

UNIVERSAL STAINLESS & ALLOY PRODUCTS INC

Form 10-K

March 07, 2008

[Table of Contents](#)

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

Washington, DC 20549

**FORM 10-K**

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the Fiscal Year Ended December 31, 2007**

**OR**

.. **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**Commission File Number 000-25032**

**UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.**

**(Exact name of Registrant as specified in its charter)**

Edgar Filing: UNIVERSAL STAINLESS & ALLOY PRODUCTS INC - Form 10-K

**DELAWARE**  
(State or other jurisdiction of  
incorporation or organization)

**25-1724540**  
(IRS Employer  
Identification No.)

**600 MAYER STREET, BRIDGEVILLE, PA 15017**  
(Address of principal executive offices, including zip code)

**(412) 257-7600**  
(Registrant's telephone number, including area code)

**Securities registered pursuant to Section 12(b) of the Act: [None]**

**Securities registered pursuant to Section 12(g) of the Act:**

**Title of Class**

**Common Stock, par value \$.001 per share**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definitions of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check One)

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

The aggregate market value of the voting stock held by non-affiliates of the registrant on June 30, 2007, based on the closing price of \$35.23 per share on that date, was \$117,529,000. For the purposes of this disclosure only, the registrant has assumed that its directors, executive officers, and beneficial owners of 5% or more of the registrant's Common Stock are the affiliates of the registrant. The registrant has made no determination that such persons are affiliates within the meaning of Rule 405 under the Securities Act of 1933.

As of February 29, 2008, there were 6,659,499 shares of the Registrant's Common Stock issued and outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Edgar Filing: UNIVERSAL STAINLESS & ALLOY PRODUCTS INC - Form 10-K

Part III of this Form 10-K incorporates by reference portions of the Company's definitive Proxy Statement for the Annual Meeting of Stockholders scheduled to be held May 21, 2008.

**Table of Contents**

FINANCIAL REVIEW

**PART I**

<i>Item 1.</i>	<i><u>Business</u></i>	3
<i>Item 1A.</i>	<i>Risk Factors</i>	7
<i>Item 1B.</i>	<i><u>Unresolved Staff Comments</u></i>	8
<i>Item 2.</i>	<i><u>Properties</u></i>	8
<i>Item 3.</i>	<i><u>Legal Proceedings</u></i>	9
<i>Item 4.</i>	<i><u>Submission of Matters to a Vote of Security Holders</u></i>	9

**PART II**

<i>Item 5.</i>	<i><u>Market for the Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities</u></i>	9
<i>Item 6.</i>	<i><u>Selected Financial Data</u></i>	11
<i>Item 7.</i>	<i><u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u></i>	11
<i>Item 7A.</i>	<i><u>Quantitative and Qualitative Disclosures about Market Risk</u></i>	18
<i>Item 8.</i>	<i><u>Financial Statements and Supplementary Data</u></i>	19
<i>Item 9.</i>	<i><u>Changes in and Disagreements with Accountants on Accounting and Financial Disclosure</u></i>	36
<i>Item 9A.</i>	<i><u>Controls and Procedures</u></i>	36
<i>Item 9B.</i>	<i><u>Other Information</u></i>	36

**PART III**

<i>Item 10.</i>	<i><u>Directors, Executive Officers and Corporate Governance</u></i>	36
<i>Item 11.</i>	<i><u>Executive Compensation</u></i>	36
<i>Item 12.</i>	<i><u>Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters</u></i>	36
<i>Item 13.</i>	<i><u>Certain Relationships and Related Transactions, and Director Independence</u></i>	37
<i>Item 14.</i>	<i><u>Principal Accountant Fees and Services</u></i>	37

**PART IV**

<i>Item 15.</i>	<i><u>Exhibits and Financial Statement Schedules</u></i>	37
-----------------	--	----

---

## Table of Contents

### PART I

#### ITEM 1. BUSINESS GENERAL

Universal Stainless & Alloy Products, Inc. and its wholly-owned subsidiaries (the Company), which was incorporated in 1994, manufactures and markets semi-finished and finished specialty steel products, including stainless steel, tool steel and certain other alloyed steels. The Company's manufacturing process involves melting, remelting, heat treating, hot and cold rolling, machining and cold drawing of semi-finished and finished specialty steels. The Company's products are sold to rerollers, forgers, service centers, original equipment manufacturers (OEMs) and wire redrawers. The Company's customers further process its products for use in a variety of industries, including the aerospace, power generation, petrochemical and heavy equipment manufacturing industries. The Company also performs conversion services on materials supplied by customers that lack certain of the Company's production facilities or that are subject to their own capacity constraints.

The Company comprises three operating locations and one corporate headquarters. For segment reporting, the Bridgeville and Titusville facilities have been aggregated into one reportable segment, Universal Stainless & Alloy Products. Dunkirk Specialty Steel represents the second reportable segment.

The Company's products are manufactured in a wide variety of grades, widths and gauges in response to customer specifications. At its Bridgeville facility, the Company produces specialty steel products in the form of long products (ingots, blooms, billets and bars) and flat rolled products (slabs and plates). Certain grades requiring vacuum-arc remelting (VAR) may be transported to the Titusville facility to complete that process and then be transported back to the Bridgeville facility for further processing. The semi-finished long products are primarily used by the Company's Dunkirk facility and certain customers to produce finished bar, rod and wire products, and the semi-finished flat rolled products are used by customers to produce fine-gauge plate, sheet and strip products. The finished bar products manufactured by the Company are primarily used by OEMs and by service center customers for distribution to a variety of end users. The Company also produces customized shapes primarily for OEMs that are cold rolled from purchased coiled strip, flat bar or extruded bar at its Precision Rolled Products department (PRP), located at its Titusville facility.

#### INDUSTRY OVERVIEW

The specialty steel industry is a relatively small but distinct segment of the overall steel industry. Specialty steels include stainless steels, high-speed and tool steels, electrical steels, high-temperature alloys, magnetic alloys and electronic alloys. Specialty steels are made with a high alloy content, which enables their use in environments that demand exceptional hardness, toughness, strength and resistance to heat, corrosion or abrasion, or combinations thereof. Specialty steels generally must conform to more demanding customer specifications for consistency, straightness and surface finish than carbon steels. According to the Specialty Steel Industry of North America (SSINA), annual domestic consumption of specialty steels approximated 3.1 million tons in 2006. Of this amount, approximately 2.3 million tons of specialty steels consumed domestically represented stainless steel sheet and strip and electrical alloy products which the Company does not produce. Also, according to SSINA data through November 30, 2007, while U.S. consumption of total specialty steel products in 2007 decreased 14% from 2006 levels, those in the Company's addressable market decreased more moderately, with consumption of stainless steel bar down 1.5%, stainless steel rod down 8.6% and stainless steel wire down 2.3%.

The Company primarily manufactures its products within the following product lines and, generally, in response to customer orders:

*Stainless Steel.* Stainless steel, which represents the largest part of the specialty steel market, contains elements such as nickel, chrome and molybdenum that give it the unique qualities of high strength, good wear characteristics, natural attractiveness, ease of maintenance and resistance to rust, corrosion and heat. Stainless steel is used, among other applications, in the automotive, aerospace and power generation industries, as well as in the manufacture of food handling, health and medical, chemical processing and pollution control equipment. The increased number of applications for stainless steel has resulted in the development of a greater variety of stainless steel metallurgical grades than carbon steel.

*Tool Steel.* Tool steels contain elements of manganese, silicon, chrome and molybdenum to produce specific hardness characteristics that enable tool steels to form, cut, shape and shear other materials in the manufacturing process. Heating and cooling at precise rates in the heat-treating process bring out these hardness characteristics. Tool steels are utilized in the manufacturing of metals, plastics, paper and aluminum extrusions, pharmaceuticals, electronics and optics.

## Edgar Filing: UNIVERSAL STAINLESS & ALLOY PRODUCTS INC - Form 10-K

*High-Temperature Alloy Steel.* These steels are designed to meet critical requirements of heat resistance and structural integrity. They generally have very high nickel content relative to other types of specialty steels. High-temperature alloy steels are manufactured for use generally in the aerospace industry.

*High-Strength Low Alloy Steel.* High-strength low alloy steel is a relative term that refers to those steels that maintain alloying elements that range in versatility. The alloy element of nickel, chrome and molybdenum in such steels typically exceeds the alloy element of carbon steels but not that of high-temperature alloy steel. High-strength low alloy steels are manufactured for use generally in the aerospace industry.

**Table of Contents**

Net sales by principal product line were as follows:

<b>For the years ended December 31,</b> <i>(dollars in thousands)</i>	<b>2007</b>	<b>2006</b>	<b>2005</b>
Stainless steel	<b>\$ 164,228</b>	\$ 151,633	\$ 135,588
Tool steel	<b>28,119</b>	23,389	20,737
High-strength low alloy steel	<b>25,892</b>	16,467	6,606
High-temperature alloy steel	<b>9,317</b>	9,837	3,694
Conversion service	<b>2,011</b>	2,137	3,030
Other	<b>369</b>	410	367
<b>Total net sales</b>	<b>\$ 229,936</b>	\$ 203,873	\$ 170,022

**RAW MATERIALS**

The Company's Bridgeville facility depends on the delivery of key raw materials for its day-to-day operations. These key raw materials are ferrous and non-ferrous scrap metal and alloys, primarily consisting of nickel, chrome, molybdenum and copper. Scrap metal is primarily generated by industrial sources and is purchased through a number of scrap brokers and dealers. Alloys are generally purchased from domestic agents and originate in Australia, Canada, China, Russia and South Africa. Political disruptions in countries such as these could cause supply interruptions and affect the availability and price of the raw materials purchased by the Company.

The Bridgeville facility supplies semi-finished specialty steel products as starting materials to the Company's Titusville and Dunkirk facilities. Semi-finished specialty steel starting materials, not capable of being produced by the Company at a competitive cost, are purchased from other suppliers. The Company generally purchases these starting materials from steel strip coil suppliers, extruders, flat rolled producers and service centers. The Company believes that adequate supplies of starting material will continue to be available.

The cost of raw materials represents more than 50% of the Company's total cost of products sold in 2007 and 2006 due to significant increases in transaction prices for raw materials purchased. Raw material prices vary based on numerous factors, including quality, and are subject to frequent market fluctuations. Future raw material prices can not be predicted with any degree of certainty. Therefore, the Company does not maintain any long-term written agreements with any of its raw material suppliers.

The Company has implemented a sales price surcharge mechanism on its products to help offset the impact of raw material price fluctuations. For substantially all semi-finished products, the surcharge is calculated at the time of order entry, based on average raw material prices reported for the previous 20-day period. For substantially all finished products, the surcharge is calculated based on average raw material prices reported for the previous 20-day period from the promised ship date. While the material surcharge mechanism is designed to offset modest fluctuations in raw material prices, it can not immediately absorb significant spikes in raw material prices. A material change in raw material prices within a short period of time could have a material adverse effect on the financial results of the Company, and there can be no assurance that the raw material surcharge mechanism will completely offset immediate changes in the Company's raw material costs.

**ENERGY AGREEMENTS**

The production of specialty steel requires the ready availability of substantial amounts of electricity and natural gas for which the Company negotiates competitive agreements for the supply of electricity and natural gas. While the Company believes that its energy agreements allow it to compete effectively within the specialty steel industry, the potential of curtailments exists as a result of decreased supplies during periods of increased demand for electricity and natural gas. These interruptions not only can adversely affect the operating performance of the Company, but also can lead to increased costs. In 2005, the Company implemented a sales price surcharge mechanism on its products to help offset the impact of natural gas price fluctuations.

**CUSTOMERS**

The Company's customer base increased from 504 customers at December 31, 2006 to 515 customers at December 31, 2007. The Company's five largest customers in the aggregate accounted for approximately 49% and 43% of net sales for the years ended December 31, 2007 and 2006, respectively. Sales to Fry Steel, Carpenter Technology Corporation (CRS) and Reliance Steel & Aluminum accounted for 13.8%, 13.2% and 10.5% of the Company's net sales for the year ended December 31, 2007, respectively, and accounted for 10.4%, 12.5% and 10.5% of the

## Edgar Filing: UNIVERSAL STAINLESS & ALLOY PRODUCTS INC - Form 10-K

Company's net sales for the year ended December 31, 2006, respectively. The accounts receivable balances from these customers comprised approximately 21% and 23% of total accounts receivable at December 31, 2007 and 2006, respectively. No other customer accounted for more than 10% of the Company's net sales for the years ended December 31, 2007 and 2006.



## Table of Contents

The Company maintains a supply contract agreement with Talley Metals Technology, Inc., a subsidiary of CRS ( Talley Metals ), which continues to automatically renew with the placement of new orders each month and requires a 90-day written notice to terminate by either party. Talley Metals is required under the agreement to purchase a minimum of 1,000 tons of stainless reroll billet products each calendar month and average at least 1,250 tons per month during the last 12-month period. The value of the contract on a monthly basis will depend on product mix and key raw material prices. During 2006 and 2007, Talley Metals did not comply with the monthly minimum purchase requirement due to market conditions. The Company has granted a waiver and expects to continue granting a waiver from this requirement until market conditions improve.

## BACKLOG

The Company primarily manufactures products to meet specific customer orders. The Company's backlog of orders on hand as of December 31, 2007 was approximately \$85 million as compared to approximately \$120 million at the same time in 2006. The decrease in the backlog is primarily due to the impact of lower raw materials costs on the selling prices for semi-finished products and reduced product demand from the service center industry, allowing them to consume excess inventory during the second half of 2007. Customer orders are generally subject to cancellation with the payment of a penalty charge prior to delivery. The Company's backlog may not be indicative of actual sales and therefore should not be used as a direct measure of future revenue.

## COMPETITION

Competition in the Company's markets is based upon product quality, delivery capability, customer service and price. Maintaining high standards of product quality, while responding quickly to customer needs and keeping production costs at competitive levels, is essential to the Company's ability to compete in its markets.

Annual domestic U.S. consumption of specialty steel products of the type manufactured by the Company approximates one million tons. The Company chooses to restrict its participation in this market by limiting the volume of commodity stainless steel products it markets because of the highly competitive nature of the commodity business.

The Company believes that nine domestic companies that manufacture one or more similar specialty steel products are significant competitors, including Allegheny Technologies Incorporated ( ATI ) and CRS. There are many smaller producing companies and material converters in the United States that are also considered to be competitors of the Company.

High import penetration of specialty steel products, especially stainless and tool steels, also impacts the competitive nature within the United States. Unfair pricing practices by foreign producers have resulted in high import penetration into the U.S. markets in which the Company participates. According to SSINA, import penetration for the years ended December 31, 2006 and 2005 was 52% and 53%, respectively, for stainless bar, and 44% and 63%, respectively, for stainless rod. Import penetration was higher than these levels during the first eleven months of 2007, with stainless bar at 54% and stainless rod 49% import penetration.

The Continued Dumping and Subsidy Offset Act of 2000 (the CDSOA ) provides for payment of import duties collected by the U.S. Treasury to domestic companies injured by unfair foreign trade practices. The assets purchased for the operations of Dunkirk Specialty Steel were previously owned and operated by AL Tech Specialty Steel, Inc. and Empire Specialty Steel, Inc. During their ownership, both organizations participated in several anti-dumping lawsuits with other domestic specialty steel producers. The Company has joined other domestic producers in the filing of trade actions against foreign producers.

In December 2006, the Company received a net payment of \$463,000 as its 2006 award, and, in November 2007, the Company received a net payment of \$586,000 as its 2007 award. Benefits awarded from the CDSOA expired on September 30, 2007. Future benefits are dependent on the amount of undistributed import duties collected as of September 30, 2007 and the relationship of Dunkirk Specialty Steel's claim in relation to claims filed by other domestic specialty steel producers.

## EMPLOYEE RELATIONS

The Company considers the maintenance of good relations with its employees to be important to the successful conduct of its business. The Company has profit-sharing plans for certain salaried employees and for all of its employees represented by United Steelworkers (the USW ) and has equity ownership programs for all of its eligible employees, in an effort to forge an alliance between its employees' interests and those of the Company's stockholders. At December 31, 2007, the Company had 308 employees at its Bridgeville facility, 49 employees at its Titusville facility and 176 employees at its Dunkirk facility, of which 246, 42 and 151 were USW members, respectively.



**Table of Contents****Collective Bargaining Agreements**

The Company recognizes the USW as the exclusive representative for the Company's hourly employees with respect to the terms and conditions of their employment. The Company has entered into the following collective bargaining agreements:

Facility	Commencement Date	Expiration Date
Bridgeville	December 2002	August 2008
Titusville	October 2005	September 2010
Dunkirk	November 2007	October 2012

The Company believes a critical component of its collective bargaining agreements is the inclusion of a profit sharing plan. Under the plans, the hourly employees are entitled to receive 8.5% of their respective facilities' annual pretax profits in excess of \$1.0 million at Bridgeville and Dunkirk, and in excess of \$500,000 at Titusville.

**Employee Benefit Plans**

The Company provides group life and health insurance plans for its hourly and salaried employees. The Company also maintains separate 401(k) retirement plans for its hourly and salaried employees. Pursuant to each 401(k) plan, participants may elect to make pre-tax and after-tax contributions, subject to certain limitations imposed under the Internal Revenue Code of 1986, as amended. In addition, the Company makes periodic contributions to the 401(k) plans based on service, except as described below.

The Company also participates in the Steelworkers Pension Trust (the Trust), a multi-employer defined-benefit pension plan that is open to all hourly and salaried employees associated with the Bridgeville facility. The Company makes periodic contributions to the Trust based on hours worked at a fixed rate for each hourly employee and a fixed monthly contribution on behalf of each salaried employee. The hourly employees may continue their contributions to the 401(k) retirement plan even if the Company contributions cease. The amount of the contribution for salaried employees will be dependent upon their contribution to the 401(k) retirement plan.

**Employee Stock Purchase Plan**

Under the 1996 Employee Stock Purchase Plan, as amended (the Plan), the Company is authorized to issue up to 150,000 shares of Common Stock to its full-time employees, nearly all of whom are eligible to participate. Under the terms of the Plan, employees can choose as of January 1 and July 1 of each year to have up to 10% of their total earnings withheld to purchase up to 100 shares of the Company's Common Stock each six-month period. The purchase price of the stock is 85% of the lower of its beginning-of-the-period or end-of-the-period market prices. At December 31, 2007, the Company had issued 96,312 shares of Common Stock since the plan's inception.

**Safety**

The Company has established and seeks to maintain appropriate safety standards and policies for its employees. To encourage plant safety, the USW agreements provide that employees will be entitled to receive 50% of the savings, if any, of reduced workers' compensation insurance premiums obtained due to reductions in the state experience modifier issued to the Company.

**ENVIRONMENTAL**

The Company is subject to federal, state and local environmental laws and regulations (collectively, Environmental Laws), including those governing discharges of pollutants into the air and water, and the generation, handling and disposal of hazardous and non-hazardous substances. The Company monitors its compliance with Environmental Laws applicable to it and, accordingly, believes that it is currently in compliance with all laws and regulations in all material respects. The Company is subject periodically to environmental compliance reviews by various regulatory offices. The Company may be liable for the remediation of contamination associated with generation, handling and disposal activities. Environmental costs could be incurred, which may be significant, related to environmental compliance, at any time or from time to time in the future.

**EXECUTIVE OFFICERS**

The following table sets forth, as of February 29, 2008, certain information with respect to the executive officers of the Company:

Edgar Filing: UNIVERSAL STAINLESS & ALLOY PRODUCTS INC - Form 10-K

<b>NAME (AGE)</b>	<b>EXECUTIVE OFFICER SINCE</b>	<b>POSITION</b>
Dennis M. Oates (55)	2008	President and Chief Executive Officer
Paul McGrath (56)	1996	Vice President of Administration, General Counsel and Secretary
Richard M. Ubinger (48)	1994	Vice President of Finance, Chief Financial Officer and Treasurer

## **Table of Contents**

On December 26, 2007, the Company announced the appointment of Dennis M. Oates as President and Chief Executive Officer of the Company effective January 2, 2008. Mr. Oates was named to the Company's Board of Directors on October 19, 2007. Mr. Oates previously served as Senior Vice President of the Specialty Alloys Operations of Carpenter Technology Corporation from 2003 to July 2007. Mr. Oates also served as President and Chief Executive Officer of TW Metals from 1998 to 2003.

Paul A. McGrath has been Vice President of Administration of the Company since January 2007, General Counsel since January 1995 and was appointed Secretary in May 1996. Mr. McGrath served as Vice President of Operations from March 2001 to December 2006. Prior thereto, he was employed by Westinghouse Electric Corporation for approximately 24 years in various management positions.

Richard M. Ubinger has been Vice President of Finance of the Company since March 2001, Chief Financial Officer and Principal Accounting Officer since August 1994 and was appointed Assistant Secretary in November 1995 and Treasurer in May 1996. From 1981 to 1994, Mr. Ubinger was employed by Price Waterhouse LLP. Mr. Ubinger is a Certified Public Accountant.

## **PATENTS AND TRADEMARKS**

The Company does not consider its business to be materially dependent on patent or trademark protection, and believes it owns or maintains effective licenses covering all the intellectual property used in its business. The Company seeks to protect its proprietary information by use of confidentiality and non-competition agreements with certain employees.

## **AVAILABLE INFORMATION**

Copies of the Company's Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, current reports on Form 8-K, and any amendments to those reports, as well as proxy and information statements that we file with the Securities and Exchange Commission (the "SEC"), are available free of charge on the Company's website at [www.univstainless.com](http://www.univstainless.com) as soon as reasonably practicable after such reports are filed with the SEC. The contents of our website are not part of this Form 10-K. You also may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. You may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC maintains an Internet site at [www.sec.gov](http://www.sec.gov) that contains reports, proxy and information statements and other information regarding issuers, like the Company, that file electronically with the SEC.

## **ITEM 1A. RISK FACTORS**

The Company's business and results of operations are subject to a wide range of substantial business and economic factors including, but not limited to, the factors discussed below, many of which are not within the Company's control. See the information under the heading "Forward-Looking Information Safe Harbor" in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, of this Annual Report on Form 10-K.

## **SIGNIFICANT CUSTOMERS AND CONCENTRATED CUSTOMER BASE**

Net sales to the Company's three largest customers and their affiliates approximated 38% and 34% of total 2007 and 2006 sales, respectively. The accounts receivable balances from these three customers comprised approximately 21% and 23% of total accounts receivable at December 31, 2007 and 2006, respectively. An adverse change in, or termination of, the Company's relationship with one or more of its major customers or one or more of its market segments could have a material adverse effect upon the Company. See the information under the heading "Customers" in Item 1, Business, of this Annual Report on Form 10-K.

## **COMPETITION**

The Company competes with domestic and foreign sources of specialty steel products. In addition, many of the finished products sold by the Company's customers are in direct competition with finished products manufactured by foreign sources, which may affect the demand for those customers' products. Any competitive factors that adversely affect the market for finished products manufactured by the Company or its customers could indirectly adversely affect the demand for the Company's semi-finished products. Additionally, the Company's products compete with products fashioned from alternative materials such as aluminum, composites and plastics, the production of which includes domestic and foreign enterprises. Competition in the Company's field is intense and is expected to continue to be so in the foreseeable future. There can be no assurance that the Company will be able to compete successfully in the future. See the information under the heading "Competition" in Item 1, Business, of this Annual Report on Form 10-K.

AEROSPACE MARKET

Approximately 45% of the Company's sales represent products sold to customers in the aerospace market. The aerospace market is historically cyclical due to both external and internal market factors. These factors include general economic conditions, airline profitability, demand for air travel, age of fleets, varying fuel and labor costs, price competition, and international and domestic political conditions such as military conflict and the threat of terrorism. The length and degree of cyclical fluctuation can be influenced by any one or a combination of these factors and therefore are difficult to predict with certainty. A downturn in the aerospace industry would adversely affect the demand for products and/or the prices at which the Company is able to sell its products, and its results of operations, business and financial condition could be materially adversely affected.

## **Table of Contents**

### **SUPPLY OF RAW MATERIALS AND COST OF RAW MATERIALS**

The Company relies on a limited number of suppliers, some of which are foreign owned, for its raw material needs. Raw material prices are affected by cyclical, seasonal and other market factors. Alloys consumed by the Company are primarily available from foreign sources, some of which are located in countries that may be subject to unstable political and economic conditions. Those conditions might disrupt supplies or affect the prices of the raw materials used by the Company. The Company does not maintain long-term supply agreements with any of its independent suppliers. If its supply of raw materials were interrupted, the Company might not be able to obtain sufficient quantities of raw materials, or obtain sufficient quantities of such materials at satisfactory prices, which, in either case, could adversely affect the Company's results of operations. In addition, significant volatility in the price of the Company's principal raw materials could adversely affect the Company's financial results. See the information under the headings "Raw Materials" in Item 1, Business, and "Liquidity and Capital Resources" in Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, of this Annual Report on Form 10-K.

### **RELIANCE ON ENERGY AGREEMENTS**

The manufacturing of specialty steels is an energy-intensive industry. While the Company believes that its energy agreements allow it to compete effectively within the specialty steel industry, the Company is subjected to curtailments as a result of decreased supplies and increased demand for electricity and natural gas. These interruptions not only can adversely affect the operating performance of the Company, but also can lead to increased costs for energy. See the information under the heading "Energy Agreements" in Item 1, Business, of this Annual Report on Form 10-K.

### **LABOR MATTERS**

The Company has 439 employees out of a total of 533 who are covered under collective bargaining agreements. The collective bargaining agreement for the 246 Bridgeville facility employees will expire in August 2008. There can be no assurance that the Company will succeed in concluding a collective bargaining agreement with the union to replace the one that expires.

### **RELIANCE ON CRITICAL MANUFACTURING EQUIPMENT**

The Company's manufacturing processes are dependent upon certain critical pieces of specialty steel making equipment, such as the Company's 50-ton electric-arc furnace and AOD (Argon Oxygen Decarburization) vessel, its ESR (Electro Slag Remelt) and VAR furnaces, and its universal rolling mill. In the event a critical piece of equipment should become inoperative as a result of unexpected equipment failure, there can be no assurance that the Company's operations would not be substantially curtailed, which may have a negative effect on the Company's financial results. See Item 2, Properties.

### **ITEM 1B. UNRESOLVED STAFF COMMENTS**

None.

### **ITEM 2. PROPERTIES**

The Company owns its Bridgeville facility, which consists of approximately 600,000 square feet of floor space and the Company's executive offices on approximately 74 acres. The Bridgeville facility contains melting, remelting, conditioning, rolling, annealing and various other processing equipment. Substantially all products shipped from the Bridgeville facility are processed through its melt shop and universal rolling mill operations.

The Company owns its Titusville facility, which consists of seven buildings on approximately 10 acres, including two principal buildings of approximately 265,000 square feet in total area. The Titusville facility contains five VAR furnaces and various rolling and finishing equipment.

The Company owns its Dunkirk facility, which consists of approximately 800,000 square feet of floor space on approximately 81 acres. The Dunkirk facility processes semi-finished billet and bar stock through one or more of its four rolling mills. The products are then finished and shipped as finished bar, rod and wire products.

## Edgar Filing: UNIVERSAL STAINLESS & ALLOY PRODUCTS INC - Form 10-K

Specialty steel production is a capital-intensive industry. The Company believes that its facilities and equipment are suitable for its present needs. The Company believes, however, that it will continue to require capital from time to time to add new equipment and to repair or replace existing equipment to remain competitive and to enable it to manufacture quality products and provide delivery and other support service assurances to its customers.



**Table of Contents****ITEM 3. LEGAL PROCEEDINGS**

On June 29, 2001, suit was filed against the Company in the Court of Common Pleas of Allegheny County, Pennsylvania by Teledyne Technologies Incorporated ( Teledyne ). The suit alleged that steel product manufactured by the Company was defective and that the Company was or should have been aware of the defects.

On May 31, 2007, the Company and Teledyne agreed to a complete settlement of this suit. Under the terms of the settlement, which contains a confidentiality provision, both parties released all claims against the other party in exchange for cash and other consideration. The net impact of this settlement, including professional fees, on the Company's net income after tax was \$517,000.

In addition, from time to time, various lawsuits and claims have been or may be asserted against the Company relating to the conduct of its business, including routine litigation relating to commercial and employment matters. The outcome of any litigation can not be predicted with certainty, and some lawsuits may be determined adversely to the Company. Management does not believe, based on information presently available, that the ultimate outcome of any pending matters is likely to have a material adverse effect on the Company's financial condition or liquidity, although the resolution in any quarter of one or more matters may have a material adverse effect on results of operations for that period.

**ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted to a vote of security holders during the fourth quarter of 2007.

**PART II****ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

At December 31, 2007, a total of 6,930,294 shares of the Company's Common Stock, par value \$.001 per share, were issued and held by approximately 147 holders of record. There were 270,795 shares of the issued Common Stock of the Company held in treasury at December 31, 2007.

Certain holders of Common Stock and the Company are party to a stockholder agreement. That agreement maintains in effect certain registration rights granted to non-management stockholders, which provides to them two demand registration rights exercisable at any time upon written request for the registration of Restricted Shares of Common Stock having an aggregate net offering price of at least \$5,000,000.

**PRICE RANGE OF COMMON STOCK**

The Common Stock is listed on the NASDAQ Global Market under the symbol USAP. The following table sets forth the range of high and low sale prices per share of Common Stock, for the periods indicated below:

	2007		2006	
	High	Low	High	Low
First quarter	\$ 51.80	\$ 31.79	\$ 26.25	\$ 14.94
Second quarter	\$ 54.17	\$ 34.98	\$ 37.05	\$ 22.52
Third quarter	\$ 42.66	\$ 28.48	\$ 30.47	\$ 21.62
Fourth quarter	\$ 41.71	\$ 29.88	\$ 37.90	\$ 21.56

**EQUITY COMPENSATION PLAN INFORMATION**

Securities authorized for issuance under equity compensation plans at December 31, 2007 are as follows:

Edgar Filing: UNIVERSAL STAINLESS & ALLOY PRODUCTS INC - Form 10-K

Plan Category	Number of shares to be issued upon exercise of outstanding options	Weighted-average exercise price of outstanding options	Number of shares remaining available for future issuance under equity compensation plans <sup>A</sup>
Equity compensation plans approved by security holders	403,650	\$ 18.14	447,356

<sup>A</sup> Includes 393,668 shares of Common Stock on stock options not issued under the Stock Incentive Plan and 53,688 available under the 1996 Employee Stock Purchase Plan, as amended.

PERFORMANCE GRAPH

The performance graph below compares the cumulative total shareholder return on the Company's stock with the cumulative total return on the equity securities of NASDAQ Market Index and a peer group selected by the Company consisting of public companies ATI and CRS. The graph assumes an investment of \$100 on December 31, 2002 and reinvestment of dividends, if any, on the date of dividend payment. The performance graph represents past performance and should not be considered to be an indication of future performance.

**Table of Contents**

**COMPARISON OF 5-YEAR CUMULATIVE TOTAL RETURN  
AMONG UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.,  
NASDAQ MARKET INDEX AND PEER GROUP INDEX**

COMPANY/PEER/MARKET	FISCAL YEAR ENDING					
	12/31/2002	12/31/2003	12/31/2004	12/31/2005	12/30/2006	12/29/2007
Universal Stainless & Alloy Products, Inc.	\$ 100.00	\$ 178.51	\$ 245.49	\$ 247.93	\$ 553.39	\$ 587.93
Company Selected Peer Group	100.00	229.61	410.78	610.62	1,321.29	1,426.42
NASDAQ Market Index	100.00	150.36	163.00	166.58	183.68	201.91

PREFERRED STOCK

The Company's Certificate of Incorporation provides that the Company may, by vote of its Board of Directors, issue up to 1,980,000 shares of Preferred Stock. The Preferred Stock may have rights, preferences, privileges and restrictions thereon, including dividend rights, dividend rates, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences and the number of shares constituting any series or designation of such series, without further vote or action by the stockholders. The issuance of Preferred Stock may have the effect of delaying, deferring or preventing a change in control of the Company without further action by the stockholders and may adversely affect the voting and other rights of the holders of Common Stock. The issuance of Preferred Stock with voting and conversion rights may adversely affect the voting power of the holders of Common Stock, including the loss of voting control to others.

The Company has no outstanding Preferred Stock and has no plans to issue any of the authorized Preferred Stock.

**DIVIDENDS**

The Company has never paid a cash dividend on its Common Stock. The Company's Credit Agreement with PNC Bank, National Association (PNC Bank) currently limits the payment of cash dividends payable on its Common Stock to 50% of the Company's excess cash flow per fiscal year. Excess cash flow represents the amount of the Company's earnings before interest, taxes, depreciation and amortization that is greater than the sum of the Company's payments for interest, income taxes, the principal portion of long-term debt and capital lease obligations, and capital expenditures.

**Table of Contents****ITEM 6. SELECTED FINANCIAL DATA**

<b>For the years ended December 31, (dollars in thousands, except per share amounts)</b>	<b>2007</b>	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
<b>SUMMARY OF OPERATIONS</b>					
Net sales	\$ 229,936	\$ 203,873	\$ 170,022	\$ 120,642	\$ 68,989
Operating income (loss)	33,407	32,359	20,145	10,955	(2,394)
Net income (loss)	22,504	20,590	12,758	7,553	(1,425)
<b>FINANCIAL POSITION AT YEAR-END</b>					
Cash and cash equivalents	\$ 10,648	\$ 2,909	\$ 620	\$ 241	\$ 4,735
Total assets	164,296	155,287	129,239	108,536	84,935
Long-term debt	1,453	17,228	17,317	12,190	5,599
Stockholders' equity	129,602	104,654	81,134	67,365	59,442
<b>COMMON SHARE DATA</b>					
Basic earnings (loss) per share	\$ 3.39	\$ 3.19	\$ 2.00	\$ 1.20	\$ (0.23)
Diluted earnings (loss) per share	3.32	3.11	1.97	1.18	(0.23)

The restatement of maintenance expenses for the four years ended December 31, 2006 changed previously reported financial data by the following amounts:

	<b>Increase (Decrease) in Previously Reported Amounts</b>			
	<b>2006</b>	<b>2005</b>	<b>2004</b>	<b>2003</b>
<i>(dollars in thousands, except per share amounts)</i>				
Change in cost of products sold	\$ 40	\$ 484	\$ (686)	\$ 12
Change in net income	(24)	(298)	421	(8)
Change in earnings per common share:	&nbsp;			