines the number of shares subject to each option, the vesting schedule, the exercise price, and the duration of the option. The exercise price of any option granted under the Stone & Webster Plan cannot be less than 100% of the fair market value on the date of grant and its duration cannot exceed 10 years. Only non-qualified options have been granted under the Stone & Webster Plan. The options awarded vest in 25% annual increments beginning one year from the date of award.

During fiscal 2001, the Company established the 2001 Employee Incentive Compensation ("2001 Plan") under which both qualified and non-qualified stock options, stock appreciation rights and restricted stock may be granted. As of August 31, 2001, approximately 2,000,000 shares of Common Stock were authorized for issuance under the 2001 Plan. The 2001 Plan is administered by a committee of the Board, which selects persons eligible to receive options and determines the number of shares subject to each option, the vesting schedule, the exercise price, and the duration of the option. The exercise price of any option granted under the 2001 Plan cannot be less than 100% of the fair market value on the date of grant and its duration cannot exceed 10 years. Both qualified options and non-qualified options have been granted under the 2001 Plan. The options awarded vest in 25% annual increments beginning one year from the date of award.

All options and other grants issued under the Stone & Webster Plan and the 2001 Plan become fully exercisable upon a change in control of the Company.

In fiscal 1997, the Company adopted a Non-Employee Director Stock Option Plan ("Directors' Plan"). Members of the Board who are not or were not an officer or employee of the Company during the one-year period preceding the date the director is first elected to the Board are eligible to participate in the Directors' Plan. A committee of two or more members of the Board who are not eligible to receive grants under the Directors' Plan administer this plan. Upon adoption, options to acquire an aggregate of 40,000 shares of Common Stock were issued. These options vested in 25% annual increments beginning one year from the date of award. Additionally, each eligible director is granted an option to acquire 1,500 shares of Common Stock on an annual basis upon his election or re-election to the Board. These options vest one year after the date of award. A total of 150,000 shares of Common Stock have been authorized for issuance under the Directors' Plan.

In October 1995, the Financial Accounting Standards Board issued SFAS No. 123, "Accounting for Stock-Based Compensation," which is effective for the Company's fiscal year beginning September 1, 1996. Under SFAS No. 123, companies can either record expense based on the fair value of stock-based compensation upon issuance or elect to remain under the APB 25 method whereby no compensation cost is recognized upon grant if certain requirements are met. The Company has elected to continue to account for its stock-based compensation under APB 25. However, pro forma disclosures, as if the Company adopted the cost recognition requirements under SFAS No. 123, are presented below.

Had compensation cost been determined based on the fair value at the grant date consistent with the provisions of SFAS No. 123, the Company's net income and earnings per common share would have approximated the pro forma amounts below:

	For the Years Ended August 31,		
	2001	2000	1999
Net income before extraordinary item and cumulative effect of change in accounting principle (in thousands):			
As reported	\$61,212	\$30,383	\$18,121
Pro forma	\$57,396	\$29,491	\$17,398
Basic earnings per share before extraordinary item and cumulative effect of change in accounting principle:			
As reported	\$ 1.53	\$ 1.03	\$ 0.76
Pro forma	\$ 1.43	\$ 1.00	\$ 0.73
Diluted earnings per share before extraordinary item and cumulative effect of change in accounting principle:			
As reported	\$ 1.46	\$ 0.99	\$ 0.73
Pro forma	\$ 1.37	\$ 0.96	\$ 0.71

The pro forma effect on net earnings for fiscal 1999 is not representative of the pro forma effect on net earnings in future years because it does not take into consideration pro forma compensation expense related to grants prior to September 1, 1995.

The following table summarizes the activity in the Company's stock option plans:

	Shares	Weighted Average Exercise Price
Outstanding at September 1, 1998	836,492	\$ 6.733
Granted	2,172,500	\$ 4.410
Exercised	(65,000)	\$ 3.827
Canceled	(428,492)	\$ 8.463
Outstanding at August 31, 1999	2,515,500	\$ 4.527
Granted	2,116,000	\$20.722
Exercised	(580,764)	\$ 3.884
Canceled	(65,000)	\$ 4.188
Outstanding at August 31, 2000	3,985,736	\$13.198
Granted	115,000	\$36.904
Exercised	(606,863)	\$ 5.389
Canceled	(282,500)	\$13.186
Outstanding at August 31, 2001	3,211,373	\$15.503
Exercisable at August 31, 2001	883,373	\$13.648

As of August 31, 2001, 2000 and 1999, the number of shares relating to options exercisable under the stock option plans was 883,373, 450,986 and 525,500, respectively, and the weighted average exercise price of those options was \$13.648, \$5.703 and \$4.662, respectively.

The weighted average fair value at date of grant for options granted during the years ended August 31, 2001, 2000 and 1999 was \$21.40, \$12.02 and \$2.62 per share, respectively. The fair value of options granted is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions for the years ended August 31, 2001, 2000 and 1999, respectively: (a) dividend yield of 0.00%, 0.00% and 0.00%; (b) expected volatility of 60%, 60% and 65%; (c) risk-free interest rate of 5.3%, 6.2% and 5.1%; and (d) expected life of 5 years, 5 years and 5 years.

The following table summarizes information about stock options outstanding as of August 31, 2001:

Range of Exercise Price	Options Outstanding			Options Exercisable	
	Number Outstanding	Weighted Average Remaining Contract Life	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
\$ 3.37 –\$ 7.930	1,095,123	7.07 Yrs	\$ 4.222	350,123	\$ 4.225
\$ 7.93 –\$12.932	88,500	7.31 Yrs	\$10.053	56,000	\$10.524
\$12.93 –\$17.934	—	— Yrs	—	—	—
\$17.935–\$22.936	1,927,750	8.89 Yrs	\$20.929	477,250	\$20.928
\$22.93 –\$27.939	10,000	9.95 Yrs	\$24.590	—	—
\$27.94 –\$32.941	—	— Yrs	—	—	—
\$32.94 –\$37.943	20,000	9.08 Yrs	\$33.750	—	—
\$37.94 –\$42.945	55,000	9.37 Yrs	\$41.500	—	—
\$42.94 –\$47.948	7,500	9.42 Yrs	\$44.750	—	—
\$47.94 –\$52.960	7,500	9.53 Yrs	\$51.993	—	—
	<u>3,211,373</u>	8.24 Yrs	\$15.503	<u>883,373</u>	\$13.648

During 1994, the Company adopted a voluntary 401(k) profit sharing plan for substantially all employees who are not subject to collective bargaining agreements. The plan provides for the eligible employee to contribute from 1% to 15% of annual compensation, subject to an annual limit as determined under federal law, with the Company matching 50% of the employee's eligible contribution up to 6% of the employee's annual compensation. The Company's expense for this plan for the years ended August 31, 2001, 2000 and 1999 was approximately \$5,664,000, \$1,704,000 and \$1,278,000, respectively. The year ended August 31, 2000 total includes approximately \$195,000 related to the Stone & Webster subsidiary's 401(k) plan covering the period of July 14, 2000 to August 31, 2000. The Stone and Webster plan required the Company to contribute 25% of the employees' elective deferral to

the plan, up to 5% of eligible employees' annual compensation. The Stone and Webster plan was terminated as of August 31, 2000 and Stone & Webster employees were offered the opportunity to participate in the Company's 401(k) plan for the year ended August 31, 2001.

The Company has other defined contribution plans at certain of its domestic and foreign locations. These plans allow the employees to contribute a portion of their earnings with the Company matching a percentage of the employee's contributions. The amounts contributed by the Company and employee vary by plan. The Company's expense for these plans was approximately \$702,000, \$323,000 and \$178,000 for the years ended August 31, 2001, 2000 and 1999, respectively.

The Company's subsidiaries in the U.K. and Canada have defined benefit plans covering their employees. The first U.K. plan was acquired November 14, 1997 through an acquisition. It is a salary-related plan for certain employees and admittance to this plan is now closed. The employees in this plan contribute 7% of their salary. The Company contribution depends on length of service, the employee's salary at retirement, and the earnings of the fund investments. If the plan's earnings are sufficient, the Company makes no contributions. The Canadian plan and second U.K. plan were acquired July 14, 2000 in conjunction with the Stone & Webster acquisition. The Canadian plan is noncontributory and the benefits are based primarily on years of service and employees' career average pay; admittance to this plan is now closed. The Company's policy is to make contributions equal to the current year cost plus amortization of prior service cost. The second U.K. plan is contributory and the benefits are based primarily on years of service and employees' average pay during their last ten years of service. For the years ended August 31, 2001, 2000 and 1999, the Company recognized income of approximately \$533,000, \$145,000 and \$18,000, respectively, for these plans.

Included in the amounts for the year ended August 31, 2001 and 2000 are the two pension plans assumed by the Company in the Stone & Webster acquisition. The projected benefit obligation of these two plans at the date of the acquisition of \$59,821,000 and the fair value of the assets at the date of acquisition of \$63,419,000 are included in the table below at the start of the 2000 fiscal year.

The following table sets forth the pension cost for the first U.K. plan and the two pension plans assumed by the Company in the Stone & Webster acquisition (from the date of acquisition to August 31, 2001), and the plans' funded status as of August 31, 2001, 2000 and 1999 in accordance with the provisions of SFAS No. 132—"Employers' Disclosure about Pensions and Other Postretirement Benefits" (in thousands):

	For the Years Ended August 31,		
	2001	2000	1999
Change in Projected Benefit Obligation			
Projected benefit obligation at the start of the year	\$75,593	\$17,149	\$17,133
Projected benefit obligations acquired in the Stone & Webster acquisition	—	59,821	—
Service cost	1,865	458	253
Interest cost	4,675	1,435	914
Member's contributions	659	218	132
Actuarial loss/(gain)	403	432	—
Benefits paid	(4,114)	(971)	(452)
Foreign currency exchange rate changes	(555)	(2,949)	(831)
Projected benefit obligation at the end of the year	78,526	75,593	17,149
Change in Plan Assets			
Fair value of the assets at the start of the year	82,013	19,296	17,437
Fair value of assets acquired in the Stone & Webster acquisition	—	63,419	—
Actual return on plan assets	(6,137)	2,861	2,949
Employer contributions	1,868	457	111
Employee contributions	659	218	132
Benefits paid	(4,114)	(971)	(452)
Foreign currency exchange rate changes	(735)	(3,267)	(881)
Fair value of the assets at the end of the year	73,554	82,013	19,296
Funded status	(4,972)	6,420	2,147
Unrecognized net loss/(gain)	10,147	(1,378)	(1,146)
Prepaid benefit cost	\$ 5,175	\$ 5,042	\$ 1,001

For the Years Ended August 31,

	2001	2000	1999
Weighted Average Assumptions			
Discount rate at end of the year	6.0–6.5%	5.5–6.5%	5.5%
Expected return on plan assets for the year	8.0–8.75%	7.0–8.75%	7.0%
Rate of compensation increase at end of the year	4.5–5.0%	4.5–5.0%	4.5%
Components of Net Periodic Benefit Cost			
Service cost	\$ 1,865	\$ 458	\$ 253
Interest cost	4,675	1,435	914
Expected return on plan assets	(6,924)	(2,038)	(1,185)
Other	(149)	—	—
Total net periodic benefit cost (income)	\$ (533)	\$ (145)	\$ (18)

The Company has a defined benefit pension plan for employees of its Connex subsidiary. Effective January 1, 1994, no new participants were admitted to the plan. The pension plan's benefit formulas generally base payments to retired employees upon their length of service. The pension plan's assets are invested in fixed income assets, equity based mutual funds, and money market funds. At August 31, 2001 and 2000, the fair market value of the plan assets was \$1,355,000 and \$1,646,000, respectively, which exceeded the estimated projected benefit obligation.

Note 16—Related Party Transactions

The Company has entered into employment agreements with its Chief Executive Officer, Chief Operating Officer and Chief Financial Officer. Under the terms of the agreements, the executives are entitled to receive their base salaries, bonuses and other employee benefit plans and programs for the periods of time specified therein. In the event of termination of employment as a result of certain reasons (including a change in control of the Company), the executives will be entitled to receive their base salaries and certain other benefits for the remaining term of their agreement and all options and similar awards shall become fully vested. Additionally, in the event of an executive's death, his estate is entitled to certain payments and benefits.

In 2001, the Company's employment agreement with its Chief Executive Officer was amended to provide for a non-compete clause upon the Chief Executive Officer's separation from the Company. The amount of the non-compete payment will be \$15,000,000 and was based upon an outside study of the fair value of the non-compete provisions. The Company agreed to set aside \$5,000,000 of Company funds in 2001 (which is included in other long-term assets in the accompanying consolidated balance sheet) and over the next two years to fund the remaining portion of the \$15,000,000 payment upon the Chief Executive Officer's separation from the Company, or upon change in control. Upon separation from the Company, the Company will amortize the payment over the non-compete period.

The Company has entered into several loan agreements with certain members of senior management, some of which were non-interest bearing. The impact of discounting such loans to record interest income is not significant. The balance of the senior management loan receivables as of August 31, 2001, 2000 and 1999 was approximately \$789,000, \$272,000 and \$1,415,000, respectively. In the ordinary course of business, the Company has made other loans to other employees. These balances are included in other assets.

During fiscal 1996, the Company entered into a non-competition agreement with a key employee of an acquired business. A related asset totaling approximately \$502,000 (net of accumulated amortization of \$1,465,000) is included in other assets and is being amortized over eight years using the straight-line method. A note payable to the executive for this agreement is included in long-term debt as further discussed in Note 7 of Notes to Consolidated Financial Statements.

A director of the Company was a managing director of the investment banking firm that was an underwriter and acted as one of the representatives of the underwriters for the November 1999 public offering of 6,000,000 shares of Common Stock discussed in Note 2 of Notes to Consolidated Financial Statements. The Company also granted to the underwriters an option to purchase up to an additional 900,000 shares of Common Stock pursuant to such terms to cover over-allotments, which over-allotment option was exercised. The closing of such public offering was completed in November 1999, at a price of \$10.50 per share, less the underwriting discounts and commissions of approximately \$4,313,000. Approximately \$150,000 of these commissions were earned by the director's investment banking firm. The same investment banking firm handled the repurchase of some of the shares of the Company's Common Stock which began in fiscal 1999, earning approximately \$74,000 in commissions.

A director of the Company is an owner of construction companies that have been used primarily as sub-contractors by the Company. During fiscal 2001, the Company made payments of approximately \$266,000 to one of these companies and in 2000 and 1999, payments to these construction companies were not material.

Note 17—Foreign Currency Transactions

The Company's wholly-owned subsidiaries in Venezuela had total assets of approximately \$17,200,000 and \$15,100,000 denominated in Venezuelan Bolivars as of August 31, 2001 and 2000, respectively. In accordance with SFAS No. 52, "Foreign Currency Translation," the U.S. dollar is used as the functional reporting currency for Venezuelan operations since the Venezuelan economy is defined as highly inflationary. Therefore, these assets and liabilities are translated into U.S. dollars using a combination of current and historical exchange rates.

During fiscal 1996, the Venezuelan government lifted its foreign exchange controls. Subsequent to this action, the Bolivar devalued from 690 to 736 (as of August 31, 2001) to the U.S. dollar. During the years ending August 31, 2001, 2000 and 1999, the Company recorded losses of approximately \$673,000, \$1,756,000 and \$652,000, respectively, in translating the assets and liabilities of its Venezuelan subsidiaries into U.S. dollars. These translation losses are reported as reductions to sales because they were partially offset by inflationary billing provisions in certain of the Company's contracts.

Other foreign subsidiaries maintain their accounting records in their local currency (primarily British pounds, Australian and Canadian dollars, and Dutch guilders). The currencies are converted to U.S. dollars with the effect of the foreign currency translation reflected in "accumulated other comprehensive income," a component of shareholders' equity, in accordance with SFAS No. 52 and SFAS No. 130—"Reporting Comprehensive Income." Foreign currency transaction gains or losses are credited or charged to income. At August 31, 2001 and 2000, cumulative foreign currency translation adjustments related to these subsidiaries reflected as a reduction to shareholders' equity amounted to \$6,308,000 and \$5,209,000, respectively; transaction gains (losses) reflected in income amounted to \$625,000 and (\$48,000) in the years ended August 31, 2001 and 2000, respectively.

Note 18—Unbilled Receivables, Retainage Receivables and Costs and Estimated Earnings on Uncompleted Contracts

In accordance with normal practice in the construction industry, the Company includes in current assets and current liabilities amounts related to construction contracts realizable and payable over a period in excess of one year. Costs and estimated earnings in excess of billings on uncompleted contracts represents the excess of contract costs and profits recognized to date on the percentage of completion accounting method over billings to date on certain contracts. Billings in excess of costs and estimated earnings on uncompleted contracts represents the excess of billings to date over the amount of contract costs and profits recognized to date on the percentage of completion accounting method on the remaining contracts.

Included in accounts receivable is \$42,664,000 and \$17,465,000 at August 31, 2001 and 2000, respectively, related to unbilled receivables. Advanced billings on contracts as of August 31, 2001 and 2000 was \$17,712,000 and \$15,992,000, respectively. Balances under retainage provisions totaled \$17,623,000 and \$32,449,000 at August 31, 2001 and 2000, respectively, and are also included in accounts receivable in the accompanying consolidated balance sheets.

The table below shows the components of costs and estimated earnings in excess of billings and billings in excess of costs and estimated earnings on the Company's uncompleted contracts as of August 31, 2001 and 2000 and does not include advanced billings on contracts as of August 31, 2001 and 2000 of \$17,712,000 and \$15,992,000, respectively. Contracts assumed in the Stone & Webster acquisition include cumulative balances from the origination of these contracts and, therefore, include amounts that were earned prior to the acquisition by the Company. In addition, the amounts below do not include accrued contract losses and gross margin reserves as of August 31, 2001 and 2000. The amounts presented below are (in thousands):

	August 31,	
	2001	2000
Costs incurred on uncompleted contracts	\$ 2,762,199	\$ 1,562,444
Estimated earnings thereon	224,977	76,267
	2,987,176	1,638,711
Less: billings applicable thereto	(3,129,517)	(1,680,944)
	(142,341)	(42,233)
Time and materials on a contract	10,934	34,800
	\$ (131,407)	\$ (7,433)
The following amounts are included in the accompanying balance sheet:		
Costs and estimated earnings in excess of billings on uncompleted contracts	\$ 95,012	\$ 143,250
Billings in excess of costs and estimated earnings on uncompleted contracts	(226,419)	(150,683)
	\$ (131,407)	\$ (7,433)

Note 19—Quarterly Financial Data (Unaudited)

<i>(In thousands, except per share data)</i>	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Fiscal 2001				
Sales	\$418,757	\$340,283	\$394,154	\$385,738
Gross profit	\$ 64,068	\$ 53,518	\$ 65,530	\$ 63,500
Income before extraordinary item and cumulative effect of change in accounting principle	\$ 12,161	\$ 11,820	\$ 17,890	\$ 19,341
Basic income per common share before extraordinary item and cumulative effect of change in accounting principle	\$ 0.32	\$ 0.29	\$ 0.44	\$ 0.47
Diluted income per common share before extraordinary item and cumulative effect of change in accounting principle	\$ 0.31	\$ 0.28	\$ 0.42	\$ 0.45
Fiscal 2000				
Sales	\$150,808	\$172,963	\$175,046	\$263,838
Gross profit	\$ 26,078	\$ 28,287	\$ 27,656	\$ 45,055
Income before extraordinary item and cumulative effect of change in accounting principle	\$ 5,820	\$ 7,024	\$ 7,384	\$ 10,155
Basic income per common share before extraordinary item and cumulative effect of change in accounting principle	\$ 0.23	\$ 0.23	\$ 0.24	\$ 0.32
Diluted income per common share before extraordinary item and cumulative effect of change in accounting principle	\$ 0.22	\$ 0.22	\$ 0.23	\$ 0.30

Report of Independent Public Accountants

To the Board of Directors and Shareholders of The Shaw Group Inc.:

We have audited the accompanying consolidated balance sheets of The Shaw Group Inc. (a Louisiana corporation) and subsidiaries as of August 31, 2001 and 2000, and the related consolidated statements of income, shareholders' equity and cash flows for each of the three years in the period ended August 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Shaw Group Inc. and subsidiaries as of August 31, 2001 and 2000, and the results of their operations and their cash flows for each of the three years in the period ended August 31, 2001, in conformity with accounting principles generally accepted in the United States.

/s/ Arthur Andersen LLP

Arthur Andersen LLP
New Orleans, Louisiana

October 5, 2001

Market for the Registrant's Common Equity and Related Stockholder Matters

The Company's Common Stock, no par value, (the "Common Stock"), is traded on the New York Stock Exchange (the "NYSE") under the symbol "SGR." The following table sets forth, for the quarterly periods indicated, the high and low sale prices per share for the Common Stock as reported by the NYSE, for the Company's two most recent fiscal years and for the current fiscal year to date.

	High	Low
Fiscal year ended August 31, 2000		
First quarter	\$12.19	\$ 9.50
Second quarter	13.97	10.13
Third quarter	22.47	12.31
Fourth quarter	27.84	18.69
Fiscal year ended August 31, 2001		
First quarter	\$46.50	\$27.25
Second quarter	55.39	31.00
Third quarter	63.48	40.70
Fourth quarter	60.00	23.00
Fiscal year ending August 31, 2002		
First quarter (through November 21, 2001)	\$35.74	\$23.79

The high and low sales prices for the fiscal year ended August 31, 2000 and the first and second quarters of the fiscal year ended August 31, 2001 have been restated to give effect to the December 2000 two-for-one stock split.

The closing sale price of the Common Stock on November 21, 2001, as reported on the NYSE, was \$28.85 per share. As of November 21, 2001, the Company had 132 shareholders of record.

The Company has not paid any cash dividends on the Common Stock and currently anticipates that, for the foreseeable future, any earnings will be retained for the development of the Company's business. Accordingly, no dividends are expected to be declared or paid on the Common Stock for the foreseeable future. The declaration of dividends is at the discretion of the Company's Board of Directors. The Company's dividend policy will be reviewed by the Board of Directors as may be appropriate in light of relevant factors at the time. The Company is, however, subject to certain prohibitions on the payment of dividends under the terms of existing credit facilities.

Effective March 23, 2001, the Company acquired the assets of Scott, Sevin & Schaffer, Inc. and Technicomp, Inc. (collectively "SS&S"). Subsequent to the effective date of the acquisition and in order to satisfy the Company's Common Stock price protection provisions under the acquisition agreement, the Company issued an additional 12,973 shares of Common Stock. The Common Stock was issued to the former shareholders of SS&S pursuant to Regulation D under the Securities Act of 1933, as amended.

Directors

J.M. Bernhard, Jr.
Chairman of the Board, President and
Chief Executive Officer
The Shaw Group Inc.
Baton Rouge, Louisiana

Albert D. McAlister, Esquire
Partner
McAlister & McAlister, P.A.
Laurens, South Carolina

L. Lane Grigsby
Chairman of the Board
Cajun Constructors, Inc.
Baton Rouge, Louisiana

David W. Hoyle
State Senator; Real Estate Developer
Gastonia, North Carolina

John W. Sindors, Jr.
Managing Director
Jeffries & Company, Inc.
Houston, Texas

William H. Grigg
Chairman Emeritus
Duke Energy Corporation
Charlotte, North Carolina

Executive Officers

J.M. Bernhard, Jr.
Chairman of the Board, President and
Chief Executive Officer

Richard F. Gill
Executive Vice President &
Chief Operating Officer

Robert L. Belk
Executive Vice President &
Chief Financial Officer

Donald G. Stokes
Senior Vice President
Construction and Maintenance

Mitchell A. Rayner
Senior Vice President
Fabrication and Manufacturing

Corporate Information

Corporate Office
8545 United Plaza Boulevard
Baton Rouge, Louisiana 70809
(225) 932-2500

Investor Relations
Certain shareholder records are main-
tained at the Company's corporate office
in Baton Rouge, Louisiana. Inquiries
may be directed to Christine N. Mollere,
Director of Investor Relations.

Stock Listing
New York Stock Exchange
Symbol: SGR

The Chicago Board Options Exchange
Symbol: SGR

Annual Meeting
The annual meeting of shareholders
will be held at 9:00 a.m. on Friday,
January 25, 2002 at the Radisson Hotel,
4728 Constitution Avenue, Baton Rouge,
Louisiana.

Transfer Agent & Registrar
First Union National Bank
Shareholder Services Group
1525 West W.T. Harris Boulevard
Building 3C3
Charlotte, North Carolina 28288-1153
(800) 829-8432

Auditors
Arthur Andersen LLP
201 St. Charles Avenue
Suite 4500
New Orleans, Louisiana 70170-4500

Counsel
Gary P. Graphia
Secretary and General Counsel
The Shaw Group Inc.

Safe Harbor Statement

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for certain forward-looking statements. The statements contained herein that are not historical facts (including without limitation statements to the effect that the Company or its management "believes," "expects," "anticipates," "plans," or other similar expressions) and statements related to revenues, earnings, backlog, or other financial information or results are forward-looking statements based on the Company's current expectations and beliefs concerning future developments and their potential effects on the Company. There can be no assurance that future developments affecting the Company will be those anticipated by the Company. These forward-looking statements involve significant risks and uncertainties (some of which are beyond our control) and assumptions and are subject to change based upon various factors. Should one or more of such risks or uncertainties materialize, or should any of our assumptions prove incorrect, actual results may vary in material respects from those projected in the forward-looking statements. The Company undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. A description of some of the risks and uncertainties that could cause actual results to differ materially from such forward-looking statements can be found in the Company's reports and registration statements filed with the Securities and Exchange Commission, including its Form 10-K and Form 10-Q, reports and on the Company's web site under the heading "Forward-Looking Statement". These documents are also available from the Securities and Exchange Commission or from the Investor Relations department of Shaw. For more information on the Company and announcements it makes from time to time on a regional basis visit our web site at www.shawgrp.com.

