

STEPAN COMPANY

Moderator: James Hurlbutt

April 26, 2006

1:00 pm CT

Operator: Ladies and gentlemen, thank you for standing by. Welcome to the Stepan Company First Quarter Earnings Results Conference Call. During the presentation, all participants will be on a listen-only mode. Afterwards, we will conduct a question and answer session.

At that time, if you have a question, please press the 1 followed by the 4 on your telephone. If at any time during the conference you need to reach an operator, please press the star followed by the 0.

As a reminder this conference is being recorded Wednesday, April 26, 2006. I would now like to turn the conference to Jim Hurlbutt, Vice President of Finance. Please go ahead, sir.

James Hurlbutt: Good afternoon. And thank you for joining us.

Before I begin, please note that information in this conference call contains forward-looking statements which are not historical facts.

These statements involve risks and uncertainties that could cause actual results to differ materially including, but not limited to, prospects for our foreign operations and certain global and regional economic conditions and factors detailed in the company's Securities and Exchange Commission filings.

I will now take a few minutes to review our first quarter operating results.

Net sales for the first quarter of 2006 increased 10% to \$289.6 million from \$264.3 million for the same period in 2005.

Higher selling prices and a 3% increase in sales volume accounted for the increase in sales. We have increased selling prices of our products over the past year to reflect price increases brought on by rising raw material costs, primarily the rapid increase in the cost of crude oil.

Net income for the first quarter was \$3.0 million or 31 cents per diluted share compared with net income of \$3.2 million or 33 cents per diluted

share a year ago. The results of our deferred compensation plan lowered net income by \$1.2 million, or 12 cents per diluted share.

Gross profit improved by 8%, to \$32.3 million. Operating income decreased 10%, to \$6.2 million for the first quarter of 2006, from \$6.9 million for the same period in 2005. Excluding deferred compensation expense, operating income would have been increased \$1.4 million or 22%.

Now I would like to highlight the performance in each of our three segments. We begin with surfactants, which accounted for approximately 78% of the company's sales for the first quarter.

Surfactant earnings rose modestly on improvement in Latin America and Europe that exceeded weaker North American results. Latin American's earnings growth resulted from improved sales volume of fabric softeners. European earnings improved due to a 17% increase in sales volume of sulfonated products.

North American earnings declined due to slightly lower sales volume coupled with higher natural gas and other operational costs, including higher costs associated with a labor dispute at our Fieldsboro, New Jersey Plant.

Contribution from sales of biodiesel was ahead of the year-ago quarter, but well below the last two quarters as market demand during the cold winter months declined. We continue to work towards a product that is acceptable for cold weather use in order to reduce this seasonal reduction in sales.

Turning to our polymer segment, which represented 20% of our revenue for the quarter, polymer earnings contributed the majority of the company's improvement in gross profit.

Polyurethane polyol earnings improved over the year ago quarter as a result of the price increases initiated during the 2005 year to recover lost margin due to rising raw material costs. Polyol volume, however, was down versus the year-ago quarter, continuing the weakness experienced in the second half of 2005. Phthalic anhydride earnings improved due to higher volume.

And finally, specialty products, which accounted for 2% of the company's sales in the first quarter. Specialty products earnings declined due to lower food ingredient margins brought about by price competition. We expect

gradual improvement over the balance of the year due to improving volumes.

Turning to expenses, a 9% increase in marketing expense was due to the reassignment of some research headcount to the marketing organization, resulting in an offsetting reduction of research and development and technical service costs of 6%.

The general administrative expenses increased during the first quarter due to higher outside legal and consulting costs, and higher salary costs brought on by filling headcount vacancies

Looking at other income, interest expense increased by 15% during the first quarter due to higher average interest rates.

Turning to the balance sheet, total debt as of March 31, 2006 was \$136.4 million, up from \$125.7 million at the end of 2005. Our total debt to total capitalization at quarter end was 44.7%, down from 46.3% at the same time last year.

Capital expenditures were \$9.1 million for the first quarter of 2006 compared to \$8.2 million for the first quarter of 2005. Full year capital spending for 2006 is projected to increase by 10 to 20% compared to \$41.5 million total spending during 2005.

Looking ahead, we expect continued improvement in surfactant earnings due to better volumes in fabric softener, amphoteric and biodiesel sales. We completed our biodiesel expansion in our (Millsdale), Joliet, Illinois site and expect improved sales volume and contribution for the balance of 2006. The continuing rise in crude oil prices should allow for improved biodiesel margins.

Polymer volume is also improving as we had forecasted.

Overall, we are optimistic that 2006 earnings will continue to show improvement over 2005.

This concludes my prepared remarks. At this time, I would like to turn the call over for questions. Operator, please read the instructions for the question portion of today's call.

Operator:

Thank you, sir.

Ladies and gentlemen, if you'd like to register a question, please press the 1 followed by the 4 on your telephone. You will hear a three-tone prompt

to acknowledge your request. If your question has been answered, and you'd like to withdraw your registration, please press the 1 followed by the 3. If you're using a speakerphone, please lift your handset before entering your request.

One moment please for the first question.

Our first question comes from the line of George Gaspar from Robert Baird.

Please go ahead.

George Gaspar: Yes, good afternoon. And pleased to see the numbers the way they were, and looking forward to better results here or improved results as you go on in your year.

My question, I would like to delve into this biodiesel a little bit. Can you describe where you came from to where you are now in terms of your poundage of capacity, what kind of investment that's gone in there and what do you think of this? What kind of percentage of the market do you think you have? And can you talk a little bit about what you actually do to for this biodiesel in terms of the market growth opportunity?

James Hurlbutt: Let me back up, and give the background that you're inquiring about.

As I think we've discussed in the past, the equipment we initially had available in our Joliet plant site was used to process coconut oil derivatives for our detergent product lines. A similar technology for processing soybean was available, so we got into the biodiesel business really using existing equipment with minimal investment. That gave us about 70 million pounds of capacity.

And then as the market developed, and the tax incentives were firmed up by Congress, we went ahead with a 70 million-pound expansion that brought us up to about 140 million pounds, or 19 million gallons. And that's where we sit today. And that capacity is up and running right now, and certainly with crude oil where it is right now, the margins have expanded in the last few weeks. So, it looks pretty good for the time being.

The tax incentives I referred to in the past are legislated to expire in 2008. So, the economics beyond 2008 are partly going to be driven by increasing demands for renewable energy sources, such as biodiesel is, as well as the fact that we see other alternative feedstocks as being viable in addition to soybean oil. So if soybean oil should rise, as we expect it will,

we would look to alternative feedstocks such as palm oil or tallow oils for production of biodiesel. As far as where we go from here, we are vigorously studying cost options for further expansions. We've looked at multiple locations within our five plants in the United States. The core operation still looks most attractive in our Illinois site. But we don't have a firm capital cost yet, and we're still studying it.

And I think, George, I don't know, if you are alluding to the impact of the sulfur reduction rules in one of your comments, but...

George Gaspar: Yes, I was.

James Hurlbutt: Certainly, it's going to be a factor if the biodiesel produced from soybean oil has no sulfur. So as these reductions come into play later this year, the more the blender puts of soybean in, the lower he can get his sulfur to meeting the sulfur standard.

George Gaspar: I see. Okay. And that's a national impact that is due to go into effect by the end of this year. Is that correct on this diesel side?

James Hurlbutt: The sulfur reduction standard?

George Gaspar: The sulfur reduction.

James Hurlbutt: I think they're phased in, and I don't think they have the exact dates.

George Gaspar: But ultimately, we're going from 500 parts per million to 15?

James Hurlbutt: I believe that's correct.

George Gaspar: Which is pretty heady. Okay.

James Hurlbutt: I know that's a real challenge.

George Gaspar: I can imagine.

Well, it looks like there's a pretty significant market opportunity on this biodiesel considering this sulfur situation, reduction.

If I could just follow up on the fabric softener side. Now you've got a plant - that I guess is - what's going to be a new plant in the Philippines that you've been constructing. And is your target still early or late third quarter? Did they get underway on that?

James Hurlbutt: Well, the completion of the construction is nearing an end. In the next few weeks we would hope to be gearing up into commercial production, sampling products to customers by mid-year and following with commercial sales by the third quarter.

You know, that's a significant, needed improvement for our operations in the Philippines. The product line in traditional sulfonated detergent lines has gotten very commoditized. The margins are very weak. So this will be a significant opportunity for us to improve the profitability of our Philippine operation, and diversify the product line.

And fortunately, a large portion of that is designed or planned to be export sales throughout Southeast Asia. So it's a market penetration opportunity into a growing market as fabric softeners are still in their relative infancy outside of North America and Europe.

George Gaspar: On that, will this be the first entrée in fabric softener outside the U. S. then as far as international?

James Hurlbutt: No. We're actually very large in fabric softeners in Europe for quite some time. So a lot of our growth has been in Latin America primarily in Mexico recently, and then continued growth in Europe and expansion in the U. S. over the last several years. So outside of Europe and North America including Mexico, this will be our first entrée.

George Gaspar: I got you. Okay, thank you.

James Hurlbutt: Thank you.

Operator: Our next question comes from the line of Beverly Machtinger from Grace and White. Please go ahead, ma'am.

Beverly Machtinger: Hi, Jim.

James Hurlbutt: Hi, Beverly.

Beverly Machtinger: I have a follow up on the biodiesel.

In the commentary, you said that there was some seasonality issues, and not having right product. Can you just talk a little about what that really means?

James Hurlbutt: It's identical to the problem that already exists with diesel fuel when you get down below zero Fahrenheit; diesel fuel starts coagulating in this. And, you have to keep either the engine running all the time or keep the

fuel heated. Otherwise, you're going to get some potential clogging in the filtration system before combustion.

Biodiesel has the similar properties and, depending on the level of purity of the biodiesel, you may have a little worse coagulation or viscosity problem than straight diesel.

So we're looking at improving the profile of our biodiesel and/or using boosters or other chemical additives to eliminate the problems. So, we're working on a solution. Hope that we will have that in place before the next winter season.

Beverly Machtinger: Okay. Great.

And then I have a question on the China joint venture.

And do you have a timetable for, maybe, that starting to add to the company or you're still investing at this stage?

James Hurlbutt: It's running close to break-even right through the first quarter. We expect it to generate profits by the end of the year. So it is - and we do expect it to turn profitable and generate modest profitability this year.

But the opportunities that we're uncovering would suggest that in the longer term, there are plenty of opportunities for us to broaden the product portfolio and downstream that capacity there. So, even though we're still at the infancy of this joint venture, all of our businesspeople still feel very positive about the opportunities that are coming forward.

Beverly Machtinger: Great. Thanks a lot.

James Hurlbutt: Thank you.

Operator: Our next question is a follow up from George Gaspar from Robert W. Baird. Please go ahead.

George Gaspar: Yes. Thank you.

A question on the European market in general, how you are experiencing your cost structure at this point, relative to the first quarter? And the environment, from a revenue generating point of view, for the remainder of the year?

James Hurlbutt: Well, I think, as you know, we've been trying very hard to get our costs under control, as well as to get our volume fully utilized over there. And

we had significant improvement last year as a result of a shutdown by Huntsman of their UK facility, which has help tighten up capacity a little bit and improved our volume in the UK and, even, we've seen some improvement in the Continent.

The raw material situation, obviously, is still very fluid with crude oil getting more volatile again, and natural gas bouncing around it. It will be a challenge, but we do believe Europe in total will be a more solid contributor this year than it was last year with steady improvement.

George Gaspar: Okay.

And then I have a question on the value of your asset base in the United States.

I mean, it's just rather unbelievable, the hurdles that companies have to get over when it comes to trying to build new chemical facilities, and specialty would probably fall into that category. And it seems like you're pretty positioned around the United States in the existing facilities that you have.

What do you envision, from an opportunity point of view, to build out your existing locations, because, it would assume that that's much better for you, and easier on a permitting basis and maybe makes a lot of other companies envious quite frankly with considering the environmental impact, can you comment at all on this?

James Hurlbutt: Well, it's very true that the indirect cost of operating a chemical plant, and getting it up and running, getting a permit, and everything is very difficult today. The trend in the chemical industry has been by consolidations, not expanding their footprint any more than they need to. We held tight with five sites in the U. S., and then one in Canada and one in Mexico to solidify our position, as competitors contracted, with our customer relations and our supply chain ability.

I think, when you talk about the opportunity to build out that platform, biodiesel is an excellent example. I mean, we were able to get into the biodiesel business for a fraction of what we believe, or understand, to be the cost associated with startup biodiesel facilities that have gone up in the Midwest in the last 12 months. So, yes, there are plenty of opportunities that we would like to continue to pursue.

The polymer group has some new product opportunities that would require a newer facility that would not be grass roots – they would be

bolt-ons to our existing facilities. So, yeah, it is an advantage that we certainly look to try and capitalize on.

George Gaspar: Okay. Thank you.

Operator: All right, sir, there are no further questions at this time.

James Hurlbutt: Okay. I'd like to thank everybody for joining us today, and look forward to talking to you in the future. Thank you.

Operator: Ladies and gentlemen, that does conclude the conference for today. We thank you for your participation, and ask that you please disconnect your lines.

Thank you.

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