

UNIVERSAL STAINLESS & ALLOY PRODUCTS INC

Form 10-Q

August 07, 2015

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2015

OR

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

For the Transition Period from            to

Commission File Number 000-25032

UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE

25-1724540

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(State or other jurisdiction of (IRS Employer

incorporation or organization) 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)

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 whether the registrant has submitted electronically and posted on its corporate Web site, 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 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 definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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 in Rule 12b-2 of the Exchange Act). Yes No

As of July 27, 2015, there were 7,102,924 shares of the Registrant's common stock outstanding.

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Universal Stainless & Alloy Products, Inc.

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## Part I. FINANCIAL INFORMATION

## Item 1. FINANCIAL STATEMENTS

## UNIVERSAL STAINLESS &amp; ALLOY PRODUCTS, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(Dollars in Thousands, Except Per Share Information)

(Unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Net sales	\$ 49,610	\$ 52,309	\$ 105,593	\$ 98,976
Cost of products sold	44,424	43,899	94,697	84,506
Gross margin	5,186	8,410	10,896	14,470
Selling, general and administrative expenses	4,961	5,169	9,655	9,797
Operating income	225	3,241	1,241	4,673
Interest expense and other financing costs	(765)	(1,042)	(1,547)	(1,905)
Other income (expense), net	11	(1)	(33)	3
(Loss) income before income taxes	(529)	2,198	(339)	2,771
(Benefit) provision for income taxes	(173)	749	(108)	1,821
Net (loss) income	\$ (356)	\$ 1,449	\$ (231)	\$ 950
Net (loss) income per common share - Basic	\$ (0.05)	\$ 0.21	\$ (0.03)	\$ 0.14
Net (loss) income per common share - Diluted	\$ (0.05)	\$ 0.20	\$ (0.03)	\$ 0.13
Weighted average shares of common stock outstanding				
Basic	7,061,545	7,031,041	7,058,026	7,022,983
Diluted	7,061,545	7,110,761	7,058,026	7,112,093

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

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## UNIVERSAL STAINLESS &amp; ALLOY PRODUCTS, INC.

## CONSOLIDATED BALANCE SHEETS

(Dollars in Thousands)

	June 30, 2015	December 31, 2014
	(Unaudited)	(Derived from audited statements)
<b>ASSETS</b>		
Current assets:		
Cash	\$ 420	\$ 142
Accounts receivable (less allowance for doubtful accounts of \$3 and \$17, respectively)	30,180	29,057
Inventory, net	99,021	101,070
Deferred income taxes	7,227	9,683
Other current assets	3,719	2,681
Total current assets	140,567	142,633
Property, plant and equipment, net	197,923	199,795
Goodwill	20,268	20,268
Other long-term assets	1,409	1,861
Total assets	\$ 360,167	\$ 364,557
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 19,178	\$ 25,009
Accrued employment costs	3,229	6,011
Current portion of long-term debt	3,000	3,000
Other current liabilities	593	861
Total current liabilities	26,000	34,881
Long-term debt	89,711	83,875
Deferred income taxes	39,650	42,108
Other long-term liabilities	58	63
Total liabilities	155,419	160,927
Commitments and contingencies (Note 7)		

Stockholders' equity:		
Senior preferred stock, par value \$0.001 per share; 1,980,000 shares authorized; 0 shares issued and outstanding	-	-
Common stock, par value \$0.001 per share; 20,000,000 shares authorized; 7,395,779 and 7,371,018 shares issued, respectively	7	7
Additional paid-in capital	54,159	52,810
Retained earnings	152,872	153,103
Treasury stock, at cost; 292,855 common shares held	(2,290)	(2,290)
Total stockholders' equity	204,748	203,630
Total liabilities and stockholders' equity	\$ 360,167	\$ 364,557

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

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## UNIVERSAL STAINLESS &amp; ALLOY PRODUCTS, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOW

(Dollars in Thousands)

(Unaudited)

	Six months ended June 30,	
	2015	2014
Operating Activities:		
Net (loss) income	\$ (231)	\$ 950
Adjustments to reconcile net (loss) income to net cash (used in) provided by operating activities:		
Depreciation and amortization	9,181	8,723
Deferred income tax	(2)	1,347
Share-based compensation expense	961	1,032
Changes in assets and liabilities:		
Accounts receivable, net	(1,123)	(10,477)
Inventory, net	1,011	(14,495)
Accounts payable	(5,831)	12,497
Accrued employment costs	(2,782)	822
Income taxes	(272)	433
Other, net	(1,039)	(402)
Net cash (used in) provided by operating activities	(127)	430
Investing Activity:		
Capital expenditures	(5,819)	(3,472)
Net cash used in investing activity	(5,819)	(3,472)
Financing Activities:		
Borrowings under revolving credit facility	63,848	45,207
Payments on revolving credit facility	(56,512)	(41,698)
Payments on term loan facility	(1,500)	(1,500)
Proceeds from the issuance of common stock	388	891



Net cash provided by financing activities	6,224	2,900
Net increase (decrease) in cash	278	(142)
Cash at beginning of period	142	307
Cash at end of period	\$ 420	\$ 165

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

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UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.

NOTES TO THE UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Note 1: Nature of Business and Basis of Presentation

Universal Stainless & Alloy Products, Inc., and its wholly-owned subsidiaries (“Universal”, “we”, “our” or the “Company”), manufacture and market semi-finished and finished specialty steel products, including stainless steel, nickel alloys, tool steel and certain other alloyed steels. Our manufacturing process involves melting, remelting, heat treating, hot and cold rolling, forging, machining and cold drawing of semi-finished and finished specialty steels. Our products are sold to service centers, forgers, rerollers, original equipment manufacturers and wire redrawers. Our customers further process our products for use in a variety of industries, including the aerospace, power generation, oil and gas and heavy equipment manufacturing industries. We also perform conversion services on materials supplied by customers.

The accompanying unaudited consolidated statements include the accounts of Universal Stainless & Alloy Products, Inc. and its subsidiaries and are prepared in accordance with U.S. generally accepted accounting principles (“U.S. GAAP”) for interim financial reports and the instructions for Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, certain information and footnote disclosures normally included in financial statements prepared under U.S. GAAP have been condensed or omitted pursuant to such regulations. However, we believe that the disclosures are adequate to make the information presented not misleading. These consolidated financial statements should be read in conjunction with our most recently audited financial statements and the notes thereto included in our Annual Report on Form 10-K as filed with the Securities and Exchange Commission. In the opinion of management, the accompanying financial statements include all adjustments necessary to present a fair presentation of the consolidated financial statements for the periods shown. Interim results are not necessarily indicative of the operating results for the full fiscal year or any future period. The preparation of these financial statements in conformity with U.S. GAAP requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and disclosure of contingent assets and liabilities. Actual results may differ from our estimates. The consolidated financial statements include our accounts and the accounts of our wholly-owned subsidiaries. All intercompany transactions and balances have been eliminated.

Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) 2014-09 “Revenue from Contracts with Customers (Topic 606).” This topic converges the guidance within U.S. GAAP and International Financial Reporting Standards and supersedes Accounting Standards Codification 605, Revenue Recognition. The new standard requires companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively, and improve guidance for multiple-element arrangements. The new guidance is effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period, and early application is not permitted. We are currently evaluating the impact that this standard will have on our consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, "Simplifying the Presentation of Debt Issuance Costs." ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The new guidance is effective for annual reporting periods beginning after December 15, 2015, including interim reporting periods within

that reporting period, and early application is permitted. We are currently evaluating the impact that this standard will have on our consolidated financial statements.

In July 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update 2015-11, "Simplifying the Measurement of Inventory" ("ASU 2015-11") to simplify the guidance on the subsequent measurement of inventory, excluding inventory measured using last-in, first out or the retail inventory method. Under the new standard, inventory should be at the lower of cost and net realizable value. The new accounting guidance is effective for interim and annual periods beginning after December 15, 2016 with early adoption permitted. The Company is currently evaluating the impact of the pending adoption of ASU 2015-11 on the Company's consolidated financial statements.

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## Note 2: Net (loss) income per Common Share

The following table sets forth the computation of basic and diluted net (loss) income per common share:

	Three months ended		Six months ended	
	June 30,		June 30,	
(dollars in thousands, except per share amounts)	2015	2014	2015	2014
Numerator:				
Net (loss) income	\$ (356)	\$ 1,449	\$ (231)	\$ 950
Adjustment for interest expense on convertible notes (A)	-	-	-	-
Net (loss) income, as adjusted	\$ (356)	\$ 1,449	\$ (231)	\$ 950
Denominator:				
Weighted average number of shares of common stock outstanding	7,061,545	7,031,041	7,058,026	7,022,983
Weighted average effect of dilutive stock options and other stock compensation	-	79,720	-	89,110
Weighted average number of shares of common stock outstanding, as adjusted	7,061,545	7,110,761	7,058,026	7,112,093
Net (loss) income per common share:				
Net (loss) income per common share - Basic	\$ (0.05)	\$ 0.21	\$ (0.03)	\$ 0.14
Net (loss) income per common share - Diluted	\$ (0.05)	\$ 0.20	\$ (0.03)	\$ 0.13

(A) An adjustment for interest expense on convertible notes was excluded from the (loss) income per share calculation for the three and six months ended June 30, 2015 and 2014 as a result of the convertible notes being antidilutive.

We had options to purchase 587,550 and 352,800 shares of common stock outstanding at an average price of \$32.96 and \$36.23 for the three months ended June 30, 2015 and 2014, respectively, which were excluded in the computation of diluted net (loss) income per common share. We had options to purchase 587,550 and 268,300 shares of common stock outstanding at an average price of \$32.96 and \$36.55 for the six months ended June 30, 2015 and 2014,

respectively, which were excluded in the computation of diluted net (loss) income per common share. These outstanding options were not included in the computation of diluted net (loss) income per common share because their respective exercise prices were greater than the average market price of our common stock. The calculation of diluted earnings per share for the three and six months ended June 30, 2015 and 2014 excluded 428,888 and 428,177 shares, respectively, for the assumed conversion of convertible notes as a result of being antidilutive. In addition, the calculation of dilutive earnings per share for the three and six months ended June 30, 2015 excluded 27,598 and 35,757 shares, respectively, for the assumed exercise of stock options and restricted stock under our stock share incentive plans, as a result of being in a net loss position.

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## Note 3: Inventory

Our raw material and starting stock inventory is primarily comprised of ferrous and non-ferrous scrap metal and alloys such as nickel, chrome, molybdenum, cobalt and copper. Our semi-finished and finished steel products are work-in-process in various stages of production or are finished products waiting to be shipped to our customers. Operating materials are primarily comprised of forge dies and production molds and rolls that are consumed over their useful lives. During the six months ended June 30, 2015 and 2014, we amortized these operating materials in the amount of \$1,039,000 and \$838,000, respectively. This expense is recorded as a component of cost of products sold on the consolidated statements of operations and included as a part of our total depreciation and amortization on the consolidated statements of cash flows. Inventory is stated at the lower of cost or market with cost principally determined on a weighted average cost method. Such costs include the acquisition cost for raw materials and supplies, direct labor and applied manufacturing overhead. We assess market based upon actual and estimated transactions at or around the balance sheet date. Typically, we reserve for slow-moving inventory and inventory that is being evaluated under our quality control process. The reserves are based upon management's expected method of disposition. Inventories consisted of the following:

(in thousands)	June 30, 2015	December 31, 2014
Raw materials and starting stock	\$ 8,939	\$ 8,943
Semi-finished and finished steel products	81,971	84,816
Operating materials	8,960	8,759
Gross inventory	99,870	102,518
Inventory reserves	(849)	(1,448)
Total inventory, net	\$ 99,021	\$ 101,070

## Note 4: Goodwill

We test goodwill for impairment by either performing a qualitative evaluation or a two-step quantitative test, which involves comparing the estimated fair value of the associated reporting unit to its carrying value. The qualitative evaluation is an assessment of factors to determine whether it is more likely than not that fair value is less than its carrying amount. Factors considered as part of the qualitative assessment include entity-specific, industry, market and general economic conditions. We may elect to bypass this qualitative assessment and perform a two-step quantitative test. We test for goodwill impairment using a combination of valuation techniques, which include consideration of a market-based approach (guideline company method) and an income approach (discounted cash flow method), in determining fair value in the annual impairment test of goodwill. We believe that the combination of the valuation models provides a more appropriate valuation by taking into account different marketplace participant assumptions. Both methods utilize market data in the derivation of a value estimate and are forward-looking in

nature. The guideline assessment of future performance and the discounted cash flow method utilize a market-derived rate of return to discount anticipated performance.

We conduct our annual impairment test during the fourth quarter of each year. Other events and changes in circumstances may also require goodwill to be tested for impairment between annual measurement dates. While a decline in stock price and market capitalization is not specifically cited as a goodwill impairment indicator, a company's stock price and market capitalization should be considered in determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying value. Additionally, a significant decline in a company's stock price may suggest that an adverse change in the business climate may have caused the fair value of the reporting unit to fall below its carrying value. The financial and credit market volatility directly impacts our fair value measurement through our stock price that we use to determine our market capitalization. During times of volatility, significant judgment must be applied to determine whether credit or stock price changes are a short-term swing or a longer-term trend. As of June 30, 2015, the Company has experienced what it believes to be a short-term downward trend of its stock price which is consistent with the highly cyclical nature of the specialty metals industry. We do not believe there have been any events or circumstances that would require us to perform an interim goodwill impairment review; however, a sustained decline in our market capitalization below its book value could lead us to determine, in a future period, that an interim goodwill impairment review is required and may result in a non-cash impairment charge which would have a negative impact on our results of operations.

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## Note 5: Long-Term Debt

Long-term debt consisted of the following:

(in thousands)	June 30, 2015	December 31, 2014
Revolving credit facility	\$ 58,350	\$ 51,350
Convertible notes	20,000	20,000
Term loan	14,000	15,500
Swing loan credit facility	361	25
Total debt	92,711	86,875
Less: current portion of long-term debt	(3,000)	(3,000)
Long-term debt	\$ 89,711	\$ 83,875
Credit Facility		

We have a Credit Agreement (as amended to date, the "Credit Agreement") with a syndication of banks which provides for a \$105.0 million senior secured revolving credit facility (the "Revolver") and a \$20.0 million senior secured term loan facility (the "Term Loan" and together with the Revolver, the "Facilities") that expires in March 2017. Under the Credit Agreement, our loan availability under the Revolver ("Borrowing Base") is calculated monthly based upon our accounts receivable and inventory balances.

We are required to pay a commitment fee of 0.25% based on the daily unused portion of the Revolver. The Revolver also provides for up to \$7.0 million of swing loans so long as the sum of the outstanding swing loans and the outstanding borrowings under the Revolver do not exceed our Borrowing Base at any given time. The Term Loan is payable in quarterly installments in the principal amount of \$750,000, which began on July 1, 2013, with the balance of the Term Loan payable in full on March 19, 2017.

Amounts outstanding under the Facilities, at our option, will bear interest at either a base rate or a LIBOR-based rate (the "LIBOR Option"), in either case calculated in accordance with the terms of the Credit Agreement. We elected to use the LIBOR Option during the six months ended June 30, 2015, which was 1.94% at June 30, 2015. Interest on the Facilities is payable monthly.

We are required to maintain a leverage ratio not exceeding a ratio decreasing from 3.5 to 1.00 for the period June 30, 2015 to September 30, 2015, 3.25 to 1.00 at December 31, 2015 and 3.00 to 1.00 from March 31, 2016 through maturity. We are required to maintain a fixed charge coverage ratio of 1.1 to 1.0 to maturity. We were in compliance with our covenants at June 30, 2015 and December 31, 2014.



## Convertible Notes

In connection with the acquisition of the North Jackson facility, in August 2011, we issued \$20.0 million in convertible notes (the "Notes") to the sellers of the North Jackson facility as partial consideration of the acquisition. The Notes are subordinated obligations and rank junior to the Facilities. The Notes bear interest at a fixed rate of 4.0% per annum, payable in cash semi-annually in arrears on each June 18 and December 18, beginning on December 18, 2011. Unless earlier converted, the Notes mature and the unpaid principal balance is due on August 17, 2017. The Notes and any accrued and unpaid interest are convertible into shares of our common stock at the option of the holder at an initial conversion price of \$47.1675 per share of common stock. The conversion price associated with the Notes may be adjusted in certain circumstances. We may prepay any outstanding Notes, in whole or in part, during a fiscal quarter if our share price is greater than 140% of the then current conversion price for at least 20 of the trading days in the 30 consecutive trading day period ending on the last trading day of the immediately preceding quarter.

## Note 6: Fair Value Measurement

The fair value hierarchy has three levels based on the inputs used to determine fair value, which are as follows:

Level 1 — Unadjusted quoted prices available in active markets for the identical assets or liabilities at the measurement date.

Level 2 — Unadjusted quoted prices in active markets for similar assets or liabilities, or unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability.

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Level 3 — Unobservable inputs that cannot be corroborated by observable market data and reflect the use of significant management judgment. These values are generally determined using pricing models for which the assumptions utilize management's estimates of market participant assumptions.

The fair value hierarchy requires the use of observable market data when available. In instances where the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input significant to the fair value measurement in its entirety. Our assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including the consideration of inputs specific to the asset or liability.

The carrying amounts of our cash, accounts receivable and accounts payable approximated fair value at June 30, 2015 and December 31, 2014 due to their short-term maturities (Level 1). The fair value of the Term Loan, Revolver and swing loans at June 30, 2015 and December 31, 2014 approximated the carrying amount as the interest rate is based upon floating short-term interest rates (Level 2). At June 30, 2015 and December 31, 2014, the fair value of our Notes was approximately \$20.5 million (Level 2).

Note 7: Commitments and Contingencies

From time to time, various lawsuits and claims have been or may be asserted against us relating to the conduct of our business, including routine litigation relating to commercial and employment matters. The ultimate cost and outcome of any litigation or claim cannot be predicted with certainty. Management believes, based on information presently available, that the likelihood that the ultimate outcome of any such pending matter will have a material adverse effect on our financial condition, or liquidity or a material impact on our results of operations is remote, although the resolution of one or more of these matters may have a material adverse effect on our results of operations for the period in which the resolution occurs.

Note 8: Income Taxes

Management estimates the annual effective income tax rate quarterly, based on current annual forecasted results. Items unrelated to current year ordinary income are recognized entirely in the period identified as a discrete item of tax. The quarterly income tax provision is comprised of tax on ordinary income provided at the most recent estimated annual effective tax rate, increased or decreased for the tax effect of discrete items.

For the six months ended June 30, 2015 and 2014, our estimated annual effective tax rate applied to ordinary income was 29.0% and 34.4%, respectively.

Including the effect of discrete items, our effective tax rate for the six months ended June 30, 2015 and 2014 was 31.7% and 65.7%, respectively and for the three months ended June 30, 2015 and 2014 was 32.5% and 34.1% respectively. The effective tax rate for the three and six months ended June 30, 2014 was reflective of a net discrete tax expense of \$869,000. The \$869,000 of discrete tax expense primarily includes tax expense of \$596,000 associated with the New York state tax rate reduction to 0% for New York qualified manufacturers, and tax expense of \$247,000 associated with a Pennsylvania tax settlement related to certain expenses which had been deducted for state income tax purposes during the 2005-2007 tax years.



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ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains or incorporates forward looking statements within the meaning of the Private Securities Reform Act of 1995, which involves risks and uncertainties. The following information should be read in conjunction with the unaudited consolidated financial information and the notes thereto included in this Quarterly Report on Form 10-Q. You should not place undue reliance on these forward looking statements. Actual events or results may differ materially due to competitive factors and other factors referred to in Part 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2014, our other filings with the Securities and Exchange Commission and elsewhere in this Quarterly Report. These factors may cause our actual results to differ materially from any forward looking statement. These forward looking statements are based on current expectations, estimates, forecasts, and projections about the industry and markets in which we operate, and management’s beliefs and assumptions. In addition, other written or oral statements that constitute forward looking statements may be made by us or on our behalf. Words such as “expect,” “anticipate,” “intend,” “plan,” “believe,” “could,” “estimate,” “may,” “target,” variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties, and assumptions that are difficult to predict.

Business Overview

We manufacture and market semi-finished and finished specialty steel products, including stainless steel, nickel alloys, tool steel and certain other alloyed steels. Our manufacturing process involves melting, remelting, heat treating, hot and cold rolling, forging, machining and cold drawing of semi-finished and finished specialty steels. Our products are sold to rerollers, forgers, service centers, original equipment manufacturers and wire redrawers. Our customers further process our products for use in a variety of industries, including the aerospace, power generation, oil and gas and general industrial markets. We also perform conversion services on materials supplied by customers.

Sales in the second quarter of 2015 were \$49.6 million, a decrease of \$6.4 million, or 11.4%, from the first quarter of 2015 and a decrease of \$2.7 million, or 5.2%, from the second quarter of 2014. Sales were generally lower due to the reduction in surcharges caused by falling metal commodity prices and lower volume caused by customer inventory destocking related to the sharp decline in the exploration for oil and gas. Sales in the second quarter 2015 declined compared to the first quarter of 2015 in most targeted end use markets with aerospace down 10%, power generation down 30.7% and oil and gas down 32.6%. Sales to the heavy equipment market increased 24.6% due to strong automotive production activity and general industrial, conversion services and other sales increased 27.2% as customers took advantage of our unique capabilities for hot rolling and forging. Compared to the second quarter of 2014, sales to aerospace increased modestly by 0.6%, heavy equipment increased by 34.6%, power generation decreased 22.6%, oil and gas decreased 23.9% and general industrial, conversion services and other sales declined 5%. Through six months of 2015, sales of \$105.6 million are \$6.6 million, or 6.7%, greater than the comparable period of 2014 with all targeted end use markets except general industrial contributing positively. The decline in metal commodity prices and the price of oil led to the slowing in sales during the second quarter. During the second quarter of 2015, our sales of premium alloy products, which we define as all vacuum induction, melt (“VIM”) products, represented \$4.2 million, or 8.6%, of total net sales. This compared to a record first quarter 2015 premium alloy sales of \$5.0 million or 9.0%. Premium alloy sales in the first half of 2015 totaled \$9.3 million, or an increase of 33.5%

over the first half of 2014. Our premium alloy products are primarily sold to the aerospace end market. Our backlog, before surcharges, at June 30, 2015 was \$48.9 million, a decline of \$9.6 million, or 16.4%, compared to March 31, 2015, and a decline of \$12.2 million, or 20.0%, since December 31, 2014. Prices for key commodities such as nickel, molybdenum and iron scrap have fallen rapidly during 2015 and the fourth quarter of 2014 creating a misalignment between surcharges in sales and the melt costs of products shipped during the first and second quarters of 2015. In addition, the sudden drop in the price of a barrel of oil and related reduction in exploration activity has caused customers to destock their inventory positions across most end markets served by us. The combination of the misalignment of surcharges and melt costs, and the lower sales and production activity as customers destocked, led to gross profit margins of 10.5% in the second quarter 2015 and 10.2% in the first quarter of 2015, compared to 16.1% in the second quarter of 2014, 16.1% in the third quarter of 2014 and 16.8% in the fourth quarter of 2014.

Selling, General and Administrative expenses were \$5.0 million in the second quarter 2015 slightly below the \$5.2 million in the second quarter 2014, but 6.4% greater than the \$4.7 million reported in the first quarter 2015. The increase compared to the first quarter was attributable to increased employment costs incurred as the development of the organization proceeds. With a lower backlog, uncertainty in the oil & gas market, continuing decreases in commodity prices like nickel and molybdenum and destocking trends among customers, we believe that our third quarter 2015 sales will be somewhat lower than the second quarter of 2015. Given these current business conditions, we are taking steps to align spending with lower activity levels, reduce material costs and lower inventory during the third quarter. At the same time, we will continue to work on gaining customer approvals for our higher value added premium melted products to expand our revenue base as we move into future periods.

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## Results of Operations

Three months ended June 30, 2015 as compared to the three months ended June 30, 2014

(in thousands, except shipped ton information)	Three months ended June 30,					
	2015		2014		Dollar / ton variance	
	Amount	Percentage of net sales	Amount	Percentage of net sales		Percentage variance
Net sales:						
Stainless steel	\$ 36,955	74.5 %	\$ 42,045	80.4 %	\$ (5,090)	(12.1) %
High-strength low alloy steel	4,154	8.4	3,451	6.6	703	20.4
Tool steel	5,086	10.3	3,389	6.5	1,697	50.1
High-temperature alloy steel	2,051	4.1	1,795	3.4	256	14.3
Conversion services and other sales	1,364	2.7	1,629	3.1	(265)	(16.3)
Total net sales	49,610	100.0	52,309	100.0	(2,699)	(5.2)
Cost of products sold	44,424	89.5	43,899	83.9	525	1.2
Gross margin	5,186	10.5	8,410	16.1	(3,224)	(38.3)
Selling, general and administrative expenses	4,961	10.0	5,169	9.9	(208)	(4.0)
Operating income	225	0.5	3,241	6.2	(3,016)	(93.1)
Interest expense	(605)	(1.2)	(882)	(1.7)	277	(31.4)
Deferred financing amortization	(160)	(0.3)	(160)	(0.3)	-	0.0
Other income (expense), net	11	-	(1)	-	12	NM
(Loss) income before income taxes	(529)	(1.0)	2,198	4.2	(2,727)	(124.1)
(Benefit) provision for income taxes	(173)	(0.3)	749	1.4	(922)	(123.1)
Net (loss) income	\$ (356)	(0.7) %	\$ 1,449	2.8 %	\$ (1,805)	124.6
Tons shipped	8,909		9,921		(1,012)	(10.2) %
Sales dollars per shipped ton	\$ 5,569		\$ 5,273		\$ 296	5.6 %

NM – Not meaningful

## Market Segment Information

(in thousands)	Three months ended June 30,					
	2015		2014		Dollar variance	Percentage variance
	Amount	Percentage of net sales	Amount	Percentage of net sales		
Net sales:						
Service centers	\$ 34,393	69.3 %	\$ 34,971	66.9 %	\$ (578)	(1.7) %
Original equipment manufacturers	5,790	11.7	4,002	7.7	1,788	44.7
Rerollers	4,162	8.4	4,627	8.8	(465)	(10.0)
Forgers	3,901	7.9	7,080	13.5	(3,179)	(44.9)
Conversion services and other sales	1,364	2.7	1,629	3.1	(265)	(16.3)
Total net sales	\$ 49,610	100.0 %	\$ 52,309	100.0 %	\$ (2,699)	(5.2) %

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## Melt Type Information

(in thousands)	Three months ended June 30,					
	2015		2014		Dollar variance	Percentage variance
	Amount	Percentage of net sales	Amount	Percentage of net sales		
Net sales:						
Specialty alloys	\$ 44,001	88.7 %	\$ 46,424	88.8 %	\$ (2,423)	(5.2) %
Premium alloys (A)	4,245	8.6	4,256	8.1	(11)	(0.3)
Conversion services and other sales	1,364	2.7	1,629	3.1	(265)	(16.3)
Total net sales	\$ 49,610	100.0 %	\$ 52,309	100.0 %	\$ (2,699)	(5.2) %

(A) Premium alloys represent all vacuum induction melted (VIM) products.

The majority of our products are sold to service centers/processors rather than the ultimate end market customers. The end market information in this Quarterly Report is our estimate based upon our knowledge of our customers and the grade of material sold to them, which they will in-turn sell to the ultimate end market customer.

## End Market Information

(in thousands)	Three months ended June 30,					
	2015		2014		Dollar variance	Percentage variance
	Amount	Percentage of net sales	Amount	Percentage of net sales		
Net sales:						
Aerospace	\$ 30,379	61.3 %	\$ 30,190	57.7 %	\$ 189	0.6 %
Power generation	5,074	10.2	6,552	12.5	(1,478)	(22.6)
Oil & gas	4,113	8.3	5,406	10.3	(1,293)	(23.9)
Heavy equipment	4,975	10.0	3,697	7.1	1,278	34.6
General industrial, conversion services and other sales	5,069	10.2	6,464	12.4	(1,395)	(21.6)
Total net sales	\$ 49,610	100.0 %	\$ 52,309	100.0 %	\$ (2,699)	(5.2) %

Net sales:



Net sales for the three months ended June 30, 2015 decreased \$2.7 million, or 5.2%, as compared to the three months ended June 30, 2014. This decrease primarily reflects a 10.2% decrease in consolidated shipments and approximately 26% decrease in average surcharge for the three months ended June 30, 2015, compared to the same prior year period. Our sales dollars per shipped ton increased by 5.6% from the three months ended June 30, 2015 to the three months ended June 30, 2014 reflecting a shift to a higher value product mix. Our product sales to all of our end markets, except aerospace and heavy equipment, decreased, as noted in the above table. During the three months ended June 30, 2015, premium alloy sales were flat when compared to the three months ended June 30, 2014. Our premium alloy sales were 8.6% of total sales for the three months ended June 30, 2015 compared to 8.1% for the three months ended June 30, 2014. Our premium alloy sales are primarily for the aerospace end market.

Gross margin:

Our gross margin, as a percentage of sales, was 10.5% and 16.1% for the three months ended June 30, 2015 and 2014, respectively. The deterioration in our gross margin for the three months ended June 30, 2015 as compared to the three months ended June 30, 2014 is the result of misalignment of surcharges as a result of falling raw material prices in three months ended June 30, 2015 compared to a period of rising surcharges in the three months ended June 30, 2014.

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Selling, general and administrative expenses:

Our selling, general and administrative (“SG&A”) expenses consist primarily of employee costs, which include salaries, payroll taxes and benefit related costs, legal and accounting services, stock compensation and insurance costs. SG&A expenses decreased by \$200,000 in the three months ended June 30, 2015 as compared to the three months ended June 30, 2014 primarily due to a decrease in salary and healthcare expense. As a percentage of sales, our SG&A expenses increased from 9.9% during the three months ended June 30, 2014 to 10.0% for the three months ended June 30, 2015 primarily as a result of the 5.2% decrease in our net sales quarter over quarter.

Interest expense and other financing costs:

Our interest expense and other financing costs decreased from \$1.0 million for the three months ended June 30, 2014 to \$765,000 for the three months ended June 30, 2015. This decrease is primarily due to lower interest rates incurred on our debt in 2015 when compared to 2014. Our interest rates are determined by a LIBOR-based rate plus an applicable margin based upon our quarterly leverage ratio. During both the three months ended June 30, 2015 and 2014, we recognized \$160,000 of deferred financing amortization.

Income tax (benefit) provision:

For the six months ended June 30, 2015 and 2014, our estimated annual effective tax rate applied to ordinary income was 29.0% and 34.4%, respectively.

Including the effect of discrete items, our effective tax rate for the six months ended June 30, 2015 and 2014 was 31.7% and 65.7%, respectively and for the three months ended June 30, 2015 and 2014 was 32.5% and 34.1%, respectively. The effective tax rate for the three and six months ended June 30, 2014 was reflective of a net discrete tax expense of \$869,000. The \$869,000 of discrete tax expense primarily includes tax expense of \$596,000 associated with the New York state tax rate reduction to 0% for New York qualified manufacturers, and tax expense of \$247,000 associated with a Pennsylvania tax settlement related to certain expenses which had been deducted for state income tax purposes during the 2005-2007 tax years.

Net income:

Our net loss of \$(356,000), or \$(0.05) per diluted share, for the three months ended June 30, 2015, decreased from net income of \$1.4 million, or \$0.20 per diluted share, for the three months ended June 30, 2014 for the reasons stated above.

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Six months ended June 30, 2015 as compared to the six months ended June 30, 2014

(in thousands, except shipped ton information)	Six months ended June 30,					
	2015		2014		Dollar / ton variance	Percentage variance
	Amount	Percentage of net sales	Amount	Percentage of net sales		
Net sales:						
Stainless steel	\$ 81,353	77.0 %	\$ 78,672	79.5 %	\$ 2,681	3.4 %
High-strength low alloy steel	9,432	8.9	7,246	7.3	2,186	30.2
Tool steel	8,893	8.4	7,061	7.1	1,832	25.9
High-temperature alloy steel	3,469	3.3	3,015	3.0	454	15.1
Conversion services and other sales	2,446	2.4	2,982	3.1	(536)	(18.0)
Total net sales	105,593	100.0	98,976	100.0	6,617	6.7
Cost of products sold	94,697	89.7	84,506	85.4	10,191	12.1
Gross margin	10,896	10.3	14,470	14.6	(3,574)	(24.7)
Selling and administrative expenses	9,655	9.1	9,797	9.9	(142)	(1.4)
Operating income	1,241	1.2	4,673	4.7	(3,432)	(73.4)
Interest expense	(1,227)	(1.2)	(1,580)	(1.6)	353	(22.3)
Deferred financing amortization	(320)	(0.3)	(325)	(0.3)	5	(1.5)
Other (expense) income, net	(33)	-	3	-	(36)	(1200.0)
(Loss) income before income taxes	(339)	(0.3)	2,771	2.8	(3,110)	(112.2)
(Benefit) provision for income taxes	(108)	(0.1)	1,821	1.8	(1,929)	(105.9)
Net (loss) income	\$ (231)	(0.2) %	\$ 950	1.0 %	\$ (1,181)	(124.3)
Tons shipped	18,801		19,246		(445)	(2.3) %
Sales dollars per shipped ton	\$ 5,616		\$ 5,143		\$ 473	9.2 %

## Market Segment Information

(in thousands)	Six months ended June 30,				Dollar variance	Percentage variance	
	2015	2014	Amount	Percentage of net sales			
Net sales:							
Service centers	\$ 71,804	68.0 %	\$ 63,762	64.4 %	\$ 8,042	12.6	%
Forgers	7,788	7.4	13,462	13.6	(5,674)	(42.1)	
Rerollers	10,819	10.2	10,852	11.0	(33)	(0.3)	
Original equipment manufacturers	12,736	12.1	7,918	8.0	4,818	60.8	
Conversion services and other sales	2,446	2.3	2,982	3.0	(536)	(18.0)	
Total net sales	\$ 105,593	100.0 %	\$ 98,976	100.0 %	\$ 6,617	6.7	%

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## Melt Type Information

(in thousands)	Six months ended June 30,				Dollar variance	Percentage variance	
	2015	2014	Percentage of net sales	Percentage of net sales			
	Amount		Amount				
Net sales:							
Specialty alloys	\$ 93,863	88.9 %	\$ 89,040	90.0 %	\$ 4,823	5.4	%
Premium alloys (A)	9,284	8.8	6,954	7.0	2,330	33.5	
Conversion services and other sales	2,446	2.3	2,982	3.0	(536)	(18.0)	
Total net sales	\$ 105,593	100.0 %	\$ 98,976	100.0 %	\$ 6,617	6.7	%

(A) Premium alloys represent all vacuum induction melted (VIM) products.

The majority of our products are sold to service centers/processors rather than the ultimate end market customers. The end market information in this Quarterly Report is our estimate based upon our knowledge of our customers and the grade of material sold to them, which they will in-turn sell to the ultimate end market customer.

## End Market Information

(in thousands)	Six months ended June 30,				Dollar variance	Percentage variance	
	2015	2014	Percentage of net sales	Percentage of net sales			
	Amount		Amount				
Net sales:							
Aerospace	\$ 64,140	60.7 %	\$ 56,897	57.5 %	\$ 7,243	12.7	%
Power generation	12,398	11.7	11,967	12.1	431	3.6	
Oil & gas	10,214	9.7	9,655	9.8	559	5.8	
Heavy equipment	8,967	8.5	7,656	7.7	1,311	17.1	
General industrial, conversion services and other sales	9,874	9.4	12,801	12.9	(2,927)	(22.9)	
Total net sales	\$ 105,593	100.0 %	\$ 98,976	100.0 %	\$ 6,617	6.7	%

## Net sales:

Net sales for the six months ended June 30, 2015 increased \$6.6 million, or 6.7%, as compared to the six months ended June 30, 2014. Consolidated shipments for the six months ended June 30, 2015 decreased by 2.3% compared to

the six months ended June 30, 2014. Despite downward pressure on pricing resulting from lower surcharges, our sales dollars per shipped ton increased by 9.2% from the six months ended June 30, 2014 to the six months ended June 30, 2015 indicating our shift to a higher value product mix. Our product sales to all of our end markets, except general industrial, conversion services and other sales, increased as noted in the above table. During the six months ended June 30, 2015, we recognized a \$2.3 million, or 33.5%, increase in premium alloy sales when compared to the same period in 2014. Our premium alloy sales increased from 7.0% of total sales for the six months ended June 30, 2014 to 8.8% in the current period. Our premium alloy sales are primarily for the aerospace end market.

Gross margin:

Our gross margin, as a percentage of sales, was 10.3% and 14.6% for the six months ended June 30, 2015 and 2014, respectively. The decrease in our gross margin over the first half of 2015 when compared to the same prior year period is a result of higher scrap rates and a misalignment of surcharge and falling raw material costs in 2015 versus a period of rising surcharge and lagging raw material costs in 2014.

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Selling, general and administrative expenses:

Our SG&A expenses decreased by \$142,000 in the six months ended June 30, 2015 as compared to the six months ended June 30, 2014 primarily due to decreased variable incentive compensation. As a percentage of sales, our SG&A expenses decreased to 9.1% for the six months ended June 30, 2015, as compared to 9.9% during the six months ended June 30, 2014.

Interest expense and other financing costs:

Our interest expense and other financing costs decreased from \$1.9 million for the six months ended June 30, 2014 to \$1.5 million for the six months ended June 30, 2015. This decrease is primarily due to lower interest rates incurred on our debt in 2015 when compared to 2014. Our interest rates are determined by a LIBOR-based rate plus an applicable margin based upon our quarterly leverage ratio. During both the six months ended June 30, 2015 and 2014, we recognized \$320,000 of deferred financing amortization.

Income tax (benefit) provision:

For the six months ended June 30, 2015 and 2014, our estimated annual effective tax rate applied to ordinary income was 29.0% and 34.4%, respectively.

Including the effect of discrete items, our effective tax rate for the six months ended June 30, 2015 and 2014 was 31.7% and 65.7%, respectively and for the three months ended June 30, 2015 and 2014 was 32.5% and 34.1%, respectively. The effective tax rate for the three and six months ended June 30, 2014 was reflective of a net discrete tax expense of \$869,000. The \$869,000 of discrete tax expense primarily includes tax expense of \$596,000 associated with the New York state tax rate reduction to 0% for New York qualified manufacturers, and tax expense of \$247,000 associated with a Pennsylvania tax settlement related to certain expenses which had been deducted for state income tax purposes during the 2005-2007 tax years.

Net income:

Our net loss of \$(231,000), or \$(0.03) per diluted share for the six months ended June 30, 2015 decreased \$(1.2) million, or \$(0.16) per diluted share, when compared to net income of \$950,000, or \$0.13 per diluted share, for the six months ended June 30, 2014 for the reasons stated above.

Recently Issued Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued Accounting Standard Update (“ASU”) 2014-09 “Revenue from Contracts with Customers (Topic 606).” This topic converges the guidance within U.S. GAAP and International Financial Reporting Standards and supersedes Accounting Standards Codification 605, Revenue Recognition. The new standard requires companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively, and improve guidance for multiple-element arrangements. The new guidance is effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period, and early application is not permitted. We are currently evaluating the impact that this standard will have on our consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, "Simplifying the Presentation of Debt Issuance Costs." ASU 2015-03 requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. The new guidance is effective for annual reporting periods beginning after December 15, 2015, including interim reporting periods within that reporting period, and early application is permitted. We are currently evaluating the impact that this standard will have on our consolidated financial statements.

In July 2015, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update 2015-11, "Simplifying the Measurement of Inventory" ("ASU 2015-11") to simplify the guidance on the subsequent measurement of inventory, excluding inventory measured using last-in, first out or the retail inventory method. Under the new standard, inventory should be at the lower of cost and net realizable value. The new accounting guidance is effective for interim and annual periods beginning after December 15, 2016 with early adoption permitted. The Company is currently evaluating the impact of the pending adoption of ASU 2015-11 on the Company's consolidated financial statements.

#### Liquidity and Capital Resources

Historically, we have financed our operating activities through cash provided by operations and cash provided through our credit facilities. At June 30, 2015, our managed working capital, defined as net accounts receivable plus net inventory minus accounts payable, increased by \$4.9 million to \$110.0 million compared to \$105.1 million at December 31, 2014. Our net accounts receivable balances increased \$1.1 million for the quarter ended June 30, 2015 compared to the quarter ended December 31, 2014. Inventory



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levels decreased by \$2.1 million to \$99.0 million as of June 30, 2015 from \$101.1 million as of December 31, 2014 due to a reduction in melting to better align inventory with lower commercial activity. As a result of lower operating activity, our accounts payable balance decreased by \$5.8 million to \$19.2 million as of June 30, 2015 from \$25.0 million as of December 31, 2014.

Net cash (used in) provided by operating activities:

During the six months ended June 30, 2015, we used net cash from operating activities of \$127,000. The decrease in our inventory net of amortization provided \$1.0 million in cash which was offset by the decrease in our net accounts payable and an increase in our net accounts receivable which used \$5.8 million and \$1.1 million of cash, respectively. In addition, during the first quarter of 2015 the reduction in our accrued employment costs, primarily the result of the payout of our 2014 variable incentive compensation during the quarter, resulted in a use of cash of \$2.3 million. During the six months ended June 30, 2015, our net income adjusted for non-cash expenses generated approximately \$9.9 million of cash.

During the six months ended June 30, 2014, we generated net cash from operating activities of \$430,000. The net increase in our accounts payable and other accruals provided \$13.4 million in cash, which was offset by the increase in our net inventory and net accounts receivable which was \$14.5 million and \$10.5 million, respectively. In addition, during the six months ended June 30, 2014, our net income adjusted for non-cash expenses generated approximately \$12.1 million of cash.

Net cash used in investing activity:

During the six months ended June 30, 2015, we used \$5.8 million in cash for capital expenditures compared to \$3.5 million during the six months ended June 30, 2014. The primary reason for increased capital spending during the six months ended June 30, 2015 as compared to the same period in 2014 was timing associated with significant projects begun in the second half of 2014 which carried over and were completed in the first half of 2015. We believe that overall capital expenditures in 2015 will be similar to 2014 spending levels, as we anticipate capital spending to be spread evenly over the year of 2015 whereas 2014 capital spending was weighted heavily toward the second half of the year.

Net cash provided by financing activities:

During the six months ended June 30, 2015, our financing activities provided \$6.2 million in cash. Net cash provided from borrowings under our credit facility was approximately \$5.8 million; additionally, we received \$388,000 in receipts from the exercise of stock options and the issuance of stock under our Employee Stock Purchase Plan. Our borrowings increased to support a decrease in net accounts payable and an increase in net accounts receivable.

During the six months ended June 30, 2014, our financing activities provided \$2.9 million in cash. Net cash provided from borrowings under our credit facility was approximately \$2.0 million; additionally, we received \$891,000 in receipts from the exercise of stock options and the issuance of stock under our Employee Stock Purchase Plan. Our borrowings increased to support increased inventory and operating levels.

We believe that our cash flows from continuing operations as well as available borrowings under our credit facility are adequate to satisfy our working capital, capital expenditure requirements, and other contractual obligations for the foreseeable future, including at least the next 12 months.

We continuously monitor market price fluctuations of key raw materials. The market values for these raw materials continue to fluctuate based on supply and demand, market disruptions, and other factors. We maintain sales price surcharge mechanisms on certain of our products, priced at time of shipment, to mitigate the risk of raw material cost fluctuations. There can be no assurance that these sales price adjustments will completely offset our raw material costs.

The following table reflects the average market values per pound for selected months during the last 18-month period:

June	December	June	December
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	2015	2014	2014	2013
Nickel	\$ 5.80	\$ 7.22	\$ 8.42	\$ 6.31
Chrome	\$ 1.10	\$ 1.12	\$ 1.16	\$ 1.04
Molybdenum	\$ 7.30	\$ 9.53	\$ 14.75	\$ 9.73
Carbon scrap	\$ 0.12	\$ 0.16	\$ 0.18	\$ 0.19

Sources: Nickel is the daily average LME Cash Settlement Price; Chrome and Molybdenum is the final monthly average as published by Ryan's Notes; Carbon is the consumer price for #1 Industrial Bundles in the Pittsburgh, PA area as reported in American Metal Market.

We have a Credit Agreement, (as amended to date, the "Credit Agreement") with a syndication of banks which provides for a \$105.0 million senior secured revolving credit facility (the "Revolver") and a \$20.0 million senior secured term loan facility (the "Term Loan" and together with the Revolver, the "Facilities") that expires in March 2017. Under the Credit Agreement, our loan availability under the Revolver ("Borrowing Base") is calculated monthly based upon our accounts receivable and inventory balances.

We are required to pay a commitment fee of 0.25% based on the daily unused portion of the Revolver. The Revolver also provides for up to \$7.0 million of swing loans so long as the sum of the outstanding swing loans and the outstanding borrowings under the Revolver do not exceed our Borrowing Base at any given time. The Term Loan is payable in quarterly installments in the principal amount of \$750,000, which began on July 1, 2013, with the balance of the Term Loan payable in full on March 19, 2017.

Amounts outstanding under the Facilities, at our option, will bear interest at either a base rate or a LIBOR-based rate (the "LIBOR Option"), in either case calculated in accordance with the terms of the Credit Agreement. We elected to use the LIBOR Option during the six months ended June 30, 2015, which was 1.94% at June 30, 2015. Interest on the Facilities is payable monthly.

We are required to maintain a leverage ratio not exceeding a ratio decreasing from 3.50 to 1.00 for the period June 30, 2015 to September 30, 2015, 3.25 to 1.00 at December 31, 2015 and 3.00 to 1.00 from March 31, 2016 through maturity. We are required to maintain a fixed charge coverage ratio of 1.1 to 1.0 to maturity. We were in compliance with our covenants at June 30, 2015 and December 31, 2014.

In connection with the acquisition of the North Jackson facility, in August 2011, we issued \$20.0 million in convertible notes (the "Notes") to the sellers of the North Jackson facility as partial consideration of the acquisition. The Notes are subordinated obligations and rank junior to the Facilities. The Notes bear interest at a fixed rate of 4.0% per annum, payable in cash semi-annually in arrears on each June 18 and December 18, beginning on December 18, 2011. Unless earlier converted, the Notes mature and the unpaid principal balance is due on August 17, 2017. The Notes and any accrued and unpaid interest are convertible into shares of our common stock at the option of the holder at an initial conversion price of \$47.1675 per share of common stock. The conversion price associated with the Notes may be adjusted in certain circumstances. We may prepay any outstanding Notes, in whole or in part, on any date during a fiscal quarter if our share price is greater than 140% of the then current conversion price for at least 20 of the trading days in the 30 consecutive trading day period ending on the last trading day of the immediately preceding quarter.

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company has reviewed its market risk and believes there are no significant changes from that disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2014, except as provided in this Form 10-Q in "Management's Discussion and Analysis of Financial Condition and Results of Operations."

Item 4. CONTROLS AND PROCEDURES

The Company's management, including the Company's Chairman, President and Chief Executive Officer and its Vice President of Finance, Chief Financial Officer and Treasurer, performed an evaluation of the effectiveness of the Company's disclosure controls and procedures. Based on that evaluation, the Company's Chairman, President and Chief Executive Officer and its Vice President of Finance, Chief Financial Officer and Treasurer concluded that, as of the end of the fiscal period covered by this quarterly report, the Company's disclosure controls and procedures are effective. During the fiscal quarter ended June 30, 2015, there were no changes in the Company's internal control over financial reporting which have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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Part II. OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

There are no material changes from the legal proceedings disclosed in Item 3. of the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

Item 1A. RISK FACTORS

There are no material changes from the risk factors disclosed in Item 1A. of the Company's Annual Report on Form 10-K for the year ended December 31, 2014.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None.

Item 3. DEFAULTS UPON SENIOR SECURITIES

None.

Item 4. MINE SAFETY DISCLOSURES

Not Applicable.

Item 5. OTHER INFORMATION

None.

Item 6. EXHIBITS

Exhibit

Number Exhibit

- 10.1 Employment Agreement dated August 4, 2015 between the Company and Larry J. Pollock (filed herewith)
- 10.2 Employment Agreement dated August 5, 2015 between the Company and Graham McIntosh (filed herewith)
- 10.3 Employment Agreement dated August 5, 2015 between the Company and Ross C. Wilkin (filed herewith)

- 31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 32.1 Certification of Chief Executive Officer and Chief Financial Officer pursuant to Rule 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).
- 101 The following financial information from this Quarterly Report on Form 10-Q for the fiscal quarter ended June 30, 2015, formatted in XBRL (Extensible Business Reporting Language) and filed electronically herewith: (i) the Consolidated Balance Sheets; (ii) the Consolidated Statements of Operations; (iii) the Consolidated Statements of Cash Flows; and (iv) the Notes to the Consolidated Financial Statements (filed herewith).

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SIGNATURES

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

Date: August 7, 2015

/s/ Dennis M. Oates  
Dennis M. Oates  
Chairman, President and Chief Executive Officer  
(Principal Executive Officer)

/s/ Ross C. Wilkin  
Ross C. Wilkin  
Vice President of Finance,  
Chief Financial Officer and Treasurer  
(Principal Financial and Accounting Officer)