IMCO RECYCLING INC
Form 10-Q/A
October 21, 2004
Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A

AMENDMENT NO. 1

---

x **Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the Quarterly Period Ended June 30, 2004

¨ **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)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes x No ¨

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the close of business on July 30, 2004.

Common Stock, $0.10 par value, 15,545,308

Table of Contents

EXPLANATORY NOTE TO FORM 10-Q/A AMENDMENT TO FORM 10-Q

FOR QUARTER ENDED JUNE 30, 2004

This Form 10-Q/A (Amendment No. 1) is being filed by IMCO Recycling Inc. with the Securities and Exchange Commission solely for the purpose of reflecting revised and additional disclosures in response to comments received from the staff of the Division of Corporation Finance with the SEC, as well as for the purposes of enhancing our disclosures following discussions with the staff. These amendments principally revise and supplement certain portions of Item 1. Financial Statements, Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations and Item 3. Quantitative and Qualitative Disclosures About Market Risk of Part I of the Company s Quarterly Report on Form 10-Q for the quarterly period ended June 30, 2004 filed with the SEC on August 9, 2004.

This Amendment No. 1 provides revised and additional disclosures under the following captions as follows:

The amendments restate the Consolidated Balance Sheet at June 30, 2004 and December 31, 2003 and the notes related thereto as contained under Item 1. Financial Statements

To reverse a gain recognized in the fourth quarter of fiscal 2003 related to the redemption of the Company s former joint venture partner s share interest in VAW-IMCO Guss und Recycling GmbH (VAW-IMCO), IMCO s German subsidiary. As a result, the consolidated balance sheets have been restated to reflect a reduction in goodwill; and

To reduce accounts receivable by $566,000, for legal fees which should have been expensed in the third quarter of 2003.

The amendments revise the Consolidated Balance Sheets and disclosures under Note D Long-Term Debt of Notes to Consolidated Financial Statements (Unaudited) under Item 1. Financial Statements to reclassify borrowings under our senior revolving credit facility as a current liability, revise the Consolidated Balance Sheet to reclassify restricted cash from current assets to long-term assets at June 30, 2004 and reclassify deferred tax assets from current assets to reduce long-term deferred tax liabilities at June 30, 2004.

The amendments also revise the Consolidated Statements of Cash Flows and Note M Condensed Consolidating Financial Statements under Item 1. Financial Statements and the applicable disclosures under Liquidity and Capital Resources under Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations, in order to reflect the decrease in restricted cash as a financing cash flow instead of an investing cash flow.

The amendments revise Note D Long-Term Debt and Note M Condensed Consolidating Financial Statements to clarify the nature of the guarantees by the company s subsidiaries guaranteeing the debt, reconcile the equity accounts of the Company in the Guarantor Condensed Consolidating Balance Sheets and reflect other changes to the Guarantor Condensed Consolidating Balance Sheets and Consolidating Statements of Cash Flows in the condensed consolidating financial statements shown in Note M.

The amendments further revise Note D Long-Term Debt to show the calculation of the specific undrawn availability tests.

The amendments revise Note L Income Taxes to revise the statutory tax rate reconciliation provided, and Note F Commitments and Contingencies to disclose our inability to make an estimate of any reasonably possible losses resulting from those contingencies listed.

The amendments revise Credit Facilities under Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations to add disclosures regarding certain of the covenants contained in the company s senior revolving credit facility.

The amendments revise the first paragraph under Item 3. Quantitative and Qualitative Disclosures About Market Risk to add language regarding our limitations on fully benefiting from future price changes in prices for natural gas and metals due to its use of hedging instruments.

The amendments revise the presentation under Contractual Obligations under Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations to clarify the treatment of interest payments in the table.

As required by Rule 12b-15 under the Securities Exchange Act of 1934, as amended (the Exchange Act), new certifications by our principal executive officer and principal financial officer are being filed as exhibits to this Form 10-Q/A under Item 6 of Part II.

For purposes of this Form 10-Q/A, and in accordance with Rule 12b-15 under the Exchange Act, each item of our Quarterly Report on Form 10-Q for the quarter ended June 30, 2004 that was affected by this Amendment No. 1 has been amended and restated in its entirety.

Table of Contents

No attempt has been made in this Form 10-Q/A to modify or update other disclosures as presented in the original Form 10-Q, except as required to reflect such amendments. This Amendment No. 1 continues to speak as of the date of filing the original Form 10-Q, and we have not updated the disclosures contained therein to reflect any events that occurred at a date subsequent to the filing of the original Form 10-Q (including disclosures relating to risks, uncertainties and other factors that may affect our future performance). You should read this Amendment No. 1 together with other documents that we have filed with the Securities and Exchange Commission subsequent to the filing of our original Form 10-Q in August 2004. Information contained in such reports and documents updates and supersedes certain information contained in this Form 10-Q/A.

Table of Contents

INTRODUCTORY NOTE

On July 21, 2004, IMCO Recycling Inc. (IMCO) filed a Registration Statement on Form S-4 with the Securities and Exchange Commission (SEC) containing a preliminary joint proxy statement/prospectus regarding a proposed merger between IMCO and Commonwealth Industries, Inc. (Commonwealth). Information concerning IMCO and the proposed merger with Commonwealth is contained in the Registration Statement, which, along with other filings containing information about IMCO, can be found at the SEC s Internet site (http://www.sec.gov). The information contained in the Registration Statement on Form S-4 as filed on July 21, 2004 is subject to amendment. See NOTE B - IMCO RECYCLING INC. AND COMMONWEALTH INDUSTRIES, INC. PROPOSED MERGER of the Notes to Consolidated Financial Statements contained in this Quarterly Report on Form 10-Q.

TABLE OF CONTENTS

	Page
Part I. Financial Information	5
Item 1. Financial Statements	5
Consolidated Balance Sheets as of December 31, 2003, and June 30, 2004	5
Consolidated Statements of Operations for the three months and six months ended June 30, 2004 and June 30, 2003	6
Consolidated Statements of Cash Flow for the six months ended June 30, 2004 and June 30, 2003	7
Notes to Unaudited Consolidated Financial Statements	8
Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations	24
Item 3. Quantitative and Qualitative Disclosures about Market Risk	40
Part II. Other Information	43
Item 6. Exhibits and Reports on Form 8-K	43

Table of Contents

PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

IMCO RECYCLING INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(in thousands, except share data)

	June 30, 2004	December 31, 2003
	Restated (unaudited)	Restated
ASSETS		
Current Assets		
Cash and cash equivalents	$ 13,934	$ 14,760
Accounts receivable (net of allowance of $1,540 and $1,228 at June 30, 2004 and December 31, 2003, respectively)	131,972	111,562
Inventories	82,514	78,270
Deferred income taxes	1,916	11,444
Other current assets	12,434	12,382
Total Current Assets	242,770	228,418
Property and equipment, net	212,829	219,668
Goodwill	63,807	63,617
Restricted cash	18,917	24,846
Investments in joint ventures	831	976
Other assets, net	14,225	13,209
Total Assets	$ 553,379	$ 550,734
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities		
Accounts payable	$ 88,870	$ 96,207
Accrued liabilities	37,384	30,955
Current maturities of long-term debt	43,316	33,017
Total Current Liabilities	169,570	160,179
Long-term debt	223,230	223,176
Deferred income taxes	9,241	20,390
Other long-term liabilities	25,705	25,244
STOCKHOLDERS EQUITY		
Preferred stock; par value $0.10: 8,000,000 shares authorized; none issued		
Common stock; par value $0.10: 40,000,000 shares authorized; 17,159,026 issued at June 30, 2004; 17,155,211 issued at December 31, 2003	1,716	1,716
Additional paid-in capital	103,607	103,264

Deferred stock compensation	(3,154)	(4,153)
Retained earnings	48,405	45,406
Accumulated other comprehensive loss	(6,892)	(4,825)
Treasury stock, at cost; 1,692,076 shares at June 30, 2004; 1,843,403 shares at December 31, 2003	(18,049)	(19,663)
Total Stockholders Equity	125,633	121,745
	$ 553,379	$ 550,734

See Notes to Consolidated Financial Statements.

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(in thousands, except per share data)

	For the three months ended June 30,		For the six months ended June 30,	
	2004	**2003**	**2004**	**2003**
Revenues	$ 292,439	$ 239,452	$ 570,947	$ 434,535
Cost of sales	270,023	221,613	525,384	404,789
Gross profit	22,416	17,839	45,563	29,746
Selling, general and administrative expense	14,717	9,452	26,648	17,457
Fees on receivables sale		291		581
Interest expense	6,861	3,704	13,305	6,053
Other (income) expense, net	41	(45)	184	22
Equity in net loss (earnings) of affiliates	62	14	45	(911)
Earnings before provision for income taxes and minority interests	735	4,423	5,381	6,544
Provision for income taxes	387	1,847	2,295	2,493
Earnings before minority interests	348	2,576	3,086	4,051
Minority interests, net of provision for income taxes	60	113	87	265
Net earnings	$ 288	$ 2,463	$ 2,999	$ 3,786
Net earnings per common share:				
Basic	$ 0.02	$ 0.17	$ 0.20	$ 0.26
Diluted	0.02	0.17	0.20	0.26
Weighted average shares outstanding:				
Basic	14,814	14,457	14,658	14,480
Diluted	15,313	14,519	15,097	14,533

See Notes to Consolidated Financial Statements.

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOW

(Unaudited)

(in thousands)

	For the six months ended June 30,	
	2004	**2003**
OPERATING ACTIVITIES		
Net earnings	$ 2,999	$ 3,786
Depreciation and amortization	14,197	13,291
Provision for (benefit from) deferred income taxes	(2,134)	331
Equity in loss (earnings) of affiliates	45	(911)
Non-cash retirement charge	1,576	
Other non-cash charges	3,459	2,869
Changes in operating assets and liabilities:		
Accounts receivable	(22,127)	(1,460)
Accounts receivable sold		(5,000)
Inventories	(5,011)	(3,737)
Other current assets	(131)	2,309
Accounts payable and accrued liabilities	4,565	(5,227)
Net cash from (used by) operating activities	(2,562)	6,251
INVESTING ACTIVITIES		
Payments for property and equipment	(12,563)	(7,723)
Net cash acquired in acquisition of remaining 50% of VAW-IMCO		15,669
Acquisition costs	(1,889)	
Other	30	486
Net cash from (used by) investing activities	(14,422)	8,432
FINANCING ACTIVITIES		
Net proceeds from long-term revolving credit facility	10,295	4,000
Net payments of long-term debt		(694)
Decrease in restricted cash	5,929	
Debt issuance costs	(510)	(757)
Other	622	(371)
Net cash from financing activities	16,336	2,178
Effect of exchange rate differences on cash and cash equivalents	(178)	595
Net increase (decrease) in cash and cash equivalents	(826)	17,456
Cash and cash equivalents at January 1	14,760	6,875
Cash and cash equivalents at June 30	$ 13,934	$ 24,331

SUPPLEMENTARY INFORMATION		
Cash payments for interest	$ 12,728	$ 4,388
Cash payments for income taxes, net of refunds received	$ 2,146	$ 1,508

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

June 30, 2004

(dollars in tables are in thousands, except per share data)

NOTE A BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the three and six month periods ended June 30, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. The accompanying financial statements include the accounts of IMCO Recycling Inc. and all of its subsidiaries (collectively, except where the context otherwise requires, referred to as IMCO , the Company , we, us, our or similar terms). All significant intercompany accounts and transactions have been eliminated. For further information, refer to the consolidated financial statements and footnotes, as amended, thereto included in our Annual Report on Form 10-K/A for the year ended December 31, 2003. Certain reclassifications have been made to prior period statements to conform to the current period presentation.

NOTE B IMCO RECYCLING INC. AND COMMONWEALTH INDUSTRIES INC. PROPOSED MERGER

On June 16, 2004, we announced the execution of a definitive merger agreement for a business combination of IMCO with Commonwealth Industries, Inc. Under the merger, we will acquire each outstanding share of Commonwealth common stock in exchange for 0.815 shares of IMCO common stock. The merger is expected to give IMCO and Commonwealth approximately equal representation on the combined company s board of directors, and IMCO s stockholders are expected to own approximately 54% of the combined company immediately following the merger. The transaction is expected to close in the fourth quarter of 2004, and its completion is subject to regulatory approval, successful completion of the refinancing of certain indebtedness of the two companies, and stockholder approval by both companies, as well as other customary closing conditions. We have capitalized $1,889,000 in acquisition costs related to this transaction as of June 30, 2004. More information on the proposed merger transaction is available in IMCO s Current Report on Form 8-K filed with the SEC on June 18, 2004.

Commonwealth is one of North America s leading manufacturers of aluminum sheet for distributors, transportation, construction and consumer durables end-use markets. Commonwealth has direct-chill casting facilities in Kentucky and continuous casting mini-mills in Ohio and California. The combination is expected to create a new vertically integrated company that can be a strong competitor in the global aluminum recycling and production industries, having benefits from procurement savings and cost synergies, an enhanced competitive position, increased scope and scale, greater technological capabilities, and improved access to capital.

NOTE C INVENTORIES

The components of inventories are:

	June 30, 2004	December 31, 2003
Finished goods	$ 38,215	$ 36,329
Raw materials	37,623	33,428
Work in process	3,981	4,613
Supplies	2,695	3,900
	$ 82,514	$ 78,270

Table of Contents

NOTE D LONG-TERM DEBT

Our long-term debt is summarized as follows:

	June 30, 2004	December 31, 2003
	Restated	Restated
Senior Credit Facility, expiring in October 2007	$ 43,286	$ 32,991
10 3/8% Senior Secured Notes, due October 6, 2010 (net of discount)	208,802	208,751
7.65% Morgantown, Kentucky Solid Waste Disposal Facilities Revenue Bonds-1996 Series, Due May 1, 2016 (net of discount)	5,706	5,705
7.45% Morgantown, Kentucky Solid Waste Disposal Facilities Revenue Bonds-1997 Series, Due May 1, 2022	4,600	4,600
6.00% Morgantown, Kentucky Solid Waste Disposal Facilities Revenue Bonds-1998 Series, Due May 1, 2023	4,100	4,100
Other	52	46
Subtotal	266,546	256,193
Less current maturities	43,316	33,017
Total	$ 223,230	$ 223,176

Senior Secured Notes

In October 2003, we issued $210,000,000 principal amount of senior secured notes as part of a refinancing of our debt facilities. The issue was priced at 99.383% to yield 10.50% and provided $208,704,000 of gross proceeds, after offering discount. Interest is payable semi-annually, on April 15 and October 15 of each year, commencing on April 15, 2004. In addition, in October 2003 we established a new four-year $120,000,000 senior secured revolving credit facility (senior credit facility). Our former senior credit facility and former receivables sale facility, which were both scheduled to expire by their terms in the fourth quarter of 2003, were replaced by the senior secured notes and the new senior credit facility.

The senior secured notes are redeemable at our option, in whole or in part, at any time after October 15, 2007. At any time prior to October 15, 2006, we may redeem up to 35% of the aggregate principal amount of the senior secured notes with the proceeds of one or more equity offerings of our common shares at a redemption price of 110.375% of the principal amount of the senior secured notes, together with accrued and unpaid interest, if any, to the date of the redemption.

The senior secured notes are jointly and severally, unconditionally guaranteed on a senior basis by all of our existing 100% owned domestic subsidiaries that are co-borrowers under the senior credit facility and by any future domestic restricted subsidiaries. The senior secured notes are not guaranteed by any of our current foreign subsidiaries. See NOTE M CONDENSED CONSOLIDATING FINANCIAL STATEMENTS. The senior secured notes and guarantees are secured by first-priority liens, subject to permitted liens, on the real property, fixtures and equipment relating to our wholly-owned domestic operating plants and on the fixtures and equipment relating to substantially all of our leased domestic operating plants. The liens securing the senior secured notes do not extend to any of our inventory, accounts receivable and related property (which secure the senior credit facility) or to any of our foreign real or personal property.

Upon the occurrence of a change of control (as defined under the indenture governing the senior secured notes), we are required to offer to purchase the senior secured notes at a price equal to 101% of the principal amount of the outstanding senior secured notes plus accrued interest. The proposed merger of IMCO and Commonwealth is not expected to cause a change of control of IMCO under the indenture.

The indenture governing the senior secured notes, among other things, contains covenants limiting our ability and the ability of our restricted subsidiaries to incur additional debt; grant liens; make restricted payments, including paying dividends or making investments; sell or otherwise dispose of assets, including capital stock of subsidiaries; engage in sale-leaseback transactions; create liens on our or our subsidiaries assets; receive distributions; engage in transactions with affiliates; and merge or sell substantially all of our or our subsidiaries assets. The proposed merger of IMCO and Commonwealth is not expected to violate any covenants under the indenture.

Senior Credit Facility

As of June 30, 2004, we had $43,286,000 of indebtedness outstanding under our senior credit facility. Under this facility, we are subject to a borrowing base limitation based on eligible domestic inventory and receivables. As of June 30, 2004, we estimated that our borrowing base would have supported additional borrowings of $38,801,000 after giving effect to outstanding borrowings of $43,286,000 and outstanding letters of credit of $6,805,000. As of June 30, 2004, our total borrowing base was estimated to be approximately $88,892,000.

Table of Contents

The terms of our senior credit facility include, among other covenants, (i) prohibitions against incurring certain indebtedness and granting liens, (ii) limitations on dividends and repurchases of shares of capital stock, and (iii) limitations on capital expenditures, investments and acquisitions. The indebtedness under the senior secured credit facility is secured by the Company s and its co-borrowers inventories, receivables, general intangibles and the proceeds thereof. We are subject to the terms of a lockbox arrangement with the administrative agent bank under the senior credit facility, whereby funds deposited from collections of receivables are applied by the lenders to reduce outstanding balances of the borrowings under the senior credit facility. If at any time during specified periods, our undrawn availability under this facility is less than $50,000,000, we will also be required to maintain a minimum fixed coverage ratio and minimum tangible net worth, as follows:

a minimum fixed charge coverage ratio of 1.0 to 1.0 (calculated based on our parent entity and wholly-owned domestic subsidiaries), and

a minimum tangible net worth of $44,500,000 plus 50% of future net income on a consolidated basis.

As of June 30, 2004, our undrawn availability was less than $50,000,000, requiring us to be in compliance with these two financial covenants. In addition, under our senior credit facility, we are currently unable to pay cash dividends to our stockholders. As of June 30, 2004, we were in compliance with all applicable debt covenants.

The terms of our senior credit facility also include covenants prohibiting certain mergers and acquisitions (including the completion of the proposed merger of IMCO and Commonwealth) without the consent of the lenders under the facility. However, the indebtedness under the senior credit facility is expected to be refinanced and replaced by a new facility or facilities at or before the completion of the proposed merger. Completion of this merger is conditioned upon, among other things, the refinancing of certain outstanding indebtedness of the two companies. See NOTE B IMCO RECYCLING INC. AND COMMONWEALTH INDUSTRIES, INC. PROPOSED MERGER.

On May 26, 2004, IMCO and its co-borrower subsidiaries under our senior credit facility entered into a First Amendment to Revolving Credit and Security Agreement with the lenders parties thereto. This amendment revised the definitions of EBITDA and Fixed Charge Ratio contained in the senior credit facility. The changes were made to enable IMCO to make withdrawals from a cash collateral account established under the terms of our senior secured notes indenture without having the amounts withdrawn being deemed capital expenditures for purposes of complying with the fixed charge coverage ratio covenant. In addition, the covenant restricting annual capital expenditures was amended to permit capital expenditures in fiscal 2004 of up to $25 million for IMCO and its co-borrowers, and then up to $20 million for IMCO and its co-borrowers for fiscal 2005 and each fiscal year thereafter during the term of the facility.

On July 16, 2004, IMCO and its co-borrower subsidiaries entered into a Second Amendment to Revolving Credit and Security Agreement. This amendment modified a section of the senior credit facility that had provided that any change in the condition or affairs of IMCO or its co-borrowers which, in the lenders agent s reasonable opinion, has a material adverse effect (as defined in the senior credit facility), would be deemed an event of default under the senior credit facility. The Second Amendment to Revolving Credit and Security Agreement revised this provision so that it now provides that such an event of default would not be applicable and that the agent and the lenders would have no rights under the provision, so long as IMCO was in compliance with certain undrawn availability tests under the senior credit facility. If the level of undrawn availability falls below $3,000,000 for three consecutive business days or below an average of $10,000,000 per day for any calendar month, then the lenders rights under this provision would be reinstated.

The amounts outstanding under the new senior secured credit facility are classified as a current liability because the terms of the facility contain contractual provisions that require the cash receipts of the Company be used to repay amounts outstanding under the revolving credit facility.

VAW-IMCO credit facilities

Our German subsidiary, VAW-IMCO Guss und Recycling GmbH (VAW-IMCO), has two lines of credit available for its working capital needs. The total amount of credit available under these facilities is 15,000,000 Euros ($18,294,000 U.S. Dollars). During the second quarter of 2004, the terms of these credit facilities were renewed and extended, and these facilities now are scheduled to expire in April and May of 2006. As of June 30, 2004, no amounts were outstanding under these lines of credit.

Other

In February 2004, VAW-IMCO paid IMCO approximately 20,000,000 Euros (U.S. $24,846,000, including interest), repaying in full its indebtedness owed to IMCO under an intercompany note that IMCO had pledged in October 2003 as part of the collateral security for the senior secured notes. The prepayment of this intercompany note, which was denominated in U.S. Dollars, resulted in a recognized gain of $278,000 for the first quarter of 2004. The funds were deposited in a collateral account held by the trustee under the indenture governing the senior secured notes, which permits us for a one-year period to use these funds for acquisitions and construction of assets and properties to be used in our domestic business, which will be added to and form a part of the collateral security for the senior secured notes. For the six months ended June 30, 2004, we have withdrawn $5,929,000 for capital expenditures relating to manufacturing equipment, pollution control equipment and buildings. These assets now form part of the collateral security for the senior secured notes.

Table of Contents

NOTE E NET EARNINGS PER SHARE

The following table set forth the reconciliation between weighted average shares used for calculating basic and diluted earnings per share (EPS):

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
	(dollars in thousands, except per-share amounts)			
Numerators for basic and diluted earnings per share:	$ 288	$ 2,463	$ 2,999	$ 3,786
Denominator:				
Denominator for basic earnings per share-weighted-average shares	14,814,096	14,457,108	14,657,534	14,479,607
Dilutive potential common shares- stock options	499,004	61,681	438,986	53,548
Denominator for diluted earnings per share	15,313,100	14,518,789	15,096,520	14,533,155
Net earnings per share:				
Basic	$ 0.02	$ 0.17	$ 0.20	$ 0.26
Diluted	$ 0.02	$ 0.17	$ 0.20	$ 0.26

As of June 30, 2004, we had a total of 330,000 shares of restricted stock outstanding. All outstanding shares of restricted stock are unvested and therefore are excluded from our basic earnings per share calculation. We also had stock options outstanding to purchase up to 386,572 shares that were considered anti-dilutive.

NOTE F COMMITMENTS AND CONTINGENCIES

General

Our operations, like those of other basic industries, are subject to federal, state, local and foreign laws, regulations and ordinances. These laws and regulations (i) govern activities or operations that may have adverse environmental effects, such as discharges to air and water, as well as handling and disposal practices for solid and hazardous wastes and (ii) impose liability for costs of cleaning up, and certain damages resulting from past spills, disposals or other releases of hazardous substances. It can be anticipated that more rigorous environmental laws will be enacted that could require us to make substantial expenditures in addition to those described here.

From time to time, our operations have resulted, or may result, in certain non-compliance with applicable requirements under environmental laws. However, we believe that any such non-compliance under such environmental laws would not have a material adverse effect on our financial position or results of operations.

Environmental proceedings

In 1997, the Illinois Environmental Protection Agency (IEPA) notified us that two of our zinc subsidiaries were potentially responsible parties (PRP) pursuant to the Illinois Environmental Protection Act for the cleanup of contamination at a site in Marion County, Illinois to which these subsidiaries, among others, in the past had sent zinc oxide for processing and resale. The site has not been fully investigated and final estimated cleanup costs have not yet been determined. Because of the nature of this matter, we cannot make an estimate of reasonable possible losses. We have been informed by the IEPA that the agency is preparing a revised list of companies that may have sent materials to the site and the volume of materials sent by each company. Once we receive this information, we may seek, possibly in connection with other PRPs, an agreed resolution of the IEPA s claims.

On February 15, 2001, the State of Michigan filed a lawsuit against us in the State Circuit Court for the 30th District, Ingham County, Michigan. The lawsuit arose out of disputes between our Alchem Aluminum Inc. subsidiary and Michigan environmental authorities concerning air emission control permits at Alchem s aluminum specialty alloy production facilities in Coldwater, Michigan. The State claimed injunctive relief and penalties for alleged non-compliance with and violations of federal and state environmental laws. The suit sought compliance by us, as well as potentially substantial monetary penalties. On January 14, 2004, the parties settled the lawsuit by entering a Consent Judgment with the State Circuit Court. The Consent Judgment requires that we (i) operate our Coldwater aluminum facilities in compliance with a permit compliance program, (ii) adhere to certain recordkeeping, notification and testing guidelines, (iii) install a baghouse and associated equipment at our Alchem facility in Coldwater; and (iv) pay a civil fine in the amount of $300,000 to the State of Michigan. We have paid the civil fine and are currently in compliance with the Consent Judgment.

On April 27, 2001, the U. S. Environmental Protection Agency, Region V, issued to us a Notice of Violation (NOV) alleging violations of the federal Clean Air Act, primarily for violations of the Michigan State Implementation Plan at our Coldwater facilities.

Table of Contents

The NOV addressed the same instances of alleged non-compliance raised in the State of Michigan lawsuit, alleging that we had purportedly failed to obtain appropriate preconstruction air quality permits prior to conducting modifications to the Coldwater facilities and exceeded permitted emission levels. All issues raised in the NOV have been resolved through the State of Michigan lawsuit and Consent Judgment.

On March 17, 2004, we were named as a co-defendant in a lawsuit filed in the U.S. District Court for the Central District of California. The listed claimants are the current owners of a Corona, California property formerly owned by one of our subsidiaries. The petition seeks declaratory relief and damages in an unspecified amount in connection with an alleged release of hazardous substances on the property. Because of the nature of this matter, we cannot make an estimate of reasonable possible losses. We believe that we have meritorious defenses to the claims contained in the petition. We plan a vigorous defense against these claims and are seeking indemnification from certain of the other co-defendants.

There is the possibility that expenditures could be required at our other facilities from time to time, because of new or revised regulations that could require that additional expenditures be made for compliance purposes. These expenditures could materially affect our results of operations and financial condition in future periods.

Other legal proceedings

In 1998 an employee filed a personal injury claim against us (Bland v. IMCO Recycling Inc.) in Missouri state court. In August 2002 the trial court entered a final judgment against us for $4,000,000. We are also involved in litigation with the surety for the appeal bond that was levied to secure the judgment in the Bland case (IMCO Recycling Inc. v. American Guarantee & Liability Insurance Company), currently pending in the Missouri Circuit Court of Appeals. To date, we have not paid any portion of the Bland judgment or reimbursed the surety. In a lawsuit between us and our umbrella coverage insurer to resolve a dispute as to coverage in the Bland case (Twin City Fire Insurance Company v. IMCO Recycling Inc.), a federal district court in Missouri entered an amended judgment in our favor in March 2004. We have reached a settlement, and in July 2004 we recovered $568,000 in attorneys fees that had previously been expensed. We have withdrawn the motion. Based on the favorable amended judgment, we believe that there is insurance coverage for the Bland claim and that we will be indemnified for any payments that we must make. We have not established any reserves for the Bland case.

We are also a party from time to time to what we believe are routine litigation and proceedings considered part of the ordinary course of our business. We believe that the outcome of such proceedings would not have a material adverse effect on our financial position or results of operations.

NOTE G OTHER COMPREHENSIVE EARNINGS (LOSS)

The following table presents the components of other comprehensive earnings (loss). These items change equity during the reporting period, but are not included in earnings.

	Total	Unrealized Gain (Loss) on Derivative Financial Instruments	Foreign Currency Translation, Unrealized Gain (Loss)

Balance at December 31, 2003	$ (4,825)	$ 1,939	$ (6,764)
Current period net change	(1,770)		(1,770)
Change in fair value of derivative financial instruments	2,115	2,115	
Reclassification of (gains) on derivative financial instruments into earnings	(2,593)	(2,593)	
Income tax effect	181	181	
Balance at June 30, 2004	$ (6,892)	$ 1,642	$ (8,534)

We translate the balance sheets of our foreign subsidiaries using fiscal period-end exchange rates. The consolidated statements of earnings are translated using the average exchange rates for the period. The cumulative effect of such translations is included in stockholders equity, other than for current intercompany accounts, as a component of other comprehensive earnings (loss). Foreign currency translation adjustments, unrealized gains or losses, accumulate in equity until the final disposition of their respective operations.

See NOTE O MARKET RISK MANAGEMENT USING FINANCIAL INSTRUMENTS for further information in regards to our deferred hedging activities.

Table of Contents

NOTE H SEGMENT REPORTING

Description of the Types of Products and Services from which Each Reportable Segment Derives its Revenues:

With the consolidation of VAW-IMCO in 2003, we now have the following product lines: Aluminum Recycling, Specialty Alloy, Zinc and International Aluminum.

The Aluminum Recycling and Specialty Alloy product lines have been aggregated for reporting purposes into one business segment for financial reporting purposes Domestic Aluminum and represents all of our aluminum melting, processing, alloying, trading and salt cake recycling activities within the United States. We have aggregated these businesses because the products produced are identical, (except for minor differences in chemical composition), are delivered in the same manner (either molten or in bars), the raw materials used are very similar, the production processes and equipment used are identical, and they report to the same member of executive management. Our international aluminum segment represents all of our aluminum melting, processing, alloying and trading activities outside the United States. Our zinc segment represents all of our zinc melting, processing and trading activities.

Measurement of Segment Profit or Loss and Segment Assets:

The accounting policies of the reportable segments are the same as those described in NOTE A SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES of our Form 10-K for the year ended December 31, 2003. We evaluate performance based on gross profit or loss from operations, net of selling expenses, which we title Segment Income. Provision for income taxes, interest expense, certain amounts of other (income) expense, net, corporate general and administrative costs, including depreciation of corporate assets and amortization of capitalized debt costs, are not allocated to the reportable segments. Intersegment sales and transfers are recorded at market value; net profits on intersegment sales and transfers were immaterial for the periods presented. Consolidated cash, net unamortized debt costs, net current deferred tax assets and assets located at our headquarters office in Irving, Texas are not allocated to the reportable segments.

Factors Management Used to Identify Our Reportable Segments:

Our reportable segments are business units that offer different types of metal products and services in different geographic locations. The reportable segments are each managed separately, because they produce distinct products and services and sell to different types of customers. The following table shows our segment assets for the indicated periods:

	June 30, 2004 Restated	December 31, 2003 Restated
Assets:		
Domestic Aluminum	$ 265,684	$ 232,209

International Aluminum	159,553	175,345
Zinc	105,122	109,815
Other unallocated assets	23,020	33,365
Total assets	$ 553,379	$ 550,734

The following table shows our revenues and income for the three and six month periods ended June 30, 2004 and June 30, 2003, respectively.

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
REVENUES:				
Domestic Aluminum	$ 143,931	$ 121,857	$ 281,610	$ 248,974
International Aluminum	92,594	80,558	183,267	113,822
Zinc	55,914	37,037	106,070	71,739
Total revenues	$ 292,439	$ 239,452	$ 570,947	$ 434,535
INCOME:				
Domestic Aluminum	$ 9,267	$ 5,363	$ 15,887	$ 11,176
International Aluminum	4,986	6,316	11,943	9,225
Zinc	2,884	1,404	6,777	2,510
Total segment income	$ 17,137	$ 13,083	$ 34,607	$ 22,911
Unallocated amounts:				
General and administrative expenses	$ (9,534)	$ (4,709)	$ (15,893)	$ (9,701)
Interest expense	(6,861)	(3,704)	(13,305)	(6,053)
Fees on receivables sale		(291)		(581)
Interest and other income	(7)	44	(28)	(32)
Earnings before provision for income taxes and minority interests	$ 735	$ 4,423	$ 5,381	$ 6,544

Table of Contents

NOTE I VAW-IMCO

VAW-IMCO owns and operates two aluminum recycling foundry alloy facilities in Grevenbroich and Töging, Germany, that together have an annual melting capacity in excess of 700 million pounds. VAW-IMCO supplies specialty alloys to the European automobile industry and serves other European aluminum markets.

Through a wholly-owned subsidiary, we had previously owned a 50% share interest in VAW-IMCO, with Hydro Aluminium Deutschland GmbH (Hydro) owning the remaining 50% share interest. On March 14, 2003, we entered into an agreement with Hydro and VAW-IMCO, finalizing the terms and conditions whereby VAW-IMCO would redeem its shares owned by Hydro. As a result of this agreement, voting control of VAW-IMCO was effectively vested in a wholly-owned subsidiary of ours, and effective March 1, 2003, the accounts of VAW-IMCO were consolidated with those of ours and reflected within our consolidated financial statements. Prior to that date, the accounts of VAW-IMCO were reflected in our financial statements under the equity method of accounting. This effective acquisition of the remaining 50% interest in VAW-IMCO was an important step in the ongoing expansion of our international operations.

The following table represents our condensed unaudited pro forma statement of operations for the six months ended June 30, 2003. The unaudited pro forma information is not necessarily indicative of the results of operations that would have occurred had the acquisition been made at the beginning of the periods presented or the future results of the combined operations. The condensed unaudited pro forma statement of operations assumes that the consolidation of VAW-IMCO occurred on January 1, 2003.

	Six months ended June 30, 2003
Revenues	$ 486,123
Gross profit	35,709
Net earnings	4,434
Net earnings per common share:	
Basic	$ 0.31
Diluted	$ 0.31
Weighted average shares outstanding:	
Basic	14,480
Diluted	14,533

NOTE J STOCK BASED COMPENSATION

We follow Accounting Principles Board Opinion No. 25 (APB 25), Accounting for Stock Issued to Employees, and related interpretations in accounting for our employee stock options. Under APB 25, if the exercise price of employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recorded. We have adopted the pro forma disclosure features of Statement of Financial Accounting Standards (SFAS) No. 123, Accounting for Stock-Based Compensation, as amended by SFAS No. 148, Accounting for Stock-Based Compensation-Transition and Disclosure. Our net earnings and earnings per share would have been reduced to the pro forma amounts shown below if compensation cost had been determined based on the fair value at the grant dates.

Our pro forma information below is presented as if we had applied the fair value recognition provision of SFAS 123 Accounting for Stock-Based Compensation.

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
Net earnings, as reported	$ 288	$ 2,463	$ 2,999	$ 3,786
Add: stock-based compensation expense included in reported net earnings, net of tax	1,118	88	1,284	179
Less: compensation cost determined under the fair value method, net of tax	(1,281)	(259)	(1,615)	(523)
Pro forma net earnings	$ 125	$ 2,292	$ 2,668	$ 3,442
Basic earnings per share:				
As reported	$ 0.02	$ 0.17	$ 0.20	$ 0.26
Pro forma	0.01	0.16	0.18	0.24
Diluted earnings per share:				
As reported	$ 0.02	$ 0.17	$ 0.20	$ 0.26
Pro forma	0.01	0.16	0.18	0.24

Table of Contents

NOTE K STOCKHOLDERS EQUITY

In February and May 2004, we awarded a total of 147,000 restricted stock units to certain of our officers and key employees. The restricted stock units cannot be transferred or pledged and are subject to forfeiture if the holder s employment with us terminates for any reason other than death, disability or retirement. The restricted stock units fully vest upon the earlier of the fifth anniversary of the date of grant, a change of control of the company or upon the holder s death, disability or retirement. The vested restricted stock units are exchangeable into shares of IMCO common stock. We recorded $1,594,000 in deferred compensation as a reduction to stockholders equity related to these awards. This amount will be recorded as compensation expense over the vesting period of the restricted stock units.

Don V. Ingram resigned as chairman of the board, president and chief executive officer of the company in April 2004. In 2000 and 2002, our board of directors had approved grants of contractual restricted stock awards to Mr. Ingram for a total of 600,000 shares. As a consequence of Mr. Ingram s resignation, as of May 7, 2004, 450,000 shares of common stock were fully vested in accordance with the terms of his restricted stock award agreement resulting in a charge of $1,576,000. The remaining 150,000 shares of his restricted stock were cancelled and returned to treasury stock. In addition, Mr. Ingram received a cash severance payment of $1,500,000. The total charge of $3,655,000 relating to the cash payment, vesting of the 450,000 shares of restricted common stock and certain legal expenses was recognized in the second quarter of 2004 in selling, general and administrative expense.

NOTE L INCOME TAXES

Our effective tax rate was 43% for the six months ended June 30, 2004. This compares to an effective tax rate of 38% for the comparable period in 2003. The effective tax rate for the three and six-month periods ended June 30, 2004 was impacted because we have not recognized deferred state income tax benefits for 2004 as a result of domestic operating losses. Our provision for income tax in 2003 excluded the equity income from VAW-IMCO, which is recorded on an after tax basis.

Higher interest expense and payments for departing executives have generated net operating losses in the U.S. for federal income tax purposes for the six month period ended June 30, 2004. Deferred tax benefits related to these net operating losses have been recorded for U.S. federal income tax purposes. While our overall effective tax rate for 2004 contemplates the utilization of such operating loss carryforwards, if further profit improvements in our domestic operations do not occur, the recording of additional U.S. federal income tax benefits for 2004 will need to be re-evaluated.

We have recorded net deferred tax assets in various state jurisdictions totaling $5,664,000, which includes amounts recorded related to the benefit for loss carryforwards and tax credits, and which expire in varying amounts between 2005 and 2024. A valuation allowance of $2,345,000 has been provided related to such net deferred tax assets. Realization is dependent on generating sufficient taxable income prior to expiration of the loss carryforwards. Although realization is not assured, management believes it is more likely than not that all of the deferred tax asset will be realized. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced.

Finally, our deferred tax asset and liability positions for both U.S. federal and various state jurisdictions will be taken into consideration in accounting for the proposed acquisition of Commonwealth (see NOTE B IMCO RECYCLING INC. AND COMMONWEALTH INDUSTRIES, INC. PROPOSED MERGER) and the amount of deferred tax positions recorded in conjunction with the purchase price allocation could be impacted.

The provision for income taxes was as follows:

	For the six months ended June 30,	
	2004	**2003**
Current:		
Federal	$ 1	$ (105)
State	151	78
Foreign	4,277	2,189
	4,429	2,162
Deferred:		
Federal	(2,415)	358
State		(62)
Foreign	281	35
	(2,134)	331
Provision for income taxes	$ 2,295	$ 2,493

Table of Contents

The income tax expense (benefit), computed by applying the federal statutory rate to earnings (loss) before income taxes, differed from the provision for income taxes as follows:

	For the six months ended June 30,	
	2004	2003
Income taxes at the federal statutory rate	$ 1,883	$ 2,290
Foreign tax rate difference	88	122
State income taxes, net	98	9
Foreign income not currently taxable	19	(335)
Other, net	207	407
Provisions for income taxes	$ 2,295	$ 2,493

NOTE M CONDENSED CONSOLIDATING FINANCIAL STATEMENTS

Certain of our subsidiaries are guarantors of the indebtedness of IMCO under its senior secured notes. See NOTE D - LONG-TERM DEBT. For purposes of complying with the reporting requirements of these guarantor subsidiaries, presented below are condensed consolidating financial statements of IMCO Recycling Inc., the Guarantor Subsidiaries, and those subsidiaries of IMCO Recycling Inc. that are not guaranteeing the indebtedness under the senior secured notes (Non-Guarantor Subsidiaries).

The condensed consolidating balance sheets are presented as of June 30, 2004, the condensed consolidating statements of operations are presented for the three and six months ended June 30, 2004 and 2003 and the condensed consolidating statements of cash flows are presented for the six months ended June 30, 2004 and 2003.

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

GUARANTOR CONDENSED CONSOLIDATING BALANCE SHEETS

As of June 30, 2004 (Restated)

	IMCO Recycling Inc.	Combined Guarantor Subsidiaries	Combined Non-guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current Assets					
Cash and cash equivalents	$ 325	$ 46	$ 13,563	$	$ 13,934
Accounts receivable, net	7,869	76,736	47,424	(57)	131,972
Inventories	2,191	53,137	27,186		82,514
Deferred Income Taxes	331	215	1,370		1,916
Other current assets	3,706	5,658	3,070		12,434
Total Current Assets	14,422	135,792	92,613	(57)	242,770
Property and equipment, net	36,305	104,431	73,950	(1,857)	212,829
Goodwill	3,760	49,631	10,416		63,807
Restricted cash	18,917				18,917
Investments in joint ventures		831			831
Deferred income taxes	6,042			(6,042)	
Other assets, net	10,373	3,066	786		14,225
Investments in subsidiaries/ intercompany receivable (payable), net	327,075	(100,196)	(4,350)	(222,529)	
	$ 416,894	$ 193,555	$ 173,415	$ (230,485)	$ 553,379
LIABILITIES AND STOCKHOLDERS EQUITY					
Current Liabilities					
Accounts payable	$ 10,986	$ 47,645	$ 30,296	$ (57)	$ 88,870
Accrued liabilities	8,287	8,408	20,689		37,384
Current maturities of long-term debt	43,286	26	4		43,316
Total Current Liabilities	62,559	56,079	50,989	(57)	169,570
Long-term debt	223,209	15	6		223,230
Deferred income taxes		6,746	8,537	(6,042)	9,241
Other long-term liabilities	5,493	3,769	16,443		25,705
Total Stockholders Equity	125,633	126,946	97,440	(224,386)	125,633
	$ 416,894	$ 193,555	$ 173,415	$ (230,485)	$ 553,379

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

GUARANTOR CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

Three Months Ended June 30, 2004

	IMCO Recycling Inc.	Combined Guarantor Subsidiaries	Combined Non-guarantor Subsidiaries	Eliminations	Consolidated
Revenues	$ 24,067	$ 181,817	$ 98,236	$ (11,681)	$ 292,439
Cost of sales	21,638	170,134	89,932	(11,681)	270,023
Gross profit	2,429	11,683	8,304		22,416
Selling, general and administrative expense	447	11,332	2,938		14,717
Interest expense	6,844	1,572	43	(1,598)	6,861
Other (income) expense, net	(586)	(972)	1	1,598	41
Equity in net loss (earnings) of affiliates	(3,282)	62		3,282	62
Earnings (loss) before provision for income taxes and minority interests	(994)	(311)	5,322	(3,282)	735
Provision (benefit) for income taxes	(1,282)	(165)	1,834		387
Earnings (loss) before minority interests	288	(146)	3,488	(3,282)	348
Minority interests, net of provision for income taxes			60		60
Net earnings (loss)	$ 288	$ (146)	$ 3,428	$ (3,282)	$ 288

IMCO RECYCLING INC. AND SUBSIDIARIES

GUARANTOR CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

Three Months Ended June 30, 2003

	IMCO Recycling Inc.	Combined Guarantor Subsidiaries	Combined Non-guarantor Subsidiaries	Eliminations	Consolidated
Revenues	$ 24,560	$ 137,084	$ 84,652	$ (6,844)	$ 239,452
Cost of sales	22,532	130,728	75,197	(6,844)	221,613
Gross profit	2,028	6,356	9,455		17,839
Selling, general and administrative expense	455	6,376	2,621		9,452

Interest expense	2,212	360	1,741	(609)	3,704
Fees on receivables sale		291			291
Other (income) expense, net	2,067	(2,239)	(482)	609	(45)
Equity in net loss (earnings) of affiliates	(5,110)	14		5,110	14
Earnings (loss) before provision for income taxes and minority interests	2,404	1,554	5,575	(5,110)	4,423
Provision (benefit) for income taxes	(59)		1,906		1,847
Earnings (loss) before minority interests	2,463	1,554	3,669	(5,110)	2,576
Minority interests, net of provision for income taxes			113		113
Net earnings (loss)	$ 2,463	$ 1,554	$ 3,556	$ (5,110)	$ 2,463

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

GUARANTOR CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

Six Months Ended June 30, 2004

	IMCO Recycling Inc.	Combined Guarantor Subsidiaries	Combined Non-guarantor Subsidiaries	Eliminations	Consolidated
Revenues	$ 51,773	$ 349,712	$ 193,111	$ (23,649)	$ 570,947
Cost of sales	46,722	328,387	173,924	(23,649)	525,384
Gross profit	5,051	21,325	19,187		45,563
Selling, general and administrative expense	921	19,200	6,527		26,648
Interest expense	13,180	3,232	339	(3,446)	13,305
Other (income) expense, net	(980)	(1,918)	(335)	3,417	184
Equity in net loss (earnings) of affiliates	(8,417)	45		8,417	45
Earnings (loss) before provision for income taxes and minority interests	347	766	12,656	(8,388)	5,381
Provision (benefit) for income taxes	(2,652)	329	4,618		2,295
Earnings (loss) before minority interests	2,999	437	8,038	(8,388)	3,086
Minority interests, net of provision for income taxes			87		87
Net earnings (loss)	$ 2,999	$ 437	$ 7,951	$ (8,388)	$ 2,999

IMCO RECYCLING INC. AND SUBSIDIARIES

GUARANTOR CONDENSED CONSOLIDATING STATEMENTS OF OPERATIONS

Six Months Ended June 30, 2003

	IMCO Recycling Inc.	Combined Guarantor Subsidiaries	Combined Non-guarantor Subsidiaries	Eliminations	Consolidated
Revenues	$ 49,446	$ 276,939	$ 122,132	$ (13,982)	$ 434,535
Cost of sales	44,844	265,205	108,722	(13,982)	404,789
Gross profit	4,602	11,734	13,410		29,746
Selling, general and administrative expense	921	13,115	3,421		17,457
Interest expense	3,927	602	1,835	(311)	6,053

Fees on receivables sale		581			581
Other (income) expense, net	4,105	(4,516)	122	311	22
Equity in net loss (earnings) of affiliates	(7,932)	(177)	(734)	7,932	(911)
Earnings (loss) before provision for income taxes and minority interests	3,581	2,129	8,766	(7,932)	6,544
Provision (benefit) for income taxes	(205)		2,698		2,493
Earnings (loss) before minority interests	3,786	2,129	6,068	(7,932)	4,051
Minority interests, net of provision for income taxes			265		265
Net earnings (loss)	$ 3,786	$ 2,129	$ 5,803	$ (7,932)	$ 3,786

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

GUARANTOR CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

Six Months Ended June 30, 2004

	IMCO Recycling Inc.	Combined Guarantor Subsidiaries	Combined Non-guarantor Subsidiaries	Eliminations	Consolidated
OPERATING ACTIVITIES:					
Net earnings	$ 2,999	$ 437	$ 7,951	$ (8,388)	$ 2,999
Depreciation and amortization	2,650	8,032	3,515		14,197
Provision for (benefit from) deferred income tax	(2,415)		281		(2,134)
Equity in loss (earnings) of affiliates	(8,417)	45		8,417	45
Non-cash retirement charge		1,576			1,576
Other non-cash items	2,618	1,113	(272)		3,459
Changes in operating assets and liabilities:					
Accounts receivable	1,947	(12,385)	(11,689)		(22,127)
Inventories	2,102	(8,224)	1,111		(5,011)
Other current assets	(56)	1,028	(1,103)		(131)
Accounts payable and accrued liabilities	(8,701)	5,248	8,018		4,565
Net cash from (used by) operating activities	**(7,273)**	**(3,130)**	**7,812**	**29**	**(2,562)**
INVESTING ACTIVITIES:					
Payments for property and equipment	(1,170)	(6,196)	(5,197)		(12,563)
Acquisition costs		(1,889)			(1,889)
Other	(1,935)	278	1,687		30
Net cash from (used by) investing activities	**(3,105)**	**(7,807)**	**(3,510)**		**(14,422)**
FINANCING ACTIVITIES:					
Net proceeds from long-term revolving credit facility	10,295				10,295
Change in restricted cash	(18,918)		24,847		5,929
Payoff of VAW-IMCO promissory note	24,847		(24,847)		
Debt issuance costs	(510)				(510)
Net transfer with subsidiaries	(6,355)	10,696	(4,312)	(29)	
Other	841	153	(372)		622
Net cash from (used by) financing activities	**10,200**	**10,849**	**(4,684)**	**(29)**	**16,336**
Effects of exchange rate changes on cash			(178)		(178)
Net (decrease) in cash and cash equivalents	(178)	(88)	(560)		(826)
Cash and cash equivalents at beginning of period	503	134	14,123		14,760
Cash and cash equivalents at end of period	**$ 325**	**$ 46**	**$ 13,563**	**$**	**$ 13,934**

Table of Contents

IMCO RECYCLING INC. AND SUBSIDIARIES

GUARANTOR CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

Six Months Ended June 30, 2003

	IMCO Recycling Inc.	Combined Guarantor Subsidiaries	Combined Non-guarantor Subsidiaries	Eliminations	Consolidated
OPERATING ACTIVITIES:					
Net earnings	$ 3,786	$ 2,129	$ 5,803	$ (7,932)	$ 3,786
Depreciation and amortization	2,879	7,867	2,545		13,291
Provision for (benefit from) deferred income tax	296		35		331
Equity in loss (earnings) of affiliates	(7,932)	(177)	(734)	7,932	(911)
Other non-cash items	(2,433)	3,715	1,587		2,869
Changes in operating assets and liabilities:					
Accounts receivable	1,034	(5,368)	2,874		(1,460)
Accounts receivable sold	(650)	(4,350)			(5,000)
Inventories	818	(1,573)	(2,982)		(3,737)
Other current assets	262	1,376	671		2,309
Accounts payable and accrued liabilities	(32,554)	11,102	(1,830)	18,055	(5,227)
Net cash from (used by) operating activities	**(34,494)**	**14,721**	**7,969**	**18,055**	**6,251**
INVESTING ACTIVITIES:					
Payments for property and equipment	(496)	(3,312)	(3,915)		(7,723)
Net cash acquired in consolidation of the remaining 50% of VAW-IMCO	750	(750)	15,669		15,669
Other	(977)	1,911	(448)		486
Net cash from (used by) investing activities	**(723)**	**(2,151)**	**11,306**		**8,432**
FINANCING ACTIVITIES:					
Net proceeds from long term-revolving credit facility	4,000				4,000
Net (payments of) proceeds from of long-term debt	2	(155)	(541)		(694)
Debt issuance costs		(757)			(757)
Net transfers with subsidiaries	29,117	(11,906)	844	(18,055)	
Other	(4)	114	(481)		(371)
Net cash from (used by) financing activities	**33,115**	**(12,704)**	**(178)**	**(18,055)**	**2,178**
Effects of exchange rate changes on cash			595		595
Net increase (decrease) in cash and cash equivalents	(2,102)	(134)	19,692		17,456
Cash and cash equivalents at beginning of period	2,418	183	4,274		6,875
Cash and cash equivalents at end of period	**$ 316**	**$ 49**	**$ 23,966**	**$**	**$ 24,331**

NOTE N EMPLOYEE BENEFITS

VAW-IMCO Pension Plan.

VAW-IMCO maintains a defined benefit pension plan for its employees. This plan is based on final pay and service, but some VAW-IMCO senior officers are entitled to receive enhanced pension benefits. The pension plan is classified as a book reserve plan; no plan assets are provided and the employer sets up a book reserve (pension accrual) for payment of the benefits. Under SFAS No. 87, Employers Accounting for Pensions, a book reserve plan under German law is an unfunded plan and a liability item has to be recognized as an unfunded accrued pension cost. This liability is insured by a German pension insurance association under German law if VAW-IMCO is unable to fulfill its obligations. These obligations are included in Other Long-Term Liabilities on our consolidated balance sheet as of June 30, 2004.

Pension cost for the defined pension plan includes the following components of net periodic benefits cost:

	Three Months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
Service cost	$ 121	$ 108	$ 242	$ 144
Interest cost	210	173	420	231
Amortization cost	36		72	
Total	$ 367	$ 281	$ 734	$ 375

Table of Contents

NOTE O MARKET RISK MANAGEMENT USING FINANCIAL INSTRUMENTS

We enter into derivative transactions to hedge the cost of energy and the price of certain aluminum and zinc products. We evaluate and document each hedge item when entered into. It is our policy not to speculate in hedging activities.

We are engaged in activities that expose us to various market risks, including the effects of natural gas prices and future selling prices of aluminum and zinc. These financial exposures are managed as an integral part of our risk management program, which seeks to reduce the potentially adverse effects that market volatility may have on operating results. We do not engage in speculative transactions, nor do we regularly hold or issue financial instruments for trading purposes. We maintain a natural gas pricing strategy to minimize significant fluctuations in earnings caused by the volatility of gas prices. We also maintain a metal pricing strategy to minimize significant, unanticipated fluctuations in earnings caused by the volatility of aluminum and zinc prices.

Domestically, we enter into hedges for aluminum, zinc and natural gas with the expectation that these instruments will be highly effective at achieving offsetting changes in future cash flows. We have this expectation both at the inception of the hedged instrument, and on an ongoing basis. We expect this because the gains and losses of the hedge instruments are based on underlings, such as commodity prices of aluminum, zinc, or natural gas, that are closely correlated to the overall purchase price of materials and energy that are required in our operations. This close correlation is a key factor in the deferral of the gains and losses of our hedges until the respective maturity of the hedges, or until the hedges are closed.

Our deferred gains and losses accumulate on our balance sheet (in Other Comprehensive (Loss) Income) until the maturity of our respective hedging agreements. Due to the sometimes volatile nature of aluminum, zinc and natural gas prices, it would be impractical to estimate the amount we expect to be realized as earnings or loss on our income statement at any given time, or when these gains or losses will be realized.

Actual amounts realized will inevitably differ from our estimates. In addition, our deferred hedging activities reduce, but do not eliminate, the effect of volatile aluminum, zinc and natural gas prices on our operations.

We are exposed to losses in the event of non-performance by the counter-parties to the financial hedge agreements and futures contracts discussed above; however, we do not currently anticipate any non-performance by counter-parties. The counter-parties are evaluated for creditworthiness and risk assessment prior to initiating trading activities with the brokers. We do not require collateral to support broker transactions.

Natural Gas: In order to manage our price exposure for natural gas purchases, we have fixed the future price of a portion of our natural gas requirements by entering into financial hedge agreements. Under these agreements, payments are made or received based on the differential between the monthly closing price on the New York Mercantile Exchange (NYMEX) and the actual hedge price. These contracts are accounted for as cash flow hedges, with all gains and losses recognized in cost of sales when the gas is consumed. In addition, we have cost escalators included in some of our long-term supply contracts with our customers, which limit our exposure to natural gas price risk.

At June 30, 2004, we had outstanding swap agreements to hedge our anticipated domestic natural gas requirements for approximately 2,540,000 Mmbtus of natural gas, which represents approximately 40%, 20% and 5% of our expected 2004, 2005 and 2006 natural gas needs, respectively. At June 30, 2004, the deferred fair value gain of these contracts was $2,694,000 ($1,671,000 net of tax). For the six months ended June 30, 2004

and 2003, natural gas hedging activities decreased cost of goods sold by $1,491,000 and $2,942,000, respectively.

Domestic Aluminum: We enter into futures sale contracts with metal brokers to fix the margin on a portion of the aluminum generated by our salt cake processing facility in Morgantown, Kentucky and some of the aluminum generated for sale from the processing of other scrap metal. These futures sale contracts are settled in the month of shipment. Estimated 2004 total production covered under these futures sale contracts as of June 30, 2004 was 12,335 metric tonnes (mt) with a fair value deferred loss of $699,000 ($433,000 net of tax).

We also enter into forward purchase contracts for aluminum. As of June 30, 2004, we had contracts for 3,260 mt with a fair value deferred gain of $212,000 ($131,000 net of tax). For the six months ended June 30, 2004 and 2003, our domestic aluminum revenue was higher by $773,000 and $145,000, respectively, for settled metal hedging contracts.

Table of Contents

Zinc: In the normal course of business, we enter into fixed-price forward sales and purchase contracts with a number of our zinc customers. At June 30, 2004, estimated total production covered under these futures sale contracts and their respective fair values were as follows:

	Metric Tons	Unrealized deferred gain (loss)	Unrealized deferred gain (loss), net of tax
Forward sales in 2004	(1,875)	$ 212,000	$ 131,000
Forward purchases in 2004	10,617	198,000	123,000
Forward purchases in 2005	3,877	39,000	24,000
Forward purchases in 2006	180	(2,000)	(1,000)
Net notional amounts	12,799	$ 447,000	$ 277,000

For the six months ended June 30, 2004 and 2003, our zinc revenue was higher (lower) by $327,000 and ($325,000), respectively, due to settled zinc metal hedging contracts.

VAW-IMCO: VAW-IMCO has a significant metal hedging program. The majority of VAW-IMCO s operations are product sales, requiring it to take ownership of the materials processed and exposing it to more risk to changes in metal prices. In order to mitigate this risk, VAW-IMCO enters into London Metals Exchange (LME) high-grade and alloy aluminum forward sales and purchase contracts. VAW-IMCO does not hold or issue any derivative financial instruments for trading purposes. The functional currency of VAW-IMCO is the Euro; however, the derivatives utilized in hedging the market risk of changing prices of aluminum purchases and sales at VAW-IMCO facilities are based in U.S. Dollars. This results in foreign currency risk in addition to the risk of changing aluminum prices.

Unlike the derivative contracts utilized throughout the rest of our hedging operations, the unrealized gains and losses on VAW-IMCO s derivative contracts do not qualify for deferred treatment under SFAS 133, Accounting for Derivatives and Hedging Activities. VAW-IMCO s derivative contracts are recorded at fair value with unrealized gains and losses recognized currently in the financial statements.

As of June 30, 2004, VAW-IMCO had forward purchase contracts for high-grade aluminum for 44,225 mt having a fair value loss of U.S. $75,419,000. Also as of June 30, 2004, VAW-IMCO had forward sales contracts for 40,975 mt having a fair value gain of U.S. $71,123,000.

VAW-IMCO recognized in its cost of goods sold unrealized net gains of approximately U.S. $1,465,000 due to metal hedging activities for the six months ended June 30, 2004 and an unrealized net loss of $446,000 for the three months ended June 30, 2004.

None of our other international locations engage in commodity hedging, as their processing activities consist mainly of tolling.

Table of Contents

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

The following is a discussion of our financial condition and results of operation for the periods presented. This discussion should be read in conjunction with the financial statements and notes and other financial information appearing elsewhere in this Form 10-Q, as well as in our Annual Report on Form 10-K for the year ended December 31, 2003. Our discussion of our financial condition and results of operations includes various forward-looking statements about our markets, the demand for our products and services and projected results. These statements are based on certain assumptions that we consider reasonable. For information about these assumptions and other risks relating to our businesses and our company, you should refer to the sub-section of this ITEM 2 entitled RISK FACTORS.

OVERVIEW

IMCO Commonwealth Proposed Merger.

On June 16, 2004, IMCO and Commonwealth announced the execution of a merger agreement for a business combination of the two companies. The merger agreement provides for a stock-for-stock merger in which 0.815 shares of IMCO common stock will be exchanged on a tax-free basis for each share of Commonwealth common stock outstanding. Cash will be paid in lieu of any fractional shares. The merger will be accounted for using the purchase method of accounting for business combinations. The transaction is subject to the approval of the stockholders of IMCO and Commonwealth, the successful completion of refinancing of certain existing indebtedness of the two companies, and certain regulatory approvals. Subject to the successful completion of these events, the transaction is expected to close in the fourth quarter of 2004. More information on the proposed merger transaction is contained in our Registration Statement on Form S-4 filed with the SEC on July 21, 2004.

Operations.

For both the three and six month periods ended June 30, 2004, total segment income increased over that recorded for the corresponding periods in the prior year due to improved economic conditions in the manufacturing sectors that we serve. However, the improvement was offset by higher interest expense and higher selling, general and administrative expense, which included severance costs and costs related to our proposed merger with Commonwealth.

Among our domestic aluminum operations, our margins improved as greater economic activity resulted in higher volumes of metals processed and an increased availability of scrap metals for purchase. Among other positive factors, the amount of scrap that the Chinese have purchased (which drives up the prices we pay for our scrap raw materials) has declined in recent periods. Our international aluminum operations continue to experience strong demand for their products and services, but margins for production in our European operations declined during 2004 s second quarter. Our zinc operations benefited from higher zinc prices due to increased industrial demand.

Negatively impacting our results for the first half of 2004 were continuing high natural gas prices and other fuel costs. In addition, as noted above, selling, general and administrative costs have increased as a result of severance costs for departing executives, the effect of the full six months of consolidated operations of VAW-IMCO in 2004 compared to 2003 and merger-related costs. Our interest expense has also increased significantly as a result of our October 2003 refinancing of substantially all of our indebtedness, higher levels of indebtedness outstanding and the new facilities higher interest rates. Obligations under our former receivables sale facility did not bear interest, although administrative fees

were charged. Despite our improved segment income performance, as a result of a number of these increased costs and expenses, we generated net operating losses from our U.S. operations for federal income tax purposes for the six months ended June 30, 2004.

Our capital expenditures are expected to be $25 million for all of 2004. A significant expansion of our Saginaw, Michigan facility is underway and expected to be completed by the end of this year. We are also expanding our landfill at Morgantown, Kentucky and are planning expansions at our VAW-IMCO facility in Töging, Germany.

Assuming that the industrial economic recovery continues and the relatively high level of automobile sales is maintained, we expect improvements in earnings from operations in 2004 s third quarter compared to the third quarter of 2003. However, high fuel costs, traditional shutdowns of auto manufacturing facilities for model changeovers and greater-than-expected merger-related costs will negatively impact our net earnings for the third quarter of 2004.

For both the three month and six month periods ended June 30, 2004, approximately 58% of our processing volumes consisted of aluminum and zinc tolled for customers. Tolling revenues reflect only processing costs and our profit margin. Our processing activities also involve the processing, recovery and specialty alloying of aluminum and zinc metal and the production of other value-added zinc products for sale. The revenues from these sales transactions reflect the cost of the metal, as well as the processing cost and our profit margin. Accordingly, our tolling business produces lower revenues and costs of sales than our product sales business.

Table of Contents

Variations in the mix between these two types of transactions can cause revenue amounts to change significantly from period to period. As a result, we have traditionally considered processing volume to be a more important determinant of performance than revenues, particularly in the domestic aluminum segment.

The following table shows total pounds processed, the percentage of total pounds processed represented by tolled metals, total revenues and total gross profits (in thousands, except percentages):

	Three months ended June 30,		Six months ended June 30,	
	2004	2003	2004	2003
Pounds processed	840,059	768,181	1,669,923	1,431,427
Percentage of pounds tolled	58%	53%	58%	54%
Revenues	$ 292,439	$ 239,452	$ 570,947	$ 434,535
Gross profit	$ 22,416	$ 17,839	$ 45,563	$ 29,746

CRITICAL ACCOUNTING POLICIES

The preparation of our financial statements in accordance with generally accepted accounting principles requires management to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities and the reported amounts of revenues and expenses. Areas of uncertainty that require judgments, estimates and assumptions include accounting for inventories, long-lived assets, derivatives, property and equipment, goodwill and other intangible assets, credit risk and income taxes. Management uses historical experience and certain other information available in order to make these judgments and estimates; actual results will inevitably differ from those estimates and assumptions that are used to prepare our financial statements at any given time.

A summary of our significant accounting policies and estimates is included in ITEM 7. Management s Discussion and Analysis of Financial Condition and Results of Operations of our Annual Report on Form 10-K for the year ended December 31, 2003. There has been no significant change to our critical accounting policies during the six months ended June 30, 2004.

RESULTS OF OPERATIONS

THREE MONTHS ENDED JUNE 30, 2004 COMPARED TO THREE MONTHS ENDED JUNE 30, 2003, AND SIX MONTHS ENDED JUNE 30, 2004 COMPARED TO SIX MONTHS ENDED JUNE 30, 2003.

PRODUCTION. The following table shows the increases in total pounds processed and the percentage tolled for the domestic aluminum, international aluminum and zinc segments (in thousands, except percentages):

	Three months ended June 30,			Six months ended June 30,		
	2004	2003	% increase	2004	2003	% increase
Pounds Processed:						
Domestic Aluminum	517,844	487,109	6%	1,036,421	974,867	6%
International Aluminum	259,333	219,174	18%	514,427	340,366	51%
Zinc	62,882	61,898	2%	119,075	116,194	2%
Total Pounds Processed	840,059	768,181	9%	1,669,923	1,431,427	17%
Percentage Tolled:						
Domestic Aluminum	67%	61%		66%	61%	
International Aluminum	54%	51%		55%	54%	
Zinc	0%	3%		1%	3%	
Total Percentage Tolled	58%	53%		58%	54%	

DOMESTIC ALUMINUM PRODUCTION: For the three and six month periods ended June 30, 2004, overall production increased compared to the same period in the prior year. Within this segment, production increased in both our aluminum recycling division and specialty alloy division. Our domestic aluminum tolling percentage increased due to a general improvement in the U.S. industrial economy for both the three and six month periods ended June 30, 2004 compared to the same periods in the prior year.

As the second quarter of 2004 ended, growth was reported in several sectors of the U.S industrial economy. However, the continuing shutdown of primary smelter capacity in the Pacific Northwest continues to adversely affect our domestic aluminum operations.

Table of Contents

Operations at our Rockwood, Tennessee facility remain provisionally suspended. We may restart operations at this facility if market conditions warrant doing so. Materials that normally would have been processed at Rockwood have been sent to our other locations for processing.

Within the aluminum recycling division, deox processing increased for both the three and six month periods ended June 30, 2004 compared to the same periods in 2003 due to increased demand from the steel industry.

Due to an increase in manufacturing and economic conditions in the specialty alloy division resulting in an increased supply of scrap metal, we have been able to process more materials than last year at this time. A significant expansion is underway at our Saginaw, Michigan facility to supply more specialty alloy materials under our long-term agreement with General Motors. This project is expected to be completed by the end of this year.

INTERNATIONAL ALUMINUM PRODUCTION: Production at our international aluminum facilities also increased. On a pro forma basis, assuming the consolidation of VAW-IMCO had occurred on January 1, 2003, production in this segment increased by 13%. Production at VAW-IMCO improved due to the installation of new IMCO-designed furnaces in 2003. Production also improved at our Monterrey, Mexico facility due to higher volumes from the addition of new customers. Tolling volume for this facility continues to be up sharply compared to the same period in 2003 due to the addition of new customers.

ZINC PRODUCTION: Zinc production increased modestly during the three and six months ended June 30, 2004 compared to the same period in the prior year. Most of the production gains occurred as a result of an increase in demand due to the improving economy.

REVENUES. The following table shows the increases in total revenue for our three operating segments for the three and six months ended June 30, 2004 compared to the same periods in the prior year, and the percentage change from the prior period (in thousands, except percentages):

	Three months ended June 30,			Six months ended June 30,		
	2004	2003	% increase	2004	2003	% increase
Revenues:						
Domestic Aluminum	$ 143,931	$ 121,857	18%	$ 281,610	$ 248,974	13%
International Aluminum	92,594	80,558	15%	183,267	113,822	61%
Zinc	55,914	37,037	51%	106,070	71,739	48%
Total Revenues	$ 292,439	$ 239,452	22%	$ 570,947	$ 434,535	31%

Our total consolidated revenues increased 22% during the three months ended June 30, 2004 compared to the same period in the prior year. Our total consolidated revenues increased 31% during the six months ended June 30, 2004 compared to the same period in the prior year. This increase is more than the percentage increase in our metal processed, due mostly to higher metal selling prices.

DOMESTIC ALUMINUM REVENUES: For the three month period ended June 30, 2004 compared to the same period in the prior year, our domestic aluminum revenues increased. This reflected stronger volumes processed at our aluminum recycling facilities and increases in our deox processing. The operating rates of our domestic aluminum recycling plants have increased due to the recovery in U.S. industrial activity and a stronger overall aluminum market. The average London Metal Exchange (LME) price of primary aluminum during the first six months of 2004 increased by approximately 22% compared to the average price during the same period in 2003.

Within this segment, for both the current quarter and the six months ended June 30, 2004, tolling revenues are running ahead of last year s amounts due to higher tolling volumes. Product sales revenues have also increased for the same time periods; however, most of this increase has been due to an increase in prices. Product sales volume was relatively unchanged for both the three and six month periods ended June 30, 2004, compared to the same time periods in the prior year.

INTERNATIONAL ALUMINUM REVENUES: Our international aluminum revenues have increased strongly since 2003, reflecting our foreign acquisitions and increased volumes. Most of this growth is due to our consolidation of VAW-IMCO, and, to a lesser degree, reflects our increased operations in Mexico. With the consolidation of VAW-IMCO, the majority of our revenues in this segment represent product sales as opposed to tolling fees. VAW-IMCO s revenues are closely tied to the European auto industry; approximately 60% of its annual output is provided to that industry. Revenue increased at our Monterrey, Mexico facility mostly due to the addition of new customers and higher processing volumes. Revenues also increased at our Swansea, UK facility in part due to new deox processing.

On a pro forma basis, assuming the consolidation of VAW-IMCO had occurred on January 1, 2003, revenues are relatively unchanged for the six months ending June 30, 2004 compared to the same time period in 2003.

Table of Contents

ZINC REVENUES: Zinc revenues increased in the second quarter of 2004 compared to the same period in 2003. Principally driving zinc revenues has been the increase in the average LME zinc price, which during the second quarter of 2004 increased by approximately 34% compared to the average price during the corresponding period in 2003.

GROSS PROFIT. The following table shows total segment income, the percentage change from the prior period and a reconciliation of segment income to our consolidated gross profit (in thousands, except percentages):

	Three months ended June 30,			Six months ended June 30,		
	2004	2003	% change	2004	2003	% change
Segment Income:						
Domestic Aluminum	$ 9,267	$ 5,363	73%	$ 15,887	$ 11,176	42%
International Aluminum	4,986	6,316	-21%	11,943	9,225	29%
Zinc	2,884	1,404	105%	6,777	2,510	170%
Total segment income	$ 17,137	$ 13,083	31%	$ 34,607	$ 22,911	51%
Items not included in gross profit:						
Plant selling expense	$ 1,300	$ 1,240	5%	$ 2,563	$ 2,420	6%
Management SG&A expense	3,883	3,415	14%	8,192	5,097	61%
Equity in earnings of affiliates	62	14	343%	45	(911)	
Other income	34	87	-61%	156	229	-32%
Gross Profit	$ 22,416	$ 17,839	26%	$ 45,563	$ 29,746	53%

DOMESTIC ALUMINUM INCOME: Domestic aluminum income increased for the three and six month periods ended June 30, 2004 compared to the same periods in the prior year due to higher volumes and selling prices. Within this segment, total margins increased, due mostly to higher amounts of material processed. Total product sales margins have improved as well, reflecting both favorable selling and scrap metal prices.

Natural gas prices, after including the effects of our hedging activities, are higher than last year s natural gas prices. On a per unit basis, overall natural gas prices are approximately 11% higher for the six months ended June 30, 2004 compared to the same period in the prior year.

Overall, excluding fuels, operating costs were relatively unchanged in this segment, both for the three and six month periods ended June 30, 2004 compared to the same periods in the prior year. Excluding fuels, operating costs on a per unit processed basis are slightly lower this year than in the same time periods last year due to more units processed this year.

INTERNATIONAL ALUMINUM INCOME: For the six months ended June 30, 2004, compared to the same time period in 2003, income in this segment increased mostly due to the consolidation of VAW-IMCO as discussed above. Metal hedging activities also affected VAW-IMCO s income; overall unrealized metal hedging gains, included in income, were $1,465,000, net.

For the three months ended June 30, 2004, compared to the same time period in 2003, income in this segment decreased mostly due to weaker margins and an unrealized hedging loss of $446,000. Higher production at VAW-IMCO, in total, has offset some of the sales margin weakness.

In contrast to VAW-IMCO, we realized improvements in income from our Monterrey, Mexico facility and our Pindamonhangaba, Brazil facility. Income at these locations increased sharply for both the three and six month periods ended June 30, 2004 compared to the same periods in the prior year due to higher volumes and prices.

ZINC INCOME: Zinc income increased for both the three and six months ended June 30, 2004 compared to the same periods in the prior year, which increase is primarily related to higher LME zinc prices. Expenses for freight and energy costs are slightly higher for the six month period ended June 30, 2004 compared to the same period in 2003.

SG&A EXPENSE. During the three months ended June 30, 2004, our SG&A expenses were $14,717,000, which was $5,265,000 higher than the $9,452,000 in the same period in 2003. During the six months ended June 30, 2004, our SG&A expenses were $26,648,000, which was $9,191,000 higher than the $17,457,000 in the same period in 2003.

Table of Contents

The increases in SG&A are due in part to the inclusion of VAW-IMCO s SG&A for the full six months ended June 30, 2004 into our results of operations for that period (which resulted from our consolidation of VAW-IMCO s results of operation into our consolidated financial statements as of March 1, 2003), certain merger expenses, and expenses amounting to $3,665,000 related to the departure of Don V. Ingram, our former chairman of the board, president and chief executive officer. These expenses included:

a cash severance payment of $1,500,000.

expenses from the vesting of Mr. Ingram s restricted stock awards.

certain legal expenses associated with his departure.

INTEREST EXPENSE. During the three months ended June 30, 2004, our interest expense was $6,861,000, which was $3,157,000 higher than the $3,704,000 in the same period in 2003. During the six months ended June 30, 2004, our interest expense was $13,305,000, which was $7,252,000 higher than $6,053,000 in the same period in 2003. Most of our outstanding debt is now related to our senior secured notes, which bear an effective fixed interest rate of 10.5%, compared to the first six months of 2003 when our former senior credit facility bore an effective annual interest rate of 7.9%. As a result of our October 2003 debt refinancing our former receivables sale facility was extinguished and we longer incur fees on receivables sales. As a result of the termination of the receivables sale facility, our average borrowings have increased.

PROVISION FOR INCOME TAXES. During the three months ended June 30, 2004, our provision for income taxes was $387,000, which was $1,460,000 below the $1,847,000 amount from the same period in the prior year. During the six months ended June 30, 2004, our provision for income taxes was $2,295,000, which was $198,000 below the $2,493,000 amount from the same period in the prior year. These reductions resulted from lower consolidated earnings. Our effective tax rate was 43% for the six months ended June 30, 2004. This compares to an effective tax rate of 38% for the comparable period in 2003. Our provision for income tax in 2003 excluded the equity income from VAW-IMCO, which was recorded on an after tax basis.

The consolidation of VAW-IMCO s results of operations into our financial statements beginning in March 2003 resulted in a higher overall effective tax on our international income due to German income taxes imposed on VAW-IMCO. This consolidation has had the impact of increasing our international earnings. Offsetting this, higher interest expense and payments for departing executives generated net operating losses for U.S. federal income tax purposes. Deferred tax benefits related to these net operating losses have been recorded. While our effective tax rate for 2004 contemplates the utilization of such operating loss carryforwards, if expected profit improvements in our domestic operations do not occur, recording of additional U.S. tax benefits for 2004 will need to be re-evaluated.

We have recorded net deferred tax assets in various state jurisdictions totaling $5,664,000, which includes amounts recorded related to the benefit for loss carryforwards and tax credits, and which expire in varying amounts between 2005 and 2024. A valuation allowance of $2,345,000 has been provided related to such net deferred tax assets. Realization is dependent on generating sufficient taxable income prior to expiration of the loss carryforwards. Although realization is not assured, management believes it is more likely than not that all of the deferred tax asset will be realized. The amount of the deferred tax asset considered realizable, however, could be reduced in the near term if estimates of future taxable income during the carryforward period are reduced.

Finally, our deferred tax asset and liability positions for both U.S. federal and various state jurisdictions will be taken into consideration in accounting for the proposed acquisition of Commonwealth (see NOTE B IMCO RECYCLING INC. AND COMMONWEALTH INDUSTRIES, INC. PROPOSED MERGER) and the amount of deferred tax positions recorded in conjunction with the purchase price allocation could be impacted.

NET EARNINGS. For the three months ended June 30, 2004, our net earnings were $288,000, which is $2,175,000 below the $2,463,000 from the same period in the prior year. For the six months ended June 30, 2004, our net earnings were $2,999,000, which is $787,000 below the $3,786,000 amount from the same period in the prior year. Overall, improved gross profits were offset by increased SG&A expenses and interest expense as discussed above.

LIQUIDITY AND CAPITAL RESOURCES

We have historically financed our operations and capital expenditures from internally generated cash and available credit facilities. We have traditionally financed our acquisitions and capacity expansions from a combination of funds from long-term borrowings and stock issuances. We believe that our cash on hand and our anticipated internally generated funds will be sufficient to fund our operational needs for at least the next twelve months.

Cash Flows from Operations. Operations used $2,562,000 of cash for the six months ended June 30, 2004, compared to providing $6,251,000 of cash for the same six months in 2003. Decreases in cash flow from operations included the effect of increasing investments in operating assets and liabilities, which totaled $22,704,000 for the six months ended June 30, 2004 compared to $13,115,000 for the same period in 2003. The majority of our change in operating assets and liabilities was due to changes in accounts receivable.

Table of Contents

For the six months ended June 30, 2004, increases in accounts receivable of $22,127,000 were due to an increase in our overall processing volume and an increase in overall metal prices. An indicator of our collections on receivables activity, and a key internal performance indicator, is our days sales outstanding statistic. We have reduced the number of average days sales outstanding since December 31, 2003, effectively strengthening our cash receipts from customers:

	June 30, 2004	December 31, 2003
Days sales outstanding	41	46

For the six months ended June 30, 2004, inventories increased $5,011,000. The majority of our increase in inventories occurred in our domestic operations due to higher metal prices and the availability of suitably-priced raw materials.

For the six months ended June 30, 2004, accounts payable and accrued liabilities increased $4,565,000. Increases in our accounts payable and accrued liabilities were mostly concentrated on our operations in Germany. This was partially offset by lower accounts payable and accrued liabilities from our domestic operations. On April 15, 2004, we paid $11,438,000 as our first interest payment under the senior secured notes we issued in October 2003. The payment of this interest obligation reduced our accrued liabilities.

Also affecting our cash used by operations was the $1,500,000 cash severance payment to our former chairman and chief executive officer, as mentioned above.

Cash Flows from Investing Activities. Cash flows from investing activities primarily reflect our capital expenditure activities. Our capital expenditures principally relate to property, plant and equipment. During the six months ended June 30, 2004, cash used by investing activities was $14,422,000. During the same time period in 2003, cash provided by investing activities was $8,432,000, due to the increase in cash resulting from the consolidation of VAW-IMCO.

Cash used for capital expenditures was $12,563,000 for the six months ended June 30, 2004, compared to a use of cash of $7,723,000 for capital expenditures during the same time period in 2003. Our overall capital expenditures for property, plant and equipment in the U.S. and at our international locations for the remainder of this year are expected to approximate $12,400,000. The majority of this sum is planned to be used for expansion of our Saginaw, Michigan facility and our Morgantown, Kentucky landfill and other maintenance capital items. These capital expenditures are expected to be funded by cash flows generated from continuing operations and from the utilization of restricted cash.

Cash Flows from Financing Activities. Cash flows from financing activities generally reflect changes in our borrowings and debt obligations. Net cash from our financing activities was $16,336,000 for the six months ended June 30, 2004, compared to $2,178,000 of cash provided by financing activities for the same time period in 2003.

During the six months ended June 30, 2004, $10,295,000 was borrowed under our senior credit facility. During the same time period in the prior year, proceeds from borrowings on our former revolving credit facility were $4,000,000.

As of June 30, 2004, we estimated that our borrowing base would have supported additional borrowings of $38,801,000 after giving effect to outstanding borrowings of $43,286,000 and outstanding letters of credit of $6,805,000. As of June 30, 2004, our total borrowing base was estimated to be approximately $88,892,000. VAW-IMCO also had unused lines of credit totaling approximately $18,294,000.

At June 30, 2004 we had $18,917,000 in restricted cash in a collateral account held by the trustee under the indenture for the benefit of holders of the senior secured notes. As permitted under the senior secured notes indenture, and subject to certain limitations, we will be able to use these funds in the collateral account for certain property and equipment expenditures until January 2005. The property and equipment that are the subject of these expenditures will also become collateral security for the senior secured notes. We currently intend to use the majority of the funds from the collateral account for these purposes in 2004. To the extent that more than $5,000,000 in unused funds remain in the collateral account after January 2005, we are required to make an offer to repurchase outstanding senior unsecured notes up to the extent of the amount of the unused funds. If the amount of notes tendered to us in response to this offer is less than the amount of the unused funds, then we may use the excess funds for our general corporate purposes, free of liens under the indenture, but subject to certain other terms and conditions. During the first six months of 2004, we used $5,929,000 of funds in the collateral account for capital expenditures.

As of June 30, 2004, we capitalized $1,889,000 of expenses incurred in connection with our proposed merger with Commonwealth.

EBITDA. We report our financial results in accordance with generally accepted accounting principles (GAAP). However, our management believes that certain non-GAAP performance measures, which our management uses in managing the business, may provide investors with additional meaningful comparisons between current results and results in prior periods.

Table of Contents

EBITDA is defined as net earnings (loss) before cumulative effect of accounting change, income tax expense, interest (income) expense, depreciation and amortization. EBITDA is a non-GAAP financial measure which is presented because we consider it an important supplemental measure of our performance and believe it is frequently used by securities analysts, investors and other interested parties in the evaluation of companies in our industry, many of which present EBITDA when reporting their results.

We also use EBITDA because our senior credit facility and our senior secured notes indenture use EBITDA with additional adjustments to measure our compliance with covenants such as interest coverage, leverage ratio and debt incurrence. EBITDA has limitations as an analytical tool, and you should not consider it in isolation or as a substitute for analysis of our financial results prepared in accordance with GAAP. Some of these limitations are:

- EBITDA does not reflect our cash expenditures, or future requirements, for capital expenditures or contractual commitments;
- EBITDA does not reflect changes in, or cash requirements for, our working capital needs;
- EBITDA does not reflect the significant interest expense or cash requirements necessary to service interest or principal payments on indebtedness;
- although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and EBITDA does not reflect any cash requirements for such replacements; and
- other companies in our industry may calculate EBITDA differently than we do, limiting its usefulness as a comparative measure.

Because of these limitations, EBITDA should not be considered as a measure of discretionary cash available to us to invest in the growth of our business. We compensate for these limitations by relying primarily on our GAAP results and using EBITDA only on a supplemental basis.

Our reconciliation of EBITDA to net earnings and net cash from (used by) operating activities is as follows (amounts in thousands):

	For the three months ended June 30,		For the six months ended June 30,	
	2004	2003	2004	2003
EBITDA	$ 14,618	$ 15,000	$ 32,796	$ 25,623
Interest expense	6,861	3,704	13,305	6,053
Income taxes	387	1,847	2,295	2,493
Depreciation and amortization	7,082	6,986	14,197	13,291
Net income	$ 288	$ 2,463	$ 2,999	$ 3,786
Depreciation and amortization	7,082	6,986	14,197	13,291
Deferred income taxes	(2,809)	(85)	(2,134)	331
Equity in net loss (earnings) of affiliates	62	14	45	(911)

Non-cash charges	3,745	1,874	5,035	2,869
Net change in working capital:				
Accounts receivable	3,879	9,513	(22,127)	(1,460)
Accounts receivable sold		(600)		(5,000)
Inventories	(7,843)	(4,818)	(5,011)	(3,737)
Other current assets	1,336	1,696	(131)	2,309
Accounts payable & accrued liabilities	(10,467)	(2,027)	4,565	(5,227)
Total net change in working capital	$ (13,095)	$ 3,764	$ (22,704)	$ (13,115)
Cash from (used by) operating activities	$ (4,727)	$ 15,016	$ (2,562)	$ 6,251

FOREIGN EXCHANGE RATES. We translate the balance sheets of our foreign subsidiaries using fiscal period-end exchange rates. The consolidated statements of earnings are translated using the average exchange rates for the period. The cumulative effect of such translations is included in shareholders equity, other than for current intercompany accounts, as a component of other comprehensive earnings (loss). Foreign currency translation adjustments, unrealized gains or losses, accumulate in equity until the final disposition of their respective operations.

During the six months ended June 30, 2004, the U.S. Dollar gained approximately 3% in value against the Euro, resulting in an unrealized foreign currency translation loss of approximately $1,387,000. Also during this same period, the U.S. Dollar gained approximately 2% in value against the Mexican Peso, resulting in an unrealized foreign currency translation loss of approximately $437,000. Partially offsetting this unrealized loss were unrealized foreign currency translation gains in the British Pound. During this

Table of Contents

same time period, the British Pound gained approximately 2% against the U.S. Dollar. The Euro is the functional currency of our German facilities, and the British Pound is the functional currency of our Wales facility. The Peso is the functional currency of our Monterrey, Mexico facility.

We also operate a facility in Pindamonhangaba, Brazil, and the Brazilian Real is the functional currency of this facility. During the six months ended June 30, 2004, the U.S. Dollar gained approximately 6% in value against the Real, resulting in a small unrealized foreign currency translation loss.

CREDIT FACILITIES. Our long-term debt is summarized as follows (in thousands):

	June 30, 2004	December 31, 2003
Senior Credit Facility, expiring in October 2007	$ 43,286	$ 32,991
10 3/8% Senior Secured Notes, due October 6, 2010 (net of discount)	208,802	208,751
7.65% Morgantown, Kentucky Solid Waste Disposal Facilities Revenue Bonds-1996 Series, Due May 1, 2016 (net of discount)	5,706	5,705
7.45% Morgantown, Kentucky Solid Waste Disposal Facilities Revenue Bonds-1997 Series, Due May 1, 2022	4,600	4,600
6.00% Morgantown, Kentucky Solid Waste Disposal Facilities Revenue Bonds-1998 Series, Due May 1, 2023	4,100	4,100
Other	52	46
Subtotal	266,546	256,193
Less current maturities	43,316	33,017
Total	$ 223,230	$ 223,176

As of June 30, 2004, we had $43,286,000 of indebtedness outstanding under our senior credit facility. Under this facility, we are subject to a borrowing base limitation based on eligible domestic inventory and receivables. As of June 30, 2004, we estimated that our borrowing base would have supported additional borrowings of $38,801,000 after giving effect to outstanding borrowings of $43,286,000 and outstanding letters of credit of $6,805,000. As of June 30, 2004, our total borrowing base was estimated to be approximately $88,892,000.

The terms of our new senior credit facility include, among other covenants, (i) prohibitions against incurring certain indebtedness, (ii) limitations on dividends and repurchases of shares of capital stock, and (iii) limitations on capital expenditures, investments and acquisitions. . We are subject to the terms of a lockbox arrangement with the administrative agent bank under the senior credit facility, whereby funds deposited from collections of receivables are applied by the lenders to reduce outstanding balances of the borrowings under the senior credit facility. At any time during specified periods (including currently) our undrawn availability under this facility is less than $50,000,000, we will also be required to maintain a minimum fixed coverage ratio and minimum tangible net worth, as follows:

A minimum fixed charge coverage ratio of 1.0 to 1.0 (calculated based on our parent entity and wholly-owned domestic subsidiaries), and

A minimum tangible net worth of $44,500,000 plus 50% of future net income on a consolidated basis.

As of June 30, 2004, we were in compliance with all applicable debt covenants. In the event that we were not in compliance with this covenant, we would not be able to borrow under the revolving credit facility.

On July 16, 2004, IMCO and its co-borrower subsidiaries entered into a Second Amendment to Revolving Credit and Security Agreement. This amendment modified a section of the senior credit facility that had provided that any change in the condition or affairs of IMCO or its co-borrowers which, in the lenders agent s reasonable opinion, has a material adverse effect (as defined in the senior credit facility), would be deemed an event of default under the senior credit facility. The Second Amendment to Revolving Credit and Security Agreement revised this provision so that it now provides that such an event of default would not be applicable and that the agent and the lenders would have no rights under the provision, so long as IMCO was in compliance with certain undrawn availability tests under the senior credit facility. If the level of undrawn availability falls below $3,000,000 for three consecutive business days or below an average of $10,000,000 per day for any calendar month, then the lenders rights under this provision would be reinstated.

In addition, VAW-IMCO has two lines of credit available for its working capital needs. The total amount of credit available under these facilities is 15,000,000 Euros ($18,294,000 U.S. Dollars). During the second quarter of 2004, the terms of these credit facilities were renewed and extended, and these facilities now are scheduled to expire in April and May of 2006. As of June 30, 2004, no amounts were outstanding under these lines of credit.

Table of Contents

CONTRACTUAL OBLIGATIONS

We are obligated to make future payments under various contracts such as debt agreements, lease agreements and unconditional purchase obligations. The following table represents certain of our significant contractual cash obligations and other commercial commitments as of June 30, 2004:

	Cash payments due by period				
	Total	Less than 1 year	2-3 years	4-5 years	After 5 years
Long-term debt obligations (does not include interest)	$ 266,546	$ 43,316	$ 22	$	$ 223,208
Operating lease obligations	8,924	3,204	4,486	1,234	
Purchase obligations	350,461	200,130	147,449	2,882	
Other long-term liabilities reflected on our balance sheet	20,998		786		20,212
Total	$ 646,929	$ 246,650	$ 152,743	$ 4,116	$ 243,420

Our noncancellable purchase obligations are principally for materials, such as metals and salt fluxes. These materials are used in our manufacturing operations. Other long-term liabilities mostly reflect liabilities for our landfills and VAW-IMCO pension obligations.

RISK FACTORS

The occurrence of any of the events described in the risk factors below could materially and adversely affect our financial condition and results of operations.

Risks of the Company

IF WE FAIL TO IMPLEMENT OUR BUSINESS STRATEGY, OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS COULD BE MATERIALLY AND ADVERSELY AFFECTED.

Our future financial performance and success are dependent in large part upon our ability to successfully implement our business strategy. We cannot assure you that we will be able to successfully implement our business strategy or be able to improve our operating results. In particular, we cannot assure you that we will be able to increase capacity utilization of our aluminum and zinc recycling plants, continue to pursue a disciplined growth strategy, leverage existing customer relationships to drive international expansion, capitalize on the increasing use of aluminum in the transportation market, increase productivity and reduce costs, minimize commodity price risks and maintain environmental efficiencies.

Furthermore, we cannot assure you that we will be successful in our growth efforts or that we will be able to effectively manage expanded or acquired operations. Our ability to achieve our expansion and acquisition objectives and to effectively manage our growth depends on a number of factors, including:

- our ability to identify appropriate acquisition targets and to negotiate acceptable terms for their acquisition;
- our ability to integrate new businesses into our operations; and
- the availability of capital on acceptable terms.

We are regularly in the process of evaluating and may, from time to time in the future, evaluate the acquisition of assets or operations that complement our existing businesses. We cannot estimate what impact, if any, our acquisition of these assets or operations may have on our business or our business strategy.

Our business strategy may require additional funding which may be provided in the form of additional debt, equity financing or a combination thereof. We cannot assure you that we will be permitted under the terms of our new senior credit facility or the notes to obtain such financing.

Implementation of our business strategy could be affected by a number of factors beyond our control, such as increased competition, legal developments, general economic conditions or increased operating costs. Any failure to successfully implement our business strategy could materially and adversely affect our financial condition and results of operations. We may, in addition, decide to alter or discontinue certain aspects of our business strategy at any time.

Table of Contents

Our business strategy will likely change materially following our proposed merger with Commonwealth assuming it is completed. See Certain Risks of the Proposed Merger below.

ASSETS AND OPERATIONS THAT WE ACQUIRE MAY BE DIFFICULT TO INTEGRATE, DISRUPT OUR BUSINESS AND DIVERT MANAGEMENT ATTENTION.

A key component of our current business strategy is to selectively seek assets and operations that complement our existing businesses. There can be no assurance that we will be successful in locating or entering into any strategic alliances or acquisitions, or that any completed transaction will achieve the expected benefits. In addition, any such transaction may result in unexpected costs, expenses and liabilities.

Our ability to achieve our expansion and acquisition objectives will also depend on the availability of capital on acceptable terms. The combined businesses resulting from any acquisition may not be able to generate sufficient operating cash flows in order for us to obtain additional financing or fund our business and expansion strategy.

Acquisitions expose us to:

- increased costs associated with the acquisition and operation of the new businesses and the management of geographically dispersed operations;
- risks associated with the assimilation of new technologies, operations, sites and personnel;
- the possible loss of key employees;
- risks that any operations or technology we acquire may not perform as well as we had anticipated;
- the diversion of management s attention and other resources from existing business concerns;
- the potential inability to replicate operating efficiencies in the acquired company s operations;
- the potential inability to generate sufficient revenues to offset associated acquisition costs;
- the increased need to maintain uniform standards, controls, and procedures; and
- the potential impairment of relationships with employees and customers as a result of integration of new personnel.

The identification of suitable acquisition candidates can be difficult, time-consuming and costly, and we may not be able to successfully complete identified potential acquisitions. Integration of acquired businesses require significant efforts from each entity, including coordinating

existing business plans and operational procedures. If we are unable to successfully integrate the operations of acquired businesses, our future results will be negatively impacted.

Acquisitions may also result in the issuance of dilutive equity securities, the incurrence or assumption of additional debt and additional expenses associated with the amortization of acquired intangible assets or potential businesses. There is no assurance that any future acquisitions will generate additional income or cash flows, or provide any benefit to our existing or future businesses.

WE MAY ENCOUNTER INCREASES IN THE COST OF RAW MATERIALS AND ENERGY, WHICH COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

We require substantial amounts of raw materials and energy in our business, consisting principally of aluminum scrap, primary aluminum metal and natural gas. Any substantial increases in their costs could adversely affect our financial condition and results of operations.

Aluminum scrap and primary aluminum metal prices are subject to significant cyclical price fluctuations. London Metals Exchange (the LME) primary aluminum metal prices declined by 56% between 1988 and 2002 and rose 30% from 2002 to 2004. Metallics (aluminum and zinc scrap, primary aluminum metal and aluminum dross) represent the largest component of our cost of sales. We purchase scrap primarily from aluminum and zinc scrap dealers. Remaining requirements are met with purchased primary metals. There is no assurance that these supply sources will continue to be available.

The availability and price of scrap 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. We often cannot adjust the selling prices for our products to recover the increases in scrap prices. If scrap and dross prices were to increase significantly without a commensurate increase in the market value of the primary metals, our financial condition and results of operations would be adversely affected.

Table of Contents

Natural gas costs represent the third largest component of our cost of sales (after labor costs). The price of natural gas can be particularly volatile. We hedge according to board policy and purchase the majority of our natural gas on a spot-market basis. As a result, our natural gas costs may fluctuate dramatically, and we may not be able to mitigate the effect of higher natural gas costs on our cost of sales. If natural gas prices remain at current levels or increase further, our financial condition and results of operations may be adversely affected.

Increased energy prices may also adversely affect our customers, which in turn affects demand for our services. For example, since 2001 we have experienced a sharp reduction in demand for our recycling services in the Pacific Northwest, because many domestic smelters located in that region have been forced to suspend or terminate their operations due to high energy costs.

OUR BUSINESS REQUIRES SUBSTANTIAL CAPITAL INVESTMENTS, MAINTENANCE EXPENDITURES AND CONTRACTUAL COMMITMENTS THAT WE MAY BE UNABLE TO FULFILL.

Our operations are capital intensive. Our total capital expenditures were $20,807,000 and $19,313,000 for 2003 and 2002, respectively. We expect to spend approximately $25,000,000 on capital expenditures during 2004. Our business also requires substantial expenditures for routine maintenance and non-capital environmental expenditures. For the six months ended June 30, 2004, we spent $12,563,000 in capital expenditures, compared to $7,723,000 during the same time period in 2003. As of June 30, 2004, in addition to debt obligations, we had contractual obligations of approximately $380,383,000 payable over time.

Our business may not generate sufficient operating cash flow and our external financing sources may not be available in an amount sufficient to enable us to make anticipated capital expenditures, service or refinance our indebtedness or fund other liquidity needs. If we are unable to make upgrades or purchase new plant and equipment, our financial condition and results of operations could be materially and adversely affected.

PRIMARY METALS PRICES COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

We purchase aluminum and zinc scrap and dross from our customers and on the open market for processing as part of our product sales business. We then sell recycled aluminum and zinc products to our customers based on a price which generally fluctuates with the market price of the primary metal. Accordingly, changes in the market price of primary aluminum and zinc impact the selling prices of our products. In particular, depressed prices adversely affect our business, particularly our zinc business, given our relatively high fixed costs and market differences between the price of scrap and the selling price of our products.

The market prices of aluminum and zinc are dependent upon supply and demand and a variety of factors over which we have little or no control, including:

- U.S. and world economic conditions;
- availability and relative pricing of metal substitutes;

labor costs;

energy prices;

environmental and conservation regulations;

seasonal factors and weather;

import and export restrictions; and

other factors.

In recent years, aluminum and zinc prices have remained depressed longer than expected relative to historical levels, which has adversely affected our results of operations.

Table of Contents

A GROWING PORTION OF OUR SALES HAS BEEN DERIVED FROM OUR INTERNATIONAL OPERATIONS, WHICH EXPOSES US TO CERTAIN RISKS INHERENT IN DOING BUSINESS ABROAD.

We currently have operations in countries outside the United States and in certain emerging markets, including Mexico and Brazil, and we plan to continue to expand our international operations. Our foreign operations are generally subject to risks, including:

- changes in U.S. and foreign governmental regulations, trade restrictions and laws, including tax laws and regulations;
- foreign currency exchange rate fluctuations;
- 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.

The occurrence of any of these events could have a material adverse effect on our financial condition and results of operations.

The financial condition and results of operations of some of our operating entities are reported in foreign currencies and then translated into U.S. Dollars at the applicable exchange rate for inclusion in our consolidated financial statements. As a result, generally speaking, appreciation of the U.S. Dollar against these foreign currencies will have a negative impact on our reported revenues and operating profit while depreciation of the U.S. Dollar against these foreign currencies will have a positive effect on reported revenues and operating profit. For example, our German and Brazilian operations were positively impacted during the first half of 2003 due to the strengthening of the Euro and Brazilian Real against the U.S. Dollar. We have not generally sought to mitigate this translation effect through the use of derivative financial instruments. This practice exposes us to risks of currency exchange rate and interest rate fluctuations to a greater degree than if we were to use financial derivative instruments.

WE MAY NOT BE ABLE TO GENERATE SUFFICIENT CASH FLOWS TO MEET OUR DEBT SERVICE OBLIGATIONS.

Our ability to make scheduled payments on, or to refinance our obligations with respect to our indebtedness, including the senior secured notes, will depend on our financial and operating performance, which in turn will be affected by general economic conditions and by financial, competitive, regulatory and other factors beyond our control. We cannot assure you that our business will generate sufficient cash flows from operations or that future sources of capital will be available to us (whether under our senior credit facility or otherwise) in an amount sufficient to enable us to service our indebtedness and fund our other liquidity needs.

If we are unable to generate sufficient cash flows to satisfy our debt obligations, we may have to undertake alternative financing plans, such as refinancing or restructuring our debt, selling assets, reducing or delaying capital investments or seeking to raise additional capital. We cannot assure you that any refinancing would be possible, that any assets could be sold, or, if sold, of the timing of the sales and the amount of proceeds that may be realized from those sales, or that additional financing could be obtained on acceptable terms, if at all. Our inability to generate sufficient cash flows to satisfy our debt obligations, or to refinance our indebtedness on commercially reasonable terms, would materially and adversely affect our financial condition and results of operations.

THE CYCLICAL NATURE OF THE METALS RECYCLING INDUSTRY AND OF OUR CUSTOMERS INDUSTRIES COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR OPERATING FLEXIBILITY, FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The metals industry in general is highly cyclical in nature. It tends to reflect and be amplified by general economic conditions, both domestically and abroad. These conditions include the level of economic growth, financing availability, employment levels, interest rates, consumer confidence and housing demand. Historically, in periods of recession or periods of minimal economic growth, the operations of metals companies have been adversely affected. We are particularly sensitive to trends in cyclical industries such as the transportation and construction industries, which are both seasonal and highly cyclical in nature, and dependent on general economic conditions. For example, during recessions or periods of low growth, the transportation and construction industries typically experience major cutbacks in production, resulting in decreased demand for aluminum and zinc. This leads to significant fluctuations in demand and pricing for our products and services. Because we generally have high fixed costs, our profitability is significantly affected by decreased processing and production volume; accordingly, reduced demand and pricing pressures will adversely affect our

Table of Contents

financial condition and results of operations. Economic downturns in the national and international economies or a prolonged recession in our principal markets have adversely affected our operations in the past, and could have a material adverse effect on the combined company s future financial condition or results of operations.

Changes in the market price of aluminum and zinc impact the selling prices our our products. Market prices of aluminum and zinc are dependent upon supply and demand and a variety of factors over which we have little or no control, including:

- U.S. and world economic conditions;
- availability and relative pricing of metal substitutes;
- labor costs;
- energy prices;
- environmental and conservation regulations;
- seasonal factors and weather; and
- import and export restrictions.

DECREASED OUTSOURCING OF ALUMINUM RECYCLING BY THE PRIMARY ALUMINUM PRODUCERS COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

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 dross 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 capacity 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 increased internal recycling by a primary producer of aluminum.

A DOWNTURN IN PRODUCTION IN THE AUTOMOTIVE OR LIGHT TRUCK MARKETS IN THE U.S. AND EUROPE, OR A DECREASE IN THE USE OF ALUMINUM IN THOSE MARKETS, COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

The majority of our specialty alloys business serves the automotive and light truck markets. The volume of automotive and light truck production in North America, Europe and the rest of the world has fluctuated, sometimes significantly, from year to year, giving rise to fluctuations in demand for aluminum. Several automotive and light truck manufacturers extended their seasonal shutdowns at certain of their manufacturing facilities and reduced their production levels, and some announced during the second half of 2003 that they intended to continue operating at reduced production levels, which affected our business. In addition, automotive and light truck production and sales can be affected by labor relations, regulatory requirements and trade agreements. Reductions in the rate of automobile or light truck production in the markets we serve, or in the level of aluminum used in automobile or light truck production, could have a material adverse effect on our financial condition and results of operations. Additionally, plant shutdowns, strikes and work stoppages at our automotive or light truck customers facilities may adversely affect our business.

CONTINUING DECREASES IN THE U.S. ALUMINUM CAN RECYCLING RATE AND A LACK OF GROWTH IN U.S. ALUMINUM CAN PRODUCTION COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

U.S. aluminum can recycling rates have decreased from approximately 62% in 1995 to a current rate of approximately 50%. Continuing deterioration in the U.S. aluminum can recycling rate and a lack of growth in aluminum can production has slowed demand in recent years for our aluminum recycling services, which in turn has contributed to a decline in our percentage of tolling activities relative to our total volumes processed. If this trend continues, our capacity utilization will continue to decline and we will become increasingly exposed to asset write-downs and similar impairment charges. If capacity utilization is permanently impaired, we may be required to write down the net book value of some of our fixed assets. Furthermore, since much of our aluminum can recycling business is tolling business, a continued decline in the U.S. aluminum can recycling rate will have the effect of increasing our exposure to aluminum price fluctuations and our working capital requirements that will be required for our increased levels of product sales.

Table of Contents

IF WE LOST ORDER VOLUMES FROM ANY OF OUR LARGEST CUSTOMERS, OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS COULD BE MATERIALLY AND ADVERSELY AFFECTED.

Our business is exposed to risks related to customer concentration. In 2003, our 10 largest customers were responsible for 36% of our net revenues. No one customer accounted for more than 10% of our net revenues in 2003. A loss of order volumes from, or a loss of market share by, any major customer could materially and adversely affect our financial condition and results of operations. In addition, our 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. In addition, several of our customers have become involved in bankruptcy or insolvency proceedings and have defaulted on their obligations to us in recent years, which has adversely affected our financial condition and results of operations.

WE MAY NOT BE ABLE TO COMPETE SUCCESSFULLY IN THE MARKETS WE SERVE, WHICH COULD REDUCE OUR MARKET SHARE AND HAVE A MATERIAL ADVERSE EFFECT ON OUR SELLING PRICES AND SALES VOLUMES.

Aluminum competes with other material such as steel, plastic and glass for various applications. Higher aluminum prices tend to make aluminum products less competitive with these alternative materials.

The aluminum and zinc markets are highly competitive. The global aluminum recycling market is highly fragmented and characterized by smaller, regional operators. The principal factors of competition in our aluminum business include price, metal recovery rates, proximity to customers, molten metal delivery capability, environmental and safety regulatory compliance and types of services offered. The U.S. zinc recycling market is concentrated among a small number of competitors. The principal factors of competition in our zinc business are price, customer service and high product quality. We may not be able to compete successfully with respect to any of the foregoing factors.

Additional competition could result in lost market share or reduced prices for our products and services, either of which could have a material adverse effect on our financial condition and results of operations.

THE COST OF COMPLIANCE WITH AND LIABILITIES UNDER ENVIRONMENTAL, HEALTH AND SAFETY LAWS COULD MATERIALLY AND ADVERSELY AFFECT OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

We have ongoing environmental matters being conducted at sites for which we have or are alleged to have partial or full responsibility. Our operations are subject to numerous federal, state, local and foreign environmental laws and regulations, which govern, among other things, the discharge of hazardous materials into the air and water, the handling, storage, and disposal of hazardous materials, the remediation of contaminated sites, and employee health and safety. Compliance with environmental requirements is a major aspect of our operations. At present, the majority of our environmental compliance expenditures are directed toward controlling air emissions from all of our operations and managing and disposing of salt cake from our aluminum recycling. Changes in environmental requirements could materially increase our costs. For example, if salt cake were to become classified as a hazardous waste in the United States, our costs to manage and dispose of it would increase. Federal and state regulations continue to impose stricter emission requirements on the aluminum industry. While we believe that current pollution control measures at the emission sources at our facilities meet current requirements, additional equipment or process changes at some of our facilities may be required to meet future requirements.

We previously have agreed to indemnify certain customers and parties to acquisition agreements against environmental liabilities for which they might otherwise share responsibility under such contractual arrangements or pursuant to law.

Our operations also require environmental permits and approvals from governmental authorities, and any of these permits and approvals are subject to denial, revocation, or modification under various circumstances. Failure to obtain or comply with these permits and approvals, or with other environmental requirements, may subject us to civil or criminal enforcement proceedings that can lead to fines and penalties against us, orders requiring us to take certain actions, and temporary or permanent shutdown of our affected operations. We have implemented practices and procedures at our operating facilities that are intended to promote compliance with environmental laws and regulations. However, we cannot assure you that we are at all times in compliance with all environmental requirements.

Because we generate waste materials in our operations, and because we and businesses and operations we have acquired have done so in the past (in some cases for many years), we may be subject to material liability arising out of conditions caused by these materials. Such liability can include the cost of investigating and cleaning up these materials, fines and penalties sought by

Table of Contents

environmental authorities, and damages arising out of personal injury, contaminated property, and other toxic tort claims, as well as lost or impaired natural resources. Certain environmental laws impose joint and several liability for some of these types of damages, meaning that a person can be held liable for all damages even though others were also involved in causing them. Certain environmental laws also impose liability for some of these types of damages regardless of whether the person causing the damages did so through any unlawful conduct or other fault. We do not carry environmental impairment liability insurance because we consider that insurance to be expensive relative to the coverage provided.

We are also subject to various federal, state, local and foreign requirements concerning safety and health conditions in our manufacturing facilities. Those requirements may also subject us to material financial penalties or liabilities for non-compliance, as well as potential business disruption if any of our facilities or a portion of any facility is required to be temporarily closed as a result of any violation of those requirements. Any such financial liability or business disruption could have a material adverse effect on our financial condition and results of operations.

We spend substantial capital and operating sums on an ongoing basis to comply with environmental requirements. In addition, we are currently involved in certain investigations and actions in connection with environmental compliance and prior disposals of solid waste, including a claim related to a site in Illinois for which the Illinois Environmental Protection Agency has asserted that two of our zinc subsidiaries, which sent zinc oxide in the past to the site for processing and resale, are among the entities potentially responsible for the site-cleanup. Estimating future environmental compliance and remediation costs and other environmental liabilities is imprecise due to the continuing evolution of environmental requirements and uncertainties about their application to our operations, the availability and applicability of technology and the allocation of costs among responsible parties. New environmental requirements, enforcement policies or legal proceedings, an environmental incident at one of our properties or operations, or the discovery of an additional environmental condition or new information about existing conditions, could all have a material adverse effect on our financial condition and results of operations.

WE MAY HAVE TO TAKE FURTHER CHARGES TO EARNINGS IF OUR GOODWILL OR ASSET VALUES ARE IMPAIRED.

We are required to test our goodwill for impairment at least annually. The difference between the book value of an asset and its market value may indicate that an impairment exists.

In addition, our landfill assets are subject to charges for asset retirement obligations, which are adjusted over time to recognize the current fair market value of the obligations. We are also subject to charges for impairment or disposal of certain of our long-lived assets and facilities. For instance, over the past three years, we have closed two aluminum recycling facilities and one zinc recycling facility, provisionally suspended operations at another aluminum recycling facility and reduced the number of furnaces we operate at other domestic facilities. Continued under-utilization at our domestic aluminum and other facilities could result in write-downs and impairment charges. In addition, the carrying value of certain of our properties and assets held for sale could be reduced in the future to their estimated fair values less costs to sell, resulting in additional asset impairment charges at that time.

WE DO NOT HAVE LONG-TERM CONTRACTUAL ARRANGEMENTS WITH A SUBSTANTIAL NUMBER OF OUR CUSTOMERS AND WE MAY BE ADVERSELY AFFECTED IF OUR CUSTOMERS SWITCH SUPPLIERS.

A substantial number of our customers do not have a long-term contractual arrangement with us. These customers purchase products and services from us on a purchase order basis. We cannot assure you that these customers will continue to purchase our products and services. The loss of these customers or a significant reduction in their purchase orders could reduce our market share and have a material adverse effect on

our sales volume and our business.

WE COULD EXPERIENCE LABOR DISPUTES THAT COULD DISRUPT OUR BUSINESS.

Approximately 13% of our domestic employees and 53% of our foreign employees are represented by unions or equivalent bodies and are covered by collective bargaining or similar agreements which are subject to periodic renegotiation.

Although we believe that we will successfully negotiate new collective bargaining agreements when our other agreements expire, these negotiations:

- may not prove successful;
- may result in a significant increase in the cost of labor; or
- may break down and result in the disruption of our operations.

Table of Contents

We can give no assurance that such labor negotiations will conclude successfully or that any work stoppage or labor disturbances will not occur. Any such work stoppages or labor disturbances may have a material adverse effect on our financial condition and results of operations.

OUR VARIABLE RATE INDEBTEDNESS SUBJECTS US TO INTEREST RATE RISK, WHICH COULD CAUSE OUR DEBT SERVICE OBLIGATIONS TO INCREASE SIGNIFICANTLY.

Borrowings under our senior credit facility are at variable rates of interest and expose us to interest rate risk. If interest rates increase, our debt service obligations on the variable rate indebtedness will increase and our net income will decrease. In addition, we may consider entering into fixed-to-floating interest rate swaps with respect to a portion of the debt represented by the senior secured notes. Such a transaction would increase our variable rate debt.

THE LOSS OF CERTAIN MEMBERS OF OUR MANAGEMENT COULD HAVE A MATERIAL ADVERSE EFFECT ON OUR FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Our success depends, in part, on the efforts of our senior management and other key employees. These individuals possess sales, marketing, engineering, manufacturing, financial and administrative skills that are critical to the operation of our business. If we lose or suffer an extended interruption in the services of one or more of our senior officers, our financial condition and results of operations may be adversely affected. Moreover, the market for qualified individuals may be highly competitive and we may not be able to attract and retain qualified personnel to replace or succeed members of our senior management or other key employees, should the need arise.

OUR SIGNIFICANT DEBT OBLIGATIONS COULD LIMIT OUR FLEXIBILITY IN MANAGING OUR BUSINESS AND EXPOSE US TO CERTAIN RISKS.

We are highly leveraged. As of June 30, 2004, we would have been able to incur an additional $38,801,000 under our senior credit facility. Whenever during specified periods our availability under this facility is less than $50,000,000, we are subject to a minimum fixed charge coverage ratio and a minimum tangible net worth covenant. In addition, we may be permitted under our senior credit facility and the indenture governing the senior secured notes to incur additional debt, subject to certain limitations. Our high degree of leverage may have important consequences including the following:

- we may have difficulty satisfying our obligations under the senior secured notes or other indebtedness and, if we fail to comply with these requirements, an event of default could result;
- we may be required to dedicate a substantial portion of our cash flow from operations to required payments on indebtedness, thereby reducing the availability of cash flow for working capital, capital expenditures and other general corporate activities;
- covenants relating to our debt may limit our ability to obtain additional financing for working capital, capital expenditures and other general corporate activities;

covenants relating to our debt may limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;

we may be more vulnerable to the impact of economic downturns and adverse developments in our business; and

we may be placed at a competitive disadvantage against any less leveraged competitors.

The occurrence of any one of these events could have a material adverse effect on our business, financial condition, results of operations, prospects and ability to satisfy our debt obligations.

Certain Risks of the Proposed Merger

WE MAY FAIL TO OBTAIN ADEQUATE FINANCING, WHICH IS A CONDITION TO THE COMPLETION OF THE MERGER, AND AS A RESULT THE MERGER MAY NOT BE CONSUMMATED, OR IF CONSUMMATED, MAY CONTAIN FINANCING TERMS LESS FAVORABLE THAN ANTICIPATED.

As a condition to the completion of the merger, we and Commonwealth are required to obtain adequate financing to, among other things, pay for the costs of the merger and refinance significant portions of each company s outstanding debt obligations, including Commonwealth s senior subordinated notes, repurchase amounts previously sold under Commonwealth s receivables purchase agreement and repay all amounts outstanding under our and Commonwealth s senior credit facilities. Such financing may

Table of Contents

consist of public offerings of debt or private debt arrangements. No assurances can be given that the financing necessary to consummate the merger will be successfully obtained, or if obtained, that such financing will be on terms and conditions favorable to us. If we are unable to obtain the necessary financing to consummate the merger, our business, prospects, and future results of operations and financial condition, and the prices of our common stock, could be adversely affected.

WE MAY FACE DIFFICULTIES IN ACHIEVING THE EXPECTED BENEFITS OF THE MERGER.

We and Commonwealth currently operate as separate companies. We may not be able to realize the operating efficiencies, synergies, cost savings or other benefits expected from the merger. In addition, the costs we incur in implementing these efficiencies, synergies, cost savings and other benefits, including our ability to terminate, amend or renegotiate prior contractual commitments of either company, may be greater than expected. We also may suffer a loss of employees, customers or suppliers, a loss of revenues, or an increase in operating or other costs as a result of the merger or other difficulties relating to the merger.

For more information regarding certain risks of our proposed merger with Commonwealth, we refer you to our Registration Statement on Form S-4 as filed with the SEC on July 21, 2004, as it may be amended.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In the ordinary course of our business, we are exposed to potential losses arising from changes in the price of aluminum, zinc and natural gas. Changes in currency values and the level of interest rates also expose us to potential losses. We use derivative instruments, such as futures, options, swaps and interest rate caps to manage the effect of such changes. Because of the use of swap and forward contract hedging instruments, we are limited in our ability to take advantage of potential changes in aluminum, gas and zinc prices. The hedging instruments require us to exercise the hedging instrument at the settlement date regardless of the market price at that time. Therefore, in an effort to offset the effect of increasing prices, we have also limited our potential benefit of declining prices.

Risk Management. All derivative contracts are held for purposes other than trading, and are used primarily to mitigate uncertainty and volatility and cover underlying exposures. Our commodity and derivative activities are subject to the management, direction and control of our Risk Management Committee, which is composed of our chief executive officer, chief financial officer, and other officers and employees that the chief executive officer designates. The Risk Management Committee reports to our Board of Directors, which has supervisory authority over all of its activities.

Counter-parties. We are exposed to losses in the event of non-performance by the counter-parties to the derivative contracts discussed below. Although non-performance by counter-parties is possible, we do not currently anticipate any non-performance by any of these parties. Counter-parties are evaluated for creditworthiness and risk assessment prior to our initiating contract activities. The counter-parties creditworthiness is then monitored on an ongoing basis, and credit levels are reviewed to ensure that there is not an inappropriate concentration of credit outstanding to any particular counter-party.

Cautionary Note. Our deferred gains and losses accumulate on our balance sheet (in Other Comprehensive (Loss) Income) until the maturity of our respective hedging agreements. Due to the sometimes volatile nature of aluminum, zinc and natural gas prices, it would be impractical to estimate the amount we expect to be realized as earnings or loss on our income statement at any given time, or when these gains or losses will be

realized. Actual amounts realized will inevitably differ from our estimates. Our deferred hedging activities reduce, but do not eliminate, our exposure to the volatility of aluminum, zinc and natural gas prices on our operations.

Overview, significant metal price changes. The prices for aluminum and zinc were higher during the six months ended June 30, 2004 compared to the same period in 2003. As measured by the LME, overall primary aluminum and zinc metal prices are up approximately 22% and 34%, respectively. However, for the second quarter of 2004, primary aluminum and zinc prices had declined below their higher levels prevailing earlier in 2004.

Metal Commodity Price Risk. Aluminum and zinc ingots are internationally produced, priced and traded commodities, with their principal trading market being the LME. As part of our efforts to preserve margins, we enter into futures and options contracts. In our domestic aluminum and zinc segments, unrealized future gains and losses on these futures and options contracts qualify for deferred treatment SFAS 133 Accounting for Derivative Instruments and Hedging Activities, and SFAS 138 Accounting for Certain Derivative Instruments and Certain Hedging Activities.

Domestic Aluminum. We enter into futures sale contracts with metal brokers to fix the margin on a portion of the aluminum generated by our salt cake processing facility in Morgantown, Kentucky and some of the aluminum generated for sale from the processing of other scrap metal. These futures sale contracts are settled in the month of shipment.

Table of Contents

Our deferred domestic aluminum hedging positions are summarized below:

	Metric tonnes	Unrealized deferred gain (loss)	Unrealized deferred gain (loss) net of tax
Forward sales in 2004	(12,335)	(699,000)	(433,000)
Forward purchases in 2004	3,260	212,000	131,000
Net notional amount	(9,075)	(487,000)	(302,000)

For the six months ended June 30, 2004 and 2003, our domestic aluminum revenue was higher by $773,000 and $145,000, respectively, for settled metal hedging contracts. The impact of a 10% change in the June 30, 2004 LME price of aluminum ingot would not be material to our estimated gross profit for the year ending December 31, 2004.

Zinc: In the normal course of business, we enter into fixed-price forward sales and purchase contracts with a number of our zinc customers. In order to hedge the risk of higher metal prices, we enter into long positions, principally using future purchase contracts. These contracts are settled in the month of the corresponding production or shipment.

Our deferred zinc hedging positions are summarized below:

	Metric tonnes	Unrealized deferred gain	Unrealized deferred gain net of tax
Forward sales in 2004	(1,875)	$ 212,000	$ 131,000
Forward purchases in 2004	10,617	198,000	123,000
Net notional amount	8,742	$ 410,000	$ 254,000
Grand total forward sales, 2004 and beyond	(1,875)	$ 212,000	$ 131,000
Grand total forward purchases, 2004 and beyond	14,674	235,000	146,000
Net notional amount	12,799	$ 447,000	$ 277,000

For the six months ended June 30, 2004 and 2003, our zinc revenue was higher (lower) by $327,000 and ($325,000), respectively, due to settled zinc metal hedging contracts. The impact of a hypothetical 10% change in the June 30, 2004 LME price of zinc ingot would be material to our estimated gross profit for the year ending December 31, 2004. At this time, we estimate that a hypothetical 10% increase in the price of zinc

would increase our gross profit for the remainder of 2004 by approximately $350,000.

VAW-IMCO: VAW-IMCO has a significant metal hedging program. The majority of VAW-IMCO s operations are product sales, requiring it to take ownership of the materials processed and exposing it to more risk to changes in metal prices. In order to mitigate this risk, VAW-IMCO enters into LME high-grade and alloy aluminum forward sales and purchase contracts. VAW-IMCO does not hold or issue any derivative financial instruments for trading purposes. The functional currency of VAW-IMCO is the Euro; however, the derivatives utilized in hedging the market risk of changing prices of aluminum purchases and sales at VAW-IMCO facilities are based in U.S. Dollars. This results in foreign currency risk in addition to the risk of changing aluminum prices.

Unlike the derivative contracts utilized throughout the rest of our hedging operations, the unrealized gains and losses on VAW-IMCO s derivative contracts do not qualify for deferred treatment under SFAS 133, Accounting for Derivatives and Hedging Activities. VAW-IMCO s derivative contracts are recorded at fair value with unrealized gains and losses recognized currently in the financial statements. VAW-IMCO s metal hedging positions are summarized below:

U.S. Dollar denominated hedges	**Metric tonnes**	**Contract Value, U.S. Dollars**
Forward sales in 2004	(1,000)	$ 1,699,000
Forward purchases in 2004	1,000	(1,406,000)
Total		$ 293,000

Euro denominated hedges	**Metric tonnes**	**Contract Value, U.S. Dollars**
Forward sales in 2004	(39,975)	$ 69,424,000
Forward purchases in 2004	43,225	(74,013,000)
Total	3,250	$ (4,589,000)

VAW-IMCO recognized, in its cost of goods sold, unrealized gains of approximately $1,465,000 due to metal hedging activities for the six month period ended June 30, 2004.

Table of Contents

The impact of either a 10% increase in the June 30, 2004 LME price of aluminum or a 10% increase in the value of the U.S. Dollar against the Euro would be material to our estimated gross profit. As of June 30, 2004 we estimate that a 10% increase in the LME price of aluminum, holding currency rates constant, would increase our gross profit by approximately $550,000. Separately, for the same period, we also estimate that a 10% increase in the value of the U.S. Dollar against the Euro, holding metal prices constant, would increase our gross profit by approximately $400,000.

Natural Gas. Natural gas is the principal fuel used in our processing of aluminum and zinc. Natural gas prices are volatile, and we attempt to manage this volatility through the use of derivative commodity instruments. Our natural gas financial derivatives are traded in months forward, and settlement dates are scheduled to coincide with gas purchases during those future periods. These contracts reference physical natural gas prices or appropriate NYMEX futures contract prices.

We have entered into forward pricing positions for a portion of our domestic natural gas requirements for 2004. We currently have contracts in place to cover about 40% of our natural gas requirements for the succeeding six months.

Under the terms of our natural gas swap contracts, we make or receive payments based on the difference between the month-end closing price on the NYMEX and the fixed price agreed to in the swap contracts. The impact of a 10% change in the June 30, 2004 NYMEX closing price would be material to our estimated gross profit for the next nine months. We estimate that a 10% increase in the price of natural gas, as of June 30, 2004, would decrease our estimated gross profit for the remainder of this year by approximately $1,050,000.

In addition, a portion of our natural gas cost is recovered through price escalation clauses in our long-term contracts.

Our natural gas hedging activities are summarized in the table below:

	As of June 30, 2004
Amount of natural gas hedged, at period end, MMBTU s	2,540,000
Deferred gain	$ 2,694,000
Deferred gain, net of tax	$ 1,671,000

Our natural gas hedging activities, for the six months ended June 30, 2004 and 2003, decreased our cost of goods sold by $1,491,000 and $2,942,000, respectively.

Our international aluminum segment had no natural gas hedging activities for the six months ended June 30, 2004.

Interest. We have historically funded our operations from our existing credit facilities. As of June 30, 2004, approximately 16% of our outstanding debt bore interest at variable interest rates.

Our earnings are affected by changes in interest rates due to the impact those changes have on our interest expense from variable-rate debt instruments. The impact of a 10% increase in interest rates prevailing as of June 30, 2004, would decrease our operating results by approximately $100,000 for the remainder of the year.

In addition, we may enter into fixed-to-floating interest rate swaps with respect to a portion of the indebtedness represented by our senior secured notes. Such a transaction would increase our variable rate debt. We did not enter into any interest rate swaps or similar financial risk contracts during the six months ended June 30, 2004.

Market risk for fixed-rate long-term debt is estimated as the potential increase in fair value resulting from a hypothetical decrease in market interest rates. With respect to our fixed-rate long-term debt outstanding at June 30, 2004, a 10% decline in market interest rates would have resulted in an increase to the fair value of our fixed-rate long-term debt of approximately $11,320,000. The fair values of our long-term debt were estimated using discounted future cash flows based on our incremental borrowing rates for similar types of borrowing arrangements.

We have not generally sought to mitigate foreign currency translation effects through the use of derivative instruments.

Table of Contents

PART II. OTHER INFORMATION

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

Number	Description
12	Ratio of Earnings to Fixed Charges
*31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a).
*31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a).
*32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.

* Filed herewith

(b) Reports on Form 8-K

On April 14, 2004 we filed a Form 8-K under Item 5 and Item 9, reporting changes in management of the Company (including the appointment of Richard L. Kerr as interim President and Chief Executive Officer and John E. Balkcom as Chairman of the Board).

On April 30, 2004, we filed a Form 8-K under Item 5 and Item 7 regarding the execution of an Agreement and General Release dated April 20, 2004 by and among Don V. Ingram, IMCO Recycling Inc. and IMCO Management Partnership L.P.

On June 18, 2004, we filed a Form 8-K under Item 5 and Item 7, reporting the execution of the Agreement and Plan of Merger dated June 16, 2004, by and among IMCO Recycling Inc., Silver Fox Acquisition Company and Commonwealth Industries, Inc.

On July 20, 2004, we filed a Form 8-K under Item 5 and Item 7, reporting the First Amendment to Revolving Credit and Security Agreement by and among IMCO Recycling Inc., the other Borrowers, and the Lenders parties thereto dated May 26, 2004 and the Second Amendment to Revolving Credit and Security Agreement by and among IMCO Recycling Inc., the other Borrowers, and the Lenders parties thereto dated July 16, 2004.

Table of Contents

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.

IMCO Recycling Inc.

(Registrant)

Date: October 21, 2004

By: /s/ Robert R. Holian

Robert R. Holian

Senior Vice President

Controller and Chief Accounting Officer

Table of Contents

EXHIBIT INDEX

Number	Exhibit Title
12	Ratio of Earnings to Fixed Charges
*31.1	Certification of Chief Executive Officer Pursuant to Rule 13a-14(a).
*31.2	Certification of Chief Financial Officer Pursuant to Rule 13a-14(a).
*32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350.

* Filed herewith