OLYMPIC STEEL INC
Form 10-Q
November 08, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

Form 10-Q

(X)QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2012

(   ) TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIESEXCHANGE ACT OF 1934

For the transition period from   to

Commission File Number 0-23320

OLYMPIC STEEL, INC.
(Exact name of registrant as specified in its charter)

Ohio (State or other jurisdiction of incorporation or organization)	34-1245650 (I.R.S. Employer Identification No.)
5096 Richmond Road, Bedford Heights, Ohio (Address of principal executive offices)	44146 (Zip Code)

Registrant's telephone number, including area code (216) 292-3800

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes (X) No ( )

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of “large accelerated filer” “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act:

Large accelerated filer ( )	Accelerated filer (X)
Non-accelerated filer ( ) (Do not check if a smaller reporting company)	Smaller reporting company ( )

Indicate by check mark whether the registrant is a shell company (as defined Rule 12b-2 of the Exchange Act). Yes ( ) No (X)

Indicate the number of shares of each of the issuer's classes of common stock, as of the latest practicable date:

Class	Outstanding as of November 8, 2012
Common stock, without par value	10,917,840

Olympic Steel, Inc.
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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

Olympic Steel, Inc.
Consolidated Balance Sheets
(in thousands)

	September 30, 2012 (unaudited)	December 31, 2011 (audited)
Assets		
Cash and cash equivalents	$3,832	$7,403
Accounts receivable, net	152,434	122,579
Inventories, net	288,698	277,765
Prepaid expenses and other	9,417	13,112
Total current assets	454,381	420,859
Property and equipment, at cost	345,593	329,116
Accumulated depreciation	(146,965)	(135,703)
Net property and equipment	198,628	193,413
Goodwill	47,370	47,254
Intangible assets, net	35,646	36,313
Other long-term assets	11,603	9,660
Total assets	$747,628	$707,499
Liabilities		
Current portion of long-term debt	$10,253	$9,662
Accounts payable	98,754	104,425
Accrued payroll	10,879	11,613
Other accrued liabilities	14,039	13,875
Total current liabilities	133,925	139,575
Credit facility revolver	211,015	170,405
Long-term debt	56,111	64,149
Other long-term liabilities	11,788	9,580
Deferred income taxes	34,952	37,214
Total liabilities	447,791	420,923
Shareholders' Equity		
Preferred stock	-	-
Common stock	121,905	119,816
Accumulated other comprehensive loss, net of tax	(568)	-
Retained earnings	178,500	166,760
Total shareholders' equity	299,837	286,576
Total liabilities and shareholders' equity	$747,628	$707,499

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

Olympic Steel, Inc.
Consolidated Statements of Comprehensive Income
(in thousands, except per share data)

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
	(unaudited)		(unaudited)	
Net sales	$342,560	$348,547	$1,091,977	$941,928
Costs and expenses				
Cost of materials sold (excludes items shown seperately below)	276,504	281,058	879,060	750,638
Warehouse and processing	21,667	19,471	63,892	51,432
Administrative and general	16,765	16,461	52,647	43,339
Distribution	8,682	8,080	26,960	20,427
Selling	7,085	7,209	20,989	18,140
Occupancy	2,057	2,297	6,495	5,790
Depreciation	4,953	4,434	14,636	11,413
Amortization	223	222	667	222
Total costs and expenses	337,936	339,232	1,065,346	901,401
Operating income	4,624	9,315	26,631	40,527
Other (income) expense, net	(51)	91	(90)	91
Income before interest and income taxes	4,675	9,224	26,721	40,436
Interest and other expense on debt	2,120	2,237	6,411	3,868
Income before income taxes	2,555	6,987	20,310	36,568
Income tax provision	916	851	7,915	12,163
Net income	$1,639	$6,136	$12,395	$24,405
Net loss on interest rate hedge, net of tax	(165)	-	(568)	-
Total comprehensive income	$1,474	$6,136	$11,827	$24,405
Earnings per share:				
Net income per share - basic	$0.15	$0.56	$1.13	$2.23
Weighted average shares outstanding - basic	10,961	10,937	10,958	10,936
Net income per share - diluted	$0.15	$0.56	$1.13	$2.23
Weighted average shares outstanding - diluted	10,967	10,951	10,967	10,949

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

Olympic Steel, Inc.
Consolidated Statements of Cash Flows
(in thousands)

	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
	(unaudited)	
Cash flows from (used for) operating activities:		
Net income	$ 12,395	$ 24,405
Adjustments to reconcile net income to net cash used for operating activities -		
Purchase price inventory adjustment	-	1,017
Depreciation and amortization	16,263	12,050
Loss on disposition of property and equipment	23	65
Stock-based compensation	1,741	647
Other long-term assets	(1,810)	1,220
Other long-term liabilities	1,640	5,399
	30,252	44,803
Changes in working capital:		
Accounts receivable	(29,855)	(49,350)
Inventories	(10,933)	(41,748)
Income taxes receivable and deferred	(2,262)	8,750
Prepaid expenses and other	3,695	(5,861)
Accounts payable	(2,195)	34,379
Change in outstanding checks	(3,476)	9,479
Accrued payroll and other accrued liabilities	(390)	(10,240)
	(45,416)	(54,591)
Net cash used for operating activities	(15,164)	(9,788)
Cash flows from (used for) investing activities:		
Acquisition of Chicago Tube and Iron, net of cash acquired	-	(148,759)
Capital expenditures	(20,290)	(24,618)
Proceeds from disposition of property and equipment	236	699
Net cash used for investing activities	(20,054)	(172,678)
Cash flows from (used for) financing activities:		
Credit facility revolver borrowings	437,925	444,134
Credit facility revolver repayments	(397,315)	(324,909)
Principal payments under capital lease obligations	(130)	(39)
Term loan borrowings	-	70,000
Term loan repayments	(6,562)	(2,188)
Industrial revenue bond repayments	(755)	-
Credit facility fees and expenses	(1,209)	(4,193)
Proceeds from exercise of stock options (including tax benefits) and employee stock purchases	348	34
Dividends paid	(655)	(654)
Net cash from financing activities	31,647	182,185

Cash and cash equivalents:		
Net change	(3,571)	(281)
Beginning balance	7,403	1,492
Ending balance	$ 3,832	$ 1,211

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

Olympic Steel, Inc.
Supplemental Disclosures of Cash Flow Information
(in thousands)

	Nine Months Ended September 30,			
		2012		2011
	(unaudited)			
Cash paid during the period				
Interest paid	$	5,622	$	3,089
Income taxes paid	$	6,170	$	8,852
Details of acquisition				
Fair value of CTI assets acquired	$	-	$	215,817
Fair value of CTI liabilities acquired		-		55,961
Cash paid		-		159,856
Less: Cash acquired		-		11,097
Net cash paid for CTI acquisition	$	-	$	148,759

The Company incurred a capital lease obligation of $1.6 million when it entered into a lease for its warehouse in Streetsboro, Ohio during the third quarter of 2011. This non-cash transaction has been excluded from the Consolidated Statement of Cash Flow for the nine months ended September 30, 2011.

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

Olympic Steel, Inc.

Notes to Consolidated Financial Statements

(unaudited)

September 30, 2012

(1) Basis of Presentation:

The accompanying consolidated financial statements have been prepared from the financial records of Olympic Steel, Inc. and its wholly-owned subsidiaries (collectively, Olympic or the Company), without audit and reflect all normal and recurring adjustments which are, in the opinion of management, necessary to fairly state the results of the interim periods covered by this report. Year-to-date results are not necessarily indicative of 2012 annual results and these financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2011. All significant intercompany transactions and balances have been eliminated in consolidation.

Commencing with the July 1, 2011 acquisition of Chicago Tube and Iron Company (CTI), the Company operates in two reportable segments; flat products and tubular and pipe products. Through its flat products segment, the Company sells and distributes large volumes of processed carbon, coated, aluminum and stainless flat-rolled sheet, coil and plate products. Through its tubular and pipe products segment, the Company distributes metal tubing, pipe, bar, valve and fittings and the fabrication of pressure parts supplied to various industrial markets.

(2) Acquisition of Chicago Tube and Iron Company:

On July 1, 2011, the Company acquired all of the outstanding common shares of CTI pursuant to the terms of an Agreement and Plan of Merger dated May 18, 2011. Total cash paid, net of cash acquired, was $148.8 million.

Pro Forma Financial Information

The following unaudited pro forma summary of financial results presents the consolidated results of operations as if the CTI acquisition had occurred on January 1, 2010, after the effect of certain adjustments, including increased depreciation expense resulting from recording fixed assets at fair value, interest expense on the acquisition debt and amortization of customer relationships, with the related tax effects. The pro forma results for the nine months ended September 30, 2011 do not include any transaction costs and other non-recurring acquisition related expenses. The pro forma results have been presented for comparative purposes only and are not indicative of what would have occurred had the acquisition been made on January 1, 2010, or of any potential results that may occur in the future.

(in thousands, except per share amounts)	Nine months ended September 30, 2011 (Pro-forma)
Pro forma (unaudited):	
Net sales	$ 1,062,435
Net income	$ 27,053

Basic earnings per common share	$	2.47
Diluted earnings per common share	$	2.47

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(3) Accounts Receivable:

The Company maintained allowances for doubtful accounts and unissued credits of $3.5 million and $2.9 million at September 30, 2012 and December 31, 2011, respectively. The allowance for doubtful accounts is maintained at a level considered appropriate based on historical experience and specific customer collection issues that have been identified. Estimations are based upon a calculated percentage of accounts receivable, which remains fairly level from year to year, and judgments about the probable effects of economic conditions on certain customers, which can fluctuate significantly from year to year. The Company cannot guarantee that the rate of future credit losses will be similar to past experience. The Company considers all available information when assessing the adequacy of its allowance for doubtful accounts and unissued credits each quarter.

(4) Inventories:

Inventories are stated at the lower of cost or market and include the costs of purchased metal, inbound freight, external processing and applicable labor and overhead costs. Cost for the Company's flat products segment (flat-rolled sheet, coil and plate products) is determined using the specific identification method.

As a result of the acquisition of CTI, certain of the Company's tubular and pipe products inventory is stated under the last-in, first-out (LIFO) method, which is not in excess of market. At September 30, 2012, approximately $46.3 million, or 16.0% of consolidated inventory, was reported under the LIFO method of accounting. The cost of the remainder of CTI's inventory is determined using a weighted average first-in, first-out method.

An actual valuation of the inventory under the LIFO method is made at the end of each year based on the inventory levels and costs at that time. Accordingly, interim LIFO calculations are based on management's estimates of expected year-end inventory levels and costs. Because estimates are subject to many factors beyond management's control, annual results may differ from interim results. Interim LIFO estimates are subject to a final year-end LIFO inventory valuation. The Company did not record a LIFO adjustment in its third quarter of 2012 because its full-year LIFO estimate anticipates prices and quantities to be below July 1, 2011 levels. As a result, there was no LIFO reserve at September 30, 2012.

Metal inventories consist of the following:

(in thousands)	September 30, 2012	December 31, 2011
Unprocessed	$ 209,995	$ 207,301
Processed and finished	78,703	70,464
Totals	$ 288,698	$ 277,765

(5) Intangible Assets:

Intangible assets, net, consisted of the following as of September 30, 2012 and December 31, 2011:

September 30, 2012 (in thousands)	Gross Carrying Amount	Accumulated Amortization	Intangible Assets, Net

Customer relationships - subject to amortization	$	13,332	$	(1,111	)	$	12,221
Trade name - not subject to amortization		23,425		-			23,425
	$	36,757	$	(1,111	)	$	35,646

December 31, 2011	Gross Carrying Amount	Accumulated Amortization	Intangible Assets, Net
(in thousands)			
Customer relationships - subject to amortization	$ 13,332	$ (444)	$ 12,888
Trade name - not subject to amortization	23,425	-	23,425
	$ 36,757	$ (444)	$ 36,313

The Company estimates that amortization expense for its intangible assets subject to amortization will be $889 thousand for the year ended December 31, 2012 and $889 thousand per year in each of the next five years.

(6) Goodwill:

The carrying amount of goodwill, by reportable segment, is as follows:

	September 30, 2012	December 31, 2011
(in thousands)		
Flat products	$ 7,083	$ 7,083
Tubular and pipe products	40,287	40,171
Total	$ 47,370	$ 47,254

The goodwill is not deductible for income tax purposes. The goodwill represents the excess of cost over the fair value of net tangible and intangible assets acquired. The Company paid for goodwill in conjunction with the acquisitions, as they enhance the Company's commercial opportunities by adding new product offerings to an expanded customer base and by increasing the Company's distribution footprint.

In accordance with the Accounting Standards Codification, on an annual basis, an impairment test of goodwill is performed in the fourth quarter, or more frequently if changes in circumstances or the occurrence of events indicate potential impairment. Events or changes in circumstances that could trigger an impairment review include significant nonperformance relative to the expected historical or projected future operating results, significant changes in the manner of the use of the acquired assets or the strategy for the overall business or significant negative industry or economic trends.

Due to the Company's book value exceeding the Company's market capitalization, a triggering event review of potential goodwill impairment was performed in the second quarter as of June 1, 2012. For the goodwill related to the tubular and pipe products segment, a qualitative assessment was performed. For the Company's reportable units within the flat products segment, a discounted cash flow analysis was performed, which contains significant unobservable inputs, based upon average earnings before interest, taxes, depreciation and amortization and cash flow multiples. In all cases, the fair values of the entities were in excess of the carrying values of the entities and there were no indications of impairment.

The Company concluded there were no new triggering events in the third quarter that would have required a goodwill impairment test as of September 30, 2012.

(7) Investments in Joint Ventures:

The Company and the United States Steel Corporation each own 50% of Olympic Laser Processing (OLP), a company that produced laser welded sheet steel blanks for the automotive industry. OLP ceased operations in 2006. In December 2006, the Company advanced $3.2 million to OLP to cover a loan guarantee.

In May 2012, the real estate associated with OLP was sold, resulting in a pre-tax loss on sale to the Company of $9 thousand. The Company expects to finalize all of the transactions related to the sale of the real estate and to dissolve OLP in the fourth quarter of 2012.

As of December 31, 2011, the investment in and advance to OLP was valued at $1.6 million on the Company's Consolidated Balance Sheet. The investment in OLP was determined using Level 2 inputs. The valuation was based upon sales comparisons of real estate properties that were similar in type and geography.

(8) Debt:

The Company's debt is comprised of the following components:

(in thousands)		September 30, 2012		December 31, 2011
Asset-based revolving credit facility due June 30, 2016	$	211,015	$	170,405
Term loan due June 30, 2016		59,792		66,354
Industrial revenue bond due April 1, 2018		5,125		5,880
Capital lease		1,447		1,577
Total debt		277,379		244,216
Less current amount		(10,253)		(9,662)
Total long-term debt	$	267,126	$	234,554

On March 16, 2012, the Company amended its existing asset-based revolving credit facility. The amendment provided, among other things: (i) a reduction in the applicable margin for loans under the Company's Loan and Security Agreement; (ii) additional revolving commitments to the borrowers in an aggregate principal amount of $50 million, which additional revolving commitments do not impact the borrowers' incremental facilities; and (iii) permits certain transactions among the borrowers and Metales de Olympic, S. de R.L. de C.V., an indirect subsidiary of the Company. The amended asset-based credit facility (the ABL Credit Facility) consists of a revolving credit line of $315 million and a $64 million term loan, with monthly principal payments. At September 30, 2012, the term loan balance was $59.8 million. Revolver borrowings are limited to the lesser of a borrowing base, comprised of eligible receivables and inventories, or $315 million in the aggregate. The ABL Credit Facility matures on June 30, 2016.

The ABL Credit Facility requires the Company to comply with various covenants, the most significant of which include: (i) until maturity of the ABL Credit Facility, if any commitments or obligations are outstanding and the Company's availability is less than the greater of $20 million, 12.5% of the aggregate amount of revolver commitments ($26 million at September 30, 2012), or 60% of the principal balance of the term loan then outstanding ($36 million at September 30, 2012), then the Company must maintain a ratio of EBITDA minus certain capital expenditures and cash taxes paid to fixed charges of at least 1.10 to 1.00 for the most recent twelve fiscal month period; (ii) limitations on dividend payments; (iii) restrictions on additional indebtedness; and (iv) limitations on investments and joint ventures. Effective with the March 16, 2012 amendment, the Company has the option to borrow under its revolver based on the agent's base rate plus a premium ranging from 0.00% to 0.50% or the London Interbank Offered Rate (LIBOR) plus a premium ranging from 1.50% to 2.00%. The interest rate under the term loan is based on the agent's base rate plus a premium ranging from 0.25% to 0.75% or LIBOR plus a premium ranging from 1.75% to 2.25%.

As of September 30, 2012, the Company was in compliance with its covenants and had approximately $75 million of availability under the ABL Credit Facility.

In June 2012, the Company entered into a forward starting fixed rate interest rate hedge commencing July 2013 in order to eliminate the variability of cash interest payments on $53 million of the outstanding LIBOR based borrowings under the ABL Credit Facility. The hedge matures on June 1, 2016 and is reduced monthly by the principal payments on the term loan. The interest rate hedge fixed the rate at 1.21% plus a premium ranging from 1.75% to 2.25%. Although the Company is exposed to credit loss in the event of nonperformance by the other parties to the interest rate hedge agreement, the Company anticipates performance by the counterparties.

As of September 30, 2012, $5.0 million of bank financing fees were included in “Prepaid expenses and other” and “Other long-term assets” on the accompanying Consolidated Balance Sheet. This includes $1.2 million of financing fees paid for the March 16, 2012 amendment. The financing fees are being amortized over the remaining term of the ABL Credit Facility.

As part of the CTI acquisition, the Company assumed approximately $5.9 million of Industrial Revenue Bond indebtedness issued through the Stanly County, North Carolina Industrial Revenue and Pollution Control Authority (IRB). As of September 30, 2012 $5.1 million was outstanding on the IRB. The bond matures in April 2018, with the option to provide principal payments annually on April 1st. Interest is payable monthly, with a variable rate that resets weekly. As security for payment of the bonds, the Company obtained a direct pay letter of credit issued by JPMorgan Chase Bank, N.A. The letter of credit reduces annually by the principal reduction amount. The interest rate at September 30, 2012 was 0.29% for the IRB debt.

The Company entered into an interest rate swap agreement to reduce the impact of changes in interest rates on the above IRB. At September 30, 2012, the effect of the swap agreement on the bond was to fix the rate at 3.46%. The swap agreement matures April 2018, but is reduced annually by the amount of the optional principal payments on the bond. Although the Company is exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreement, the Company anticipates performance by the counterparties.

(9) Derivative Instruments:

Nickel swaps

During 2012 and 2011, the Company entered into nickel swaps indexed to the London Metal Exchange (LME) price of nickel with third-party brokers. The nickel swaps are treated as derivatives for accounting purposes. The Company entered into the swaps to mitigate its customers' risk of volatility in the price of nickel. The nickel swaps vary in length from nine to 21 months and are settled with the broker at maturity. The nickel swaps settle on a monthly basis from December 2012 through November 2013. The economic benefit or loss arising from the changes in fair value of the swaps is contractually passed through to the customer. The primary risk associated with the nickel swaps is the ability of customers or third-party brokers to honor their agreements with the Company related to derivative instruments. If the customer or third-party brokers are unable to honor their agreements, the Company's risk of loss is the fair value of the nickel swap.

In October 2011, MF Global UK Limited (MF Global UK), a United Kingdom based broker-dealer, was placed into the United Kingdom's administration process (a process similar to bankruptcy proceedings in the United States) by the Financial Services Authority following the Chapter 11 bankruptcy filing of its U.S. parent, MF Global Holdings Ltd. The Company had used MF Global UK as one of its third-party brokers for nickel swaps. All of the Company's open hedges with MF Global UK were closed effective November 1, 2011, and the Company does not believe it has a material obligation to MF Global UK as of September 30, 2012. However, bankruptcy and administration processes are uncertain and the results could change and the Company's financial statements may be materially impacted in the future.

While these derivatives are intended to help the Company manage risk, they have not been designated as hedging instruments. The periodic changes in fair value of the nickel and embedded customer derivative instruments are included in "Cost of materials sold" in the Consolidated Statement of Comprehensive Income. We recognize derivative positions with both the customer and the third party for the derivatives and we classify cash settlement amounts associated with them as part of "Cost of materials sold" in the Consolidated Statements of Comprehensive Income. The periodic changes in fair value of the interest rate swap are included in "Other income and expense, net" in the Consolidated Statement of Comprehensive Income. Cash settlement amounts associated with the interest rate swap are included in "Interest and other expense on debt" in the Consolidated Statements of Comprehensive Income.

The embedded customer derivatives are included in "Accounts receivable, net", and the nickel and interest rate swaps are included in "Other accrued liabilities" and "Other long-term liabilities" on the Consolidated Balance Sheets at

September 30, 2012 and December 31, 2011.

Interest rate swap

CTI entered into an interest rate swap to reduce the impact of changes in interest rates on its IRB. The swap agreement matures April 2018, the same time as the IRB, but is reduced annually by the amount of the principal payments on the IRB. Although the Company is exposed to credit loss in the event of nonperformance by the other parties to the interest rate swap agreement, the Company anticipates performance by the counterparties. The interest rate swap is not treated as a hedging instrument for accounting purposes.

Fixed rate interest rate hedge

In June 2012, the Company entered into a forward starting fixed rate interest rate hedge commencing July 2013 in order to eliminate the variability of cash interest payments on $53 million of the outstanding LIBOR-based borrowings under the ABL Credit Facility. The hedge matures on June 1, 2016 and is reduced monthly by the principal payments on the term loan. The fixed rate interest rate hedge is accounted for as a cash flow hedging instrument for accounting purposes.

The table below shows the total net gain or (loss) recognized in the Company's Consolidated Statement of Comprehensive Income of the derivatives for the three and nine months ended September 30, 2012 and 2011.

	Net Gain (Loss) Recognized			
	Three Months Ended September 30,		Nine Months Ended September 30,	
	2012	2011	2012	2011
(in thousands)				
Interest rate swap	$7	$(80)	$23	$(80)
Nickel swaps	245	(973)	16	901
Embedded customer derivatives	(245)	973	(16)	(901)
Total gain (loss)	$7	$(80)	$23	$(80)

(10) Fair Value of Financial Instruments:

The Company's financial instruments include cash and cash equivalents, short-term trade receivables, derivative instruments, accounts payable and debt instruments. For short-term instruments, other than those required to be reported at fair value on a recurring basis and for which additional disclosures are included below, management concluded the historical carrying value is a reasonable estimate of fair value because of the short period of time between the origination of such instruments and their expected realization.

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is an exit price concept that assumes an orderly transaction between willing market participants. Valuation techniques must maximize the use of observable inputs and minimize the use of unobservable inputs. To measure fair value, the Company applies a fair value hierarchy that is based on three levels of input, of which the first two are considered observable and the last unobservable, as follows:

Level 1 – Quoted prices in active markets for identical assets and liabilities.

Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices that are not active; or other inputs that are observable or can be corroborated by observable market date for substantially the full term of the assets or liabilities.

Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

During the nine months ended September 30, 2012, there were no transfers of financial assets between the levels in the fair value hierarchy. Following is a description of the valuation methodologies used for assets and liabilities measured at fair value as of September 30, 2012 and December 31, 2011:

Nickel swaps and embedded customer derivatives – Determined by using Level 2 inputs that include the price of nickel indexed to the LME. The fair value is determined based on quoted market prices and reflects the estimated amounts the Company would pay or receive to terminate the nickel swaps.

Interest rate swap and fixed rate interest rate hedge – Based on the present value of the expected future cash flows, considering the risks involved, and using discount rates appropriate for the maturity date. Market observable Level 2 inputs are used to determine the present value of future cash flows.

The following table presents information about the Company's assets and liabilities that were measured at fair value on a recurring basis and indicates the fair value hierarchy of the valuation techniques utilized by the Company:

	Value of Items Recorded at Fair Value As of September 30, 2012			
(in thousands)	Level 1	Level 2	Level 3	Total
Liabilities:				
Embedded customer derivatives	-	16	-	16
Nickel swaps	-	39	-	39
Interest rate swap	-	468	-	468
Fixed interest rate hedge	-	923	-	923
Total liabilities at fair value	$-	$1,446	$-	$1,446

	Value of Items Not Recorded at Fair Value As of September 30, 2012			
(in thousands)	Level 1	Level 2	Level 3	Total
Liabilities:				
Debt				