IMCO RECYCLING INC
Form 10-K
March 15, 2004
Table of Contents

Index to Financial Statements

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 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, 2003

¨ Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File No. 1-7170

IMCO Recycling Inc.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

75-2008280

(I.R.S. Employer Identification No.)

5215 North O Connor Blvd., Suite 1500

Central Tower at Williams Square

Irving, Texas 75039

(Address of principal executive offices) (Zip code)

(972) 401-7200

(Registrant s telephone number, including area code)

SECURITIES REGISTERED PURSUANT TO SECTION 12(b) OF THE ACT:

Title of Each Class	Name of Exchange on Which Registered
Common Stock, $0.10 Par Value	**New York Stock Exchange**

SECURITIES REGISTERED PURSUANT TO SECTION 12(g) OF THE ACT: None

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of regulation S-K 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 an accelerated filer (as defined in Rule 12b-2 of the Act). Yes x No ¨

As of June 30, 2003, the aggregate market value of the registrant s outstanding common stock held by non-affiliates of the registrant was $82,822,413, based on the closing market price of $6.64 per share on June 30, 2003.

Indicate the number of shares outstanding of each of the registrant s classes of common stock, as of March 1, 2004.

Common Stock, $0.10 par value: 15,610,615 shares

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant s definitive proxy statement relating to its 2004 Annual Meeting of Stockholders are incorporated by reference into Part III hereof.

Table of Contents

Index to Financial Statements

Table of Contents

Index to Financial Statements

PART I

Introductory Note: This Annual Report on Form 10-K contains forward-looking statements as defined by the Private Securities Litigation Reform Act of 1995. Forward-looking statements should be read in conjunction with the cautionary statements and other important factors included in this Form 10-K. See ITEM 7 - MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - RISK FACTORS, for a description of important factors which could cause actual results to differ materially from those contained in the forward-looking statements. Forward-looking statements include statements about plans, objectives, goals, strategies, future events or performance, and assumptions underlying those statements. These forward-looking statements may be identified by words such as anticipates, estimates, expects, intends, plans, predicts, projects, and similar expressions. Our expectations, beliefs and p are expressed in good faith and we believe we have a reasonable basis to make these statements, through our management s examination of historical operating trends, data contained in our records and other data available from third parties, but there can be no assurance that our management s expectations, beliefs or projections will result or be achieved.

The financial statements contained in this Form 10-K include the accounts of IMCO Recycling Inc. and all of its majority owned subsidiaries (which collectively, except where context otherwise requires, are referred to herein as we, us, or our). The term VAW-IMCO refers to our German subsidiary, VAW-IMCO Guss und Recycling GmbH. In March 2003, we reached an agreement to acquire effective full ownership of VAW-IMCO. This resulted in the consolidation of the financial condition and results of operations of VAW-IMCO with ours effective March 1, 2003. In this Form 10-K, when we refer to production data calculated on a pro forma basis, we are giving pro forma effect to this consolidation as if it had occurred on January 1, 2003, and are including VAW-IMCO s production with ours for all of fiscal 2003.

Information in this Form 10-K concerning processing volumes, production capacity, rankings and other industry and market information, including our general expectations concerning the aluminum and zinc recycling industries, are based on estimates prepared by us based on certain assumptions and our knowledge of these industries as well as data from third party sources. These data include, but are not limited to, data from The Aluminum Association and U.S. Geological Surveys. The sources of this information generally state that the information contained therein is believed to be reliable, but there can be no assurance as to the accuracy or completeness of included information. We have not independently verified any of the data from third party sources, nor have we ascertained the underlying economic assumptions relied upon therein.

Table of Contents

Index to Financial Statements

ITEM 1. BUSINESS

COMPANY OVERVIEW

We are the largest recycler of aluminum and zinc in the United States and believe we are the largest aluminum recycler in the world, with total processing capacity of approximately 4.1 billion pounds as of December 31, 2003. Our manufacturing and distribution network consists of 26 production plants; 21 are located in the United States, two in Germany, and one each in Brazil, Mexico and Wales. Our aluminum production network includes a domestic recycling division, a domestic specialty alloys division and an international division that represent 48%, 21% and 23%, respectively, of our overall capacity. Our zinc division, which represents 8% of our overall capacity, includes facilities dedicated to the production of zinc oxide, zinc dust and zinc metal.

For the year ended December 31, 2003, we processed 3.0 billion pounds of aluminum and zinc and we generated revenues of $892,015,000 and EBITDA of $53,375,000. Pro forma, including VAW-IMCO for all of 2003, we processed 3.1 billion pounds of aluminum and zinc and generated revenues of $944,186,000 for the year ended December 31, 2003.

Aluminum materials we process include:

- new scrap generated from manufacturing processes, including turnings from production of auto wheels, engine blocks and heads, and manufacturing scrap from production of can stock, extrusions and building products;
- old scrap such as used beverage cans (UBCs), vehicle and building components and other types of industrial and consumer scrap; and
- dross (a by-product of the melting process that is used in rolling mill cast houses, foundries and primary aluminum smelters).

We convert scrap and dross into molten metal in furnaces at our facilities and deliver the recycled aluminum to our customers in molten or ingot form. We provide these services under either tolling arrangements or through product sales.

Most of our domestic aluminum recycling division s processing capacity is utilized for tolling arrangements, by which we recycle customer-owned scrap and dross and return the recycled metal to our customers in molten or ingot form, for a fee. For the year ended December 31, 2003, approximately 55% of our total pounds processed across all divisions involved tolling.

Most of our domestic specialty alloys division s processing capacity is utilized for product sales, by which we process and melt scrap that is purchased from customers and on the open market. Our specialty alloys division is also included within our domestic aluminum segment. To produce specialty alloys, we combine molten aluminum and certain other metals that provide specific desirable qualities such as increased strength, formability and wear resistance. We then sell the specialty alloys to customers in molten or ingot form.

Table of Contents

Index to Financial Statements

Our international division includes both aluminum recycling and specialty alloys operations. Our facilities in Brazil, Mexico and Wales are dedicated to aluminum recycling. Our German facilities have capacity to serve both aluminum recycling and specialty alloys markets.

Our aluminum customers include some of the world s major aluminum producers and aluminum fabricators, diecasters, extruders, automotive companies and other processors. Most of the aluminum metal processed by us is used to produce products for the transportation, packaging and construction industries. Due to the increasing use of aluminum in automotive components, much of our recent growth has been directed toward serving the transportation sector. Our principal aluminum customers include General Motors Corporation (GM), The BMW Group (BMW), DaimlerChrysler Corporation, Alcoa Inc. (Alcoa), Contech (a unit of SPX Corporation), Ford Motor Company, Hydro Aluminium Deutschland GmbH (Hydro), Arco Aluminum, and Commonwealth Aluminum Corporation (Commonwealth).

Our zinc division operates seven U.S. production facilities that use furnaces to convert primary zinc, zinc scrap and dross into various value-added zinc products, such as:

- zinc oxide, which is used in the vulcanizing process for tires and rubber products;
- zinc dust, which is an essential ingredient in corrosion-resistant industrial paints, coatings and specialty chemicals; and
- zinc metal, which is sold to galvanizers for corrosion protection of steel.

Our zinc customers include some of the world s major tire and rubber producers and galvanizers, steel companies and other processors, including Michelin Tire, Bridgestone Firestone, Cooper Tire, and Dow AgroSciences LLC.

INTERNET ADDRESS AND SEC FILINGS

Our Internet website address is http://www.imcorecycling.com. We make available on our Internet website for no charge our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports, as soon as reasonably practicable after the materials are electronically filed with or furnished to the Securities and Exchange Commission (SEC). The SEC also maintains a website at www.sec.gov that contains reports, proxy statements and other information regarding SEC registrants, including our company.

ALUMINUM RECYCLING

Aluminum has several characteristics that make it a highly valuable commodity. Compared to several substitute metals, it is light-weight, has a high strength-to-weight ratio and residual value and is resistant to corrosion.

Aluminum s greatest advantage is its sustained recyclability; it can be processed again and again without any material decline in performance or quality. About two-thirds of all aluminum ever produced 440 million tons of a total of 680 million tons manufactured since 1886 is still in use. Recycling of aluminum provides energy savings of 95% compared to the production of the primary metal, and it lowers capital equipment costs by about 90%. In addition, solid wastes associated with the primary production process (like bauxite residue and spent potlinings) are avoided. Because of these two benefits, U.S. production of recycled aluminum has increased substantially over the past two decades, and similar increases have occurred in the world s major industrial regions.

World growth in aluminum use has exceeded that of competing metals. Since 1950, aluminum use has increased by a factor of 18 while uses of copper and steel have risen by factors of 13 and 3, respectively. Aluminum is the world s second most widely used metal.

Table of Contents

Index to Financial Statements

Over the last two decades, annual U.S. aluminum supply (which includes primary, recycled and imported aluminum) increased 65%, from 5,762 thousand metric tonnes in 1982 to 9,500 thousand metric tonnes in 2002. During this same period, the economic and environmental advantages of recycled aluminum have caused annual production of recycled aluminum to increase by 75%, from 1,666 thousand metric tonnes to 2,920 thousand metric tonnes. U.S. primary aluminum production has declined significantly over the past two decades because of increases in energy, environmental and labor costs. As a result of this decline, primary aluminum s role in total U.S. aluminum supply has decreased while those of recycled aluminum and imports have expanded. In 2002, the primary industry accounted for 29% of total domestic aluminum supply while recycled metal provided 30% and imports provided 41% of aluminum supply.

Transportation, containers & packaging and building & construction are the three largest end-use markets for aluminum. In 2002, these industries accounted for about 68% of total industry shipments. Because of greater use of aluminum in vehicles, shipments to the transportation sector have risen in recent years, and it is now the largest and fastest-growing aluminum market in the United States. In 2002, the last year for which statistics are available, transportation consumed about 32% of total shipments while containers & packaging, mainly the production of beverage cans, utilized some 21% of annual shipments and building & construction accounted for 15%. Exports, consumer durables, electrical, machinery & equipment are other important markets for aluminum.

COMPETITIVE FACTORS

Market positions. We are the largest recycler of aluminum and zinc in the United States and believe we are the largest aluminum recycler in the world. We are also one of the world s largest zinc recyclers. The global aluminum recycling market is highly fragmented and characterized by smaller, regional operators. The zinc recycling market in the U.S. is concentrated among a small number of competitors. We attribute our market strength to our ability to meet our customers needs for high rates of metal recovery and timely delivery of products that satisfy required technical specifications in an environmentally responsible manner.

Long-term contractual arrangements with our customers. We have long-term contractual arrangements for our aluminum recycling services with a number of our largest customers at many of our plant locations. These customers include Commonwealth, GM, Alcoa, Alcan Inc., Aluminium Norf GmbH, Tomra Latasa, and NEMAK, S.A. For the year ended December 31, 2003 on a pro forma basis, we processed 880 million pounds of aluminum pursuant to long-term contractual arrangements, which represented approximately 28% of our total processing volume. We plan to seek similar dedicated long-term arrangements in the future.

Plant locations. Our competitive position is strengthened by the location of many of our facilities near our major customers plants. These locations are strategically important because the industry traditionally has been regionally constrained due to freight costs that limit the distance to which recycled materials can be shipped economically. The close proximity of many of our plants to customers facilities allows us to specialize in just-in-time delivery of recycled aluminum in molten form by customized trucks. This delivery method lowers our customers energy and capital expenses as well as metal melt loss, thus increasing their productivity. As of December 31, 2003, about 85% of our annual aluminum recycling capacity could be delivered in molten form. In addition, in conjunction with our enterprise resource information technology system, our production network enables us to reallocate processing work among our various facilities, thereby maximizing capacity utilization and balancing demand.

Table of Contents

Index to Financial Statements

Customer relationships and customer service. We are dedicated to developing new methods and processes to better serve our customers. We believe we create substantial value for our customers through:

- our operational and design technologies that produce higher metal quality and recovery yields;
- the close proximity of many of our facilities to our customers, providing greater convenience and accessibility and enabling us to integrate into our customers supply chains;
- our ability to deliver recycled aluminum in molten form for just-in-time delivery, thereby saving customers the expense of re-melting aluminum ingots; and
- our environmental technologies and practices, including our dedicated disposal facilities and a process we developed to recover aluminum from by-products of the recycling process.

We also conduct tests with our customers to improve recycling processes and enhance metal recovery, quality and chemistry. We believe these factors allow us to maintain and develop strong relationships and loyalty with our customers.

Reduced commodity risk and working capital. For the year ended December 31, 2003, on a pro forma basis, tolling arrangements accounted for approximately 55% of our total pounds processed across all divisions. Tolling requires minimal working capital commitments and does not expose us to aluminum price fluctuations. In addition, when purchasing scrap on the open market for our aluminum and zinc operations, management attempts to reduce price risk by aligning metal purchases with metal sales, hedging open metal positions to protect margins and minimizing inventory levels consistent with the need to allow for continuous operation of production facilities.

Technology. Our plants use advanced metal preparation equipment and furnace recycling technologies. We have developed instrumentation and statistical process control calibration programs at many of our facilities to assure reliable chemical analysis of our customers metal. A number of our plants have earned ISO (International Organization for Standardization) certifications that their production, management and environmental systems satisfy guidelines that enable us to consistently deliver products meeting customer specifications. We have added more efficient fuel-burning technologies to our melting furnaces within the past three years, resulting in lower natural gas usage and more efficient operating processes. In addition, we have installed new or additional pollution control equipment at some of our facilities and have implemented procedures throughout our production network that we believe will help assure that materials are handled in an environmentally responsible manner. The improvements in our metal preparation techniques and increased automation at our plants have been key drivers of our cost reduction programs in recent years.

Management team. Our senior executive officers and our key employees have on average more than 21 years experience in the aluminum or zinc industries.

Table of Contents

Index to Financial Statements

OUR BUSINESS STRATEGY

Increase capacity utilization at our aluminum and zinc recycling plants. We emphasize maximizing capacity utilization rates at our plants as a means of increasing profitability. We manage our capacity utilization by seeking long-term contractual arrangements with many of our largest customers and aggressively pursuing additional recycling opportunities. In addition, our production network enables us to reallocate processing work among our various facilities, thereby maximizing utilization and balancing demand. Furthermore, when market conditions warrant, we are able to temporarily suspend operations at certain of our plants to reduce costs and maintain higher levels of capacity utilization at our other plants.

Continue to pursue a disciplined growth strategy. We have a successful track record of growing our aluminum business by constructing new facilities or acquiring existing facilities in conjunction with long-term contractual arrangements with customers. These contractual arrangements typically provide for a predetermined minimum processing volume at a new facility and reduce the risk of bringing on new processing capacity. In recent years, we have executed this growth strategy through our pursuit of the following opportunities:

During 2002, we constructed a new production facility in Monterrey, Mexico, with a long-term contract to recycle aluminum alloy dross and manufacturing scrap for a large manufacturer of cylinder heads and engine blocks.

During 2002, we acquired an aluminum recycling plant in Pindamonhangaba, Brazil and signed long-term contracts to supply the country s only can sheet rolling mill and recycle used beverage cans and production scrap for a facility owned by South America s largest manufacturer of aluminum cans.

In 2000, we completed construction of our Saginaw, Michigan facility in order to supply GM with almost two billion pounds of specialty alloys over the course of a 13-year supply contract.

We intend to seek out additional opportunities to expand our aluminum business through acquisitions of existing facilities, construction of new facilities and expansion of existing facilities. However, the terms of our debt facilities currently impose certain restrictions on our ability to fund our growth. See ITEM 7 - MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS - CREDIT FACILITIES AND REFINANCING.

Leverage existing customer relationships to drive international expansion. Over the past decade, our long-term relationships with certain major U.S. customers have allowed us to increase our processing capacity. With demand for aluminum recycling services and products growing in many regions throughout the world, we intend to continue to leverage these existing relationships by serving the foreign operations of these same customers. The consolidation of VAW-IMCO in March 2003 is an important step in the ongoing expansion of our international operations, because its two aluminum recycling and specialty alloys facilities provide a platform for further growth in Europe. We plan to continue seeking foreign locations for our processing facilities where market conditions warrant.

Capitalize on increasing use of aluminum in the transportation market. The transportation sector has become the largest and fastest-growing market for aluminum in recent years because of significantly greater use of the metal in all types of vehicles. The average amount of aluminum per vehicle has increased from 183 pounds in 1992 to 274 pounds in 2003, and is expected to reach at least 350 pounds by 2010. We intend to capitalize on this growth by providing aluminum recycling services and specification alloy products to automotive vehicle manufacturers and their component producers.

8

Table of Contents

Index to Financial Statements

Increase productivity and reduce costs. We are focused on increasing productivity and lowering operating costs at our plants as a means of improving our profitability. Over the past several years, we have emphasized raising overall productivity through the implementation of more technically advanced processes and equipment. During 2002, we conducted a furnace operation benchmarking program that included all of our U.S. facilities as well as those in Europe and Brazil in order to identify the best practices at each plant and test the performance of each newly modified furnace system to verify that the capital expenditures involved accomplished their objectives. We have also implemented enterprise resource planning software, which allows us to align our information technology system with our business strategy. Through this centralized system, we are better able to manage several aspects of our business, including the purchasing and selling of metals, the deployment of our working capital and risk management techniques related to commodity exposure.

Continue to minimize commodity price risks. We use a variety of hedging methods to mitigate uncertainty and volatility and to cover underlying exposures to minimize the risks associated with aluminum, zinc and natural gas prices. Our policies prohibit us from engaging in speculative derivatives transactions. As part of the risk management program, we have recently centralized our aluminum metal management function to effectively align our metal purchasing, selling, hedging and inventory functions.

Maintain environmental efficiencies. We continue our emphasis on environmental compliance, which promotes good relationships with our customers and our plant communities. Our customers benefit from the enhanced environmental facilities we employ, such as the lined landfill at our Morgantown, Kentucky facility, which is built to hazardous waste standards. We also seek to provide efficiencies at our plants through our environmental compliance efforts. For example, we continue our efforts to develop a closed loop production system in which virtually all materials used in the recycling process are reclaimed or consumed, thus reducing the need for and expense of landfilling. Our Kentucky salt cake processing plant and our patented wet-milling process employed to recycle salt cake at our Arizona facility are our initial steps in the development of these types of systems.

INCREASE IN PROCESSING CAPACITY

Since our formation in 1988, we have increased our number of facilities and capacity through acquisitions, construction of new facilities and expansion of existing facilities. Implementation of this growth strategy was accelerated during the mid-1990s.

Table of Contents

Index to Financial Statements

The following table shows our growth since 1993:

Date	Total number of US facilities owned and operated	Total number of foreign facilities owned and operated	Total annual melting capacity aluminum	Total annual melting capacity zinc and other metals
January 1993	5	- 0 -	735 million pounds	50 million pounds
December 2003	21	5*	3.8 billion pounds	300 million pounds

* Facilities in Swansea, Wales, Monterrey, Mexico, Pindamonhangaba, Brazil, and two VAW-IMCO facilities in Germany.

During 2003 and 2002, we expanded our international operations:

In 1995, we formed our VAW-IMCO joint venture with a predecessor of Hydro and acquired a 50% equity interest in VAW-IMCO. During 2002, we exercised an option to cause the joint venture to redeem the shares then owned by Hydro, and in November 2003 VAW-IMCO completed its redemption of the shares owned by Hydro. VAW-IMCO owns and operates two aluminum foundry alloy facilities in Grevenbroich and Töging, Germany, that, after expansions in 2003, together have a total annual processing capacity in excess of 700 million pounds. These facilities principally serve the European automotive markets. We plan further capacity expansion at our facilities in Germany.

In October 2002, we completed construction and began operations at our new production facility in Monterrey, Mexico. This facility recycles aluminum scrap and dross under a long-term contract with a major producer of auto engine components. In December 2003, we acquired the remaining minority interest in this facility.

In May 2002, we acquired our Brazil facility.

We are regularly in the process of evaluating the acquisition of assets or operations that complement our existing businesses. We cannot estimate what impact, if any, any such acquisition may have on our businesses.

PRODUCTS AND SERVICES

Aluminum. We recycle aluminum scrap and dross and deliver the recycled metal to customers as molten aluminum or ingots. Our aluminum customers include some of the world s primary aluminum producers and aluminum fabricators, diecasters, extruders, automotive companies and other processors. We also manufacture specification aluminum alloy products at five dedicated U.S. facilities for automotive equipment manufacturers and their suppliers. In addition, two of our aluminum recycling plants manufacture a variety of aluminum products that are ultimately used as metallurgical additions in the steel making process, such as slag conditioners, deoxidizers, steel desulfurizers and hot topping compounds. The major force behind increased demand for recycled aluminum in recent years has been aluminum s increased use in auto and truck components, including body structures.

Zinc. Zinc is used in diecastings, in brass-making as an alloying metal with copper and in chemical compounds to produce rubber, ceramics, paints and fertilizer. Its most unique quality is its natural ability to metallurgically bond with iron and steel and protect these metals from corrosion. We manufacture three value-added zinc products:

Zinc oxide is used predominantly in the tire and rubber industries and by the specialty chemical, motor oil and ceramics industries;

Table of Contents

Index to Financial Statements

Zinc dust is used in paints, specialty chemical and mining applications; and

Zinc metal is used to galvanize steel.

SALES AND LONG-TERM CONTRACTUAL ARRANGEMENTS

Aluminum. Our principal aluminum customers use recycled aluminum to produce can sheet, building, automotive and other aluminum products. No customer accounted for more than 10% of revenues in 2003. GM accounted for approximately 11% of our consolidated revenues during fiscal 2002.

Customarily, agreements with customers in the aluminum recycling industry have been short-term. These usually result from a bidding process where aluminum producers and metal traders offer to sell materials or to have materials tolled. Consequently, we historically have maintained no significant backlog of orders.

Long-term aluminum contractual arrangements. We have long-term contractual arrangements for our aluminum recycling services with a number of our largest customers at many of our plant locations. The remaining terms of these arrangements as of December 31, 2003 ranged from one year to nine years, although many of them provide for extensions. Amounts processed under long-term contractual arrangements represented approximately 35% of our total aluminum volume for 2002, and 28% for the year ended December 31, 2003 on a pro forma basis. The majority of our pounds processed under long-term contractual arrangements are subject to price escalators directly related to production costs such as labor, natural gas and supplies. In addition, many of these contractual arrangements contain provisions obligating us to indemnify the customer for certain environmental liabilities that it may incur.

We plan to seek similar dedicated long-term arrangements with customers in the future. Increased emphasis on dedicated facilities and dedicated arrangements with customers carries the inherent risk of increased dependence on a single or few customers with respect to a particular facility of ours. In such cases, the loss of such a customer, or the reduction of that customer s business with one or more of our facilities, could have a material adverse effect on our financial condition and results of operations, and any timely replacement of volumes could prove difficult.

Zinc. Most of our zinc products are sold directly to end-users. No single zinc customer accounted for more than 10% of our consolidated revenues in 2003. Most of our agreements with zinc customers are for a term of one year or less. We historically have maintained no significant backlog of orders for zinc products.

THE RECYCLING/MANUFACTURING PROCESS

Aluminum. We use two types of furnace technology: rotary and reverberatory. Rotary (or barrel-like) furnaces are able to pour a batch of melted aluminum recovered from scrap and immediately switch to

11

Table of Contents

Index to Financial Statements

other types of material and then switch back again. Reverberatory furnaces are stationary and use both radiation and convection heating to melt the material being processed. Each of these furnace technologies has advantages over the other, depending on the type of material processed.

The recovered metal is poured directly into an ingot mold or hot metal crucible for delivery to customers. Many of our plants deliver molten aluminum in crucibles directly to their customers manufacturing facilities. As of December 31, 2003, we had the capacity to provide approximately 85% of our processed aluminum in molten form. The molten aluminum is poured from the crucible into the customer s furnace, saving the customer the time and expense of re-melting aluminum ingots. We normally charge an additional fee for transportation and handling of molten aluminum.

Alloying. At our metal alloying facilities in Coldwater and Saginaw, Michigan and Shelbyville, Tennessee, additional materials are blended with molten aluminum to produce a metal alloy. The alloyed aluminum is shipped in either molten or ingot form to our customers. These alloying facilities generate dross, which is then recycled at one of our other aluminum recycling facilities.

By-products. A by-product of processing aluminum materials in reverbatory furnaces is aluminum dross, which is sent to our rotary furnaces for processing. The recycling process from our rotary furnaces produces a by-product called salt cake, which is formed from the coatings and other miscellaneous materials on aluminum scrap and dross, and the salts added during the aluminum recycling process. Salt cake is composed of salts, metallic aluminum, aluminum oxide and small amounts of other materials.

We dispose of our salt cake and certain airborne contaminants (or baghouse dust) in landfills that we use exclusively or that are permitted specifically to handle the types of waste materials we generate. Salt cake is not listed as a hazardous waste under the Resource Conservation and Recovery Act of 1976 (RCRA) or as a hazardous substance under the Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA). We own and operate a lined landfill at our Morgantown, Kentucky facility. Its design exceeds current requirements for salt cake disposal and meets RCRA Subchapter C hazardous waste standards.

We also own and operate a facility adjacent to our Morgantown, Kentucky plant to further process salt cake through the use of a materials separation process, which involves crushing the salt cake and separating aluminum out of the salt cake. The residual non-metallic product is then landfilled in our Morgantown, Kentucky landfill.

Certain of our other facilities also process salt cake and other by-products from the aluminum recycling process into aluminum concentrates, aluminum oxide and salt brine.

Zinc. Zinc oxide is produced by melting top dross, a low iron-content zinc by-product of continuous galvanizing, and re-melt die cast, a high zinc-content alloy, in a sweat or pre-melt furnace. Zinc dust with extra low lead content is preferred by the domestic industrial paint industry. It is produced by converting primary zinc into a molten form using an electro-thermal furnace. Regular zinc dust is produced by processing bottom dross, an iron-bearing zinc residue created during the galvanizing process, and re-melt die cast in a pot or ladle. Zinc metal is produced by placing pieces of oxidized zinc-bearing metals into a ball mill where we separate out the oxidic zinc. The zinc oxide is then sold as fertilizer additives. After the ball mill process, the metallic zinc-bearing material is melted, refined, poured into molds and shipped to galvanizers.

The recycling process at our Coldwater, Michigan zinc plant involves melting continuous galvanizers top dross in an electric induction furnace which is then transferred to a reactor which removes the impurities

Table of Contents

Index to Financial Statements

(iron and zinc oxide, which are sold as by-products). The remaining molten zinc is poured into a reverberatory holding furnace from which it is blended and cast into ingots, which are either sold or returned to the customer.

OPERATIONS

Aluminum. In our aluminum tolling operations, we accept scrap owned by our customers and process this material for a tolling charge per pound of incoming weight. In order to retain control of their metal supplies, customers have often desired to toll, rather than sell, their scrap materials. Tolling requires no metal inventory to be purchased or held by us. In addition, tolling does not expose us to fluctuating metal prices because we do not own the material processed. For the year ended December 31, 2003, on a pro forma basis, approximately 55% of our total pounds of aluminum processed involved tolling. Compared to product sales transactions, tolling decreases our exposure to the risk of fluctuating metal prices and working capital requirements.

We also enter into metal brokerage transactions under which we buy metal from primary and other producers and then sell the metal to end-users. These transactions involve buying and selling metal without processing it. Additionally, in order to facilitate acquiring metal for our production process, we occasionally enter into swap transactions whereby we agree to exchange our recycled finished goods for scrap raw materials.

When purchasing metals in the open market for our product sales business, we attempt to reduce the risk of fluctuating metal prices by hedging anticipated sales of aluminum and zinc and by avoiding large inventories, except to the extent judged necessary to allow our plants to operate without interruption.

Throughout 2002 and for most of 2003, we provisionally suspended operations at our Wendover, Utah aluminum facility due to adverse market conditions. During the fourth quarter of 2003, we permanently closed this plant. In August 2003, we provisionally suspended operations at our Rockwood, Tennessee plant due to reduced demand for aluminum recycling services there. We intend to keep the Rockwood plant idle until market conditions improve.

Zinc. Our zinc operations primarily consist of product sales business. Product sales from our zinc operations represent approximately 97% of our total zinc production; the remainder is from tolling transactions.

Through programs conducted by the International Organization for Standardization (ISO), many of our company s facilities have earned certifications that their production management and environmental systems meet guidelines that assure delivery of consistent and reliable products.

Table of Contents

Index to Financial Statements

Recognized Safety Performance. The leadership provided by the safety committees at our Coldwater, Michigan and Sapulpa, Oklahoma aluminum recycling facilities has earned major safety awards for their plants.

The Coldwater facility became the first industrial plant in Michigan to receive the state s Safety and Health Achievement Recognition Program (SHARP) award. The state established this program to recognize employers who have achieved especially notable safety and health excellence.

After two years in which its total case incident rate was well below the Bureau of Labor Statistics national average for facilities of this type, our Sapulpa plant achieved SHARP status with the Occupational Safety and Health Administration (OSHA). The receipt of SHARP status means that OSHA has recognized that the Sapulpa facility anticipates safety problems and has put procedures into place to ensure that hazards are identified and corrected quickly and effectively. Plants with SHARP status are exempt from programmed OSHA inspections for each year the certificate is maintained.

COMPETITION

General. The domestic aluminum and zinc recycling industries are highly competitive. We believe that our position as the largest U.S. recycler of aluminum and zinc is a positive competitive factor.

The international recycling business is highly fragmented and very competitive. However, we believe we will be able to compete effectively in certain international areas because of our processing technology. We intend to expand internationally in connection with long-term processing arrangements from our customers. The expansions into Brazil and Mexico are examples of this strategy.

We also compete both with other secondary recyclers and our customers when purchasing and processing scrap for our product sales business.

Aluminum. The principal factors of competition in our aluminum segments are price, metal recovery rates, proximity to customers, molten metal delivery capability, environmental and safety regulatory compliance and types of services (for example, the ability to deliver molten aluminum). Freight costs also limit the geographic areas in which we can compete effectively. Our largest domestic aluminum competitor is Wabash Alloys, a secondary aluminum processor, followed by several smaller competitors.

Zinc. The principal factors of competition in the zinc segment are price, customer service and high product quality. Competition is regionally focused due to high freight costs. The zinc recycling market in the U.S. is concentrated among a small number of competitors.

Table of Contents

Index to Financial Statements

For zinc oxide, our major competitors are Zinc Corporation of America, a subsidiary of Horsehead Industries, Inc., and Zochem, a subsidiary of Hudson Bay Mining & Smelting, Ltd. For zinc dust, our major competitors are Purity Zinc Metals Company, Ltd. and Meadowbrook Company, a subsidiary of T.L. Diamond Company, Inc. For zinc metal, we consider both primary and secondary zinc producers to be competitors.

OUTSOURCING OF RECYCLING BY PRIMARY ALUMINUM PRODUCERS

The amount of our aluminum tolling business can vary depending upon the extent that the primary aluminum producers internally process their own scrap. The primary aluminum producers, some of which are our largest customers, have generally elected in recent years to outsource the processing of their scrap and dross under tolling arrangements and focus their resources on other aspects of aluminum production. However, these producers are capable of processing their own scrap and vary the amount of their internal recycling depending upon furnace availability, inventory levels, the price of aluminum, their own internal demand for metal and other factors. In particular, the primary producers have historically decreased their outsourcing in times of lower overall demand for aluminum. In addition, in some instances some of these producers have expanded their aluminum recycling capacity. Decreased outsourcing or increases in internal recycling by primary producers could reduce demand for our recycling services and have a material adverse effect on our financial condition and results of operations. For instance, we have recently experienced decreased utilization rates at some of our operations and have provisionally suspended some of our operations due to an increase in internal recycling capacity by a primary producer of aluminum.

SOURCE AND AVAILABILITY OF RAW MATERIALS AND ENERGY

Metallics. Metallics (aluminum and zinc scrap and dross) represent the largest component of our cost of sales. The availability and price of scrap and dross depend on a number of factors outside our control, including general economic conditions, foreign demand for metallics and internal recycling activities by primary aluminum producers. Increased domestic and worldwide demand for aluminum and zinc scrap have had and will continue to have the effect of increasing the prices that we pay for these raw materials, thereby increasing our cost of sales.

The primary sources of aluminum scrap and dross for our recycling and alloying activities include automotive component manufacturers, can stock producers, used beverage cans and aluminum smelters. Many of our aluminum suppliers are also our customers. We also buy aluminum scrap from metal scrap traders on the open market.

A significant portion of our zinc products is produced from zinc dross and other secondary materials provided by the galvanizing and scrap metals industries. These industries have operated at lower levels during the past three years, reducing the availability of profitable processing opportunities. We also purchase primary zinc to produce high-grade zinc and for metals brokerage purposes.

We purchase our zinc raw materials from numerous suppliers. Many hot dip galvanizers, which supply us with zinc raw materials, are also our customers.

Our zinc brokerage unit also procures raw materials for use in our zinc manufacturing operations. The availability of zinc dross is dependent upon the demand for galvanized steel, which has historically paralleled fluctuations in customer demand in the automotive, appliance and construction industries.

15

Table of Contents

Index to Financial Statements

Energy. Our operations are fueled by natural gas, which represents the third largest component of our cost of sales, after metal and labor costs. We purchase the majority of our natural gas on a spot-market basis. However, in an effort to acquire the most favorable natural gas costs, we have secured some of our natural gas at fixed price commitments. Most of our pounds processed under long-term contractual arrangements with our customers are subject to price escalators directly related to natural gas costs. While we have the ability to pass on to customers some of our increases in natural gas costs based on our long-term arrangements with them, and while we have hedged some of our natural gas costs, in many instances we are not able to mitigate the effect of higher natural gas costs on our cost of sales. We believe that we will continue to have access to adequate energy supplies to meet our needs for the foreseeable future.

SEASONALITY

Aluminum. Our used beverage can collections have historically been highest in the summer months and lowest in the winter months. Our automotive industry customers have typically experienced a decline in molten metal deliveries during periods when their production facilities cease production to perform new model changeovers and during the holidays in December. Our European operations also experience some slowdowns in the month of August, which is a peak holiday time in Europe.

Zinc. Historically, demand for our zinc products used by paint manufacturers and those used in fertilizers has been somewhat higher in the summer months.

Table of Contents

Index to Financial Statements

TRANSPORTATION

We receive incoming metal by rail and truck. Most of our plants own their own rail siding or have access to rail lines nearby. We own and lease various trucks and trailers to support our business. Customarily, the transportation costs of scrap materials to be tolled are paid by our customers, while the transportation costs of metal we purchase and sell may be paid by either our customers or us. We contract with third-party transportation firms for hauling some of our solid waste for disposal.

INTERNATIONAL OPERATIONS

VAW-IMCO. VAW-IMCO, our German subsidiary, supplies specialty alloys to the European automobile industry and serves other European aluminum markets. VAW-IMCO owns and operates two aluminum recycling foundry alloy facilities in Grevenbroich and Töging, Germany, that together have an annual processing capacity in excess of 700 million pounds. Approximately 57% of VAW-IMCO s annual processing volume involves aluminum product sales; the remainder is represented by aluminum tolling. VAW-IMCO has long-standing relationships with several of its customers, including BMW, Ford, Hydro and Daimler Chrysler. VAW-IMCO competes with certain of its customers that have in-house recycling capacity.

Other. We own a facility in Swansea, Wales, which supplies aluminum to a variety of customers. This facility has an annual processing capacity of approximately 100 million pounds of aluminum.

We own a facility in Pindamonhangaba, Brazil, which supplies Brazil s only can sheet rolling mill and recycles used beverage cans and production scrap for a facility owned by South America s largest manufacturer of aluminum cans. This facility has an annual processing capacity of approximately 100 million pounds of aluminum.

We own a facility in Monterrey, Mexico, which recycles aluminum dross and scrap under a long-term contract with a large manufacturer of cylinder heads and engine blocks. This facility has an annual processing capacity of approximately 100 million pounds of aluminum.

POLITICAL AND REGULATORY ENVIRONMENT

General political and economic conditions in foreign countries may affect our business prospects and results of operations. Our foreign operations are generally subject to risks, including foreign currency exchange rate fluctuations, changes in U.S. and foreign governmental regulations, trade restrictions and laws (including tax laws and regulations), tariffs and other trade barriers, the potential for nationalization of enterprises, interest rate fluctuations, inflation, currency restrictions and limitations on repatriation of profits, divergent environmental laws and regulations and political, economic and social instability.

Table of Contents

Index to Financial Statements

Each of our foreign plants is subject to the environmental requirements established by the country and locale in which the plant is located. These requirements differ from country to country, but as in the United States, activities that could harm the environment, such as air emissions of hazardous materials or the management and disposal of waste materials, are subject to regulation. We are also required to obtain and comply with permits or other authorizations for some of the operations at our foreign plants. The environmental regulations in foreign countries are evolving, and it is expected that such requirements will become more stringent in the future. We have been, and will continue to be, required to make expenditures to comply with the environmental requirements applicable to our foreign plants, but, to date, such expenditures have not had a material effect on our results of operations.

In member states of the European Union, some principles of the regulatory environment applicable to VAW-IMCO s operations are set forth by European directives and regulations. These European provisions are implemented into national law or are directly applicable in the individual states. In particular, these rules determine thresholds for certain air emissions, such as sulphur dioxide, nitrogen dioxide, nitrogen oxide, carbon monoxide and suspended dust, and regulate the use of waste as secondary fuel.

According to a decision of the Council of Ministers for the Environment of the European Union, a European Union-wide trade in carbon dioxide emissions is supposed to commence in 2005. The proposal for a directive of the European Parliament and the Council on a system for trading greenhouse gas emissions rights in the European Community has not yet been passed and also would have to be implemented in the member states. Nevertheless, it is expected that the participation in such trading will be mandatory for all industries with high energy consumption levels by 2008. As a consequence, a cap with respect to the amount of carbon dioxide emissions will be determined for each individual company. If the carbon dioxide emissions of a company exceed such individual cap, the company will have to purchase the necessary carbon dioxide emission quantity from another company that has not exhausted its full quota.

SEGMENT REPORTING

Giving effect to the March 2003 consolidation of the results and operations of VAW-IMCO, we now have three business segments that meet the reporting requirements of Statement of Financial Accounting Standards No. 131, Disclosures about Segments of an Enterprise and Related Information. See ITEM 7 MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS SEGMENT INFORMATION and NOTE M SEGMENT INFORMATION of Notes to Consolidated Financial Statements. Previously, VAW-IMCO s financial results had been reported under the equity method of accounting which only recorded our 50% share of VAW-IMCO s after tax earnings. Reportable segments are defined as components of an enterprise about which separate, discrete financial information is available for evaluation.

Our **domestic aluminum** segment represents all of our aluminum melting, processing, alloying, trading and salt cake recovery activities, including investments in joint ventures, within the United States. Our **international aluminum** segment represents all of our aluminum melting, processing, alloying, and trading activities outside of the United States. Our **zinc** segment represents all of our zinc melting, processing and trading activities. Prior period results have been reclassified to reflect the **international aluminum** segment.

Table of Contents

Index to Financial Statements

EMPLOYEES

As of December 31, 2003, we had total of 1,788 employees, consisting of 472 employees engaged in administrative and supervisory activities and 1,316 employees engaged in production and maintenance. Labor relations with employees have been satisfactory. Employees at five of our production facilities are represented by collective bargaining groups as set forth below:

FACILITY	REPRESENTATIVE	NUMBER OF EMPLOYEES	CONTRACT EXPIRES
Hillsboro, IL	Laborer s International Union of North America	15	February 2005
Saginaw, MI	United Auto Workers	21	September 2005
Uhrichsville, OH	United Mine Workers of America	117	January 2005
Töging, Germany	Industry Trade Union for Mining, Chemical and Energy	151	May 2004
Grevenbroich, Germany	Industry Trade Union for Mining, Chemical and Energy	166	April 2004

ENVIRONMENTAL MATTERS

General. Our operations are subject to environmental laws, regulations and ordinances in our plants locales of operation. While we believe that current environmental control measures at our facilities comply in all material respects with current legal requirements, additional measures at some of our facilities may be required. Our operations generate discharges and emissions, including in some cases off-site dust and odors, which are subject to environmental laws, including, in the United States, the Federal Clean Air Act. From time to time, our operations have resulted, or may result, in non-compliance with applicable requirements under environmental laws. We may also incur liabilities for off-site disposals of salt cake and other materials. In addition, historical or current operations at, or in the vicinity of, our facilities, may have resulted in soil or groundwater contamination.

Table of Contents

Index to Financial Statements

Due to relatively high costs and limited coverage, we do not carry environmental impairment liability insurance. Domestically, we made capital expenditures for environmental control facilities of $2,009,000 in 2003, most of which was related to air pollution control equipment for our Clarksville, Tennessee, and Coldwater, Michigan facilities. Domestic environmental expenditures for 2004 and 2005, which primarily relate to our landfills and air pollution control equipment, are currently estimated to be approximately $5,300,000 and $3,000,000, respectively. We expect to spend in 2004 and 2005 a total of approximately $4,800,000 for expansion of our landfill at Morgantown, Kentucky.

Aluminum. The processing of scrap generates solid waste in the form of salt cake and baghouse dust. This material is disposed of at off-site landfills or at our permitted disposal sites at two of our facilities. If salt cake were ever classified as a hazardous waste or substance under RCRA or CERCLA, we would have to modify our handling and disposal practices.

Based on current annual processing volumes, planned utilization rates and remaining landfill capacity, the estimated remaining life of our landfill at our Sapulpa, Oklahoma plant is three years. We estimate that phase two of our Morgantown, Kentucky landfill cell has a remaining useful life of approximately one year. Remaining landfill life at Morgantown is estimated by using independent aerial photography and engineering calculations based on that photography. When the current Morgantown landfill was originally permitted, it was anticipated that there would be three phases to this landfill site. We are currently operating in the second phase. A planned expansion at this landfill in 2004 (which will be the third phase) is anticipated to provide an additional six years of useful life.

The amounts recognized for landfill asset retirement obligations, as of January 1, 2003, were $4,177,000 for our Morgantown, Kentucky landfill and $1,018,000 for our Sapulpa, Oklahoma landfill. The related asset retirement cost for each facility was capitalized as a long-lived asset (asset retirement cost) which is to be amortized over the remaining useful life of the landfills. See NOTE K IMPACT OF RECENTLY ISSUED FINANCIAL ACCOUNTING STANDARDS of Notes to Consolidated Financial Statements.

Table of Contents

Index to Financial Statements

Zinc. Several of our zinc manufacturing processes create various by-products which are either sold to downstream processors or re-used internally. There are virtually no by-products requiring disposal.

ITEM 2. PROPERTIES

Our aluminum facilities are located in:

Sapulpa, Oklahoma(1)
Rockwood, Tennessee(1)
Morgantown, Kentucky(1)
Uhrichsville, Ohio(1)
Loudon, Tennessee(1)
Bedford, Indiana(1)
Chicago Heights, Illinois(1)
Töging, Germany(1)
Elyria, Ohio(1)
Rock Creek, Ohio(1)
Coldwater, Michigan(1)
Swansea, Wales UK(2)
Shelbyville, Tennessee(1)