

OLYMPIC STEEL INC  
Form 10-Q  
August 08, 2007

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549  
Form 10-Q**

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

**For the quarterly period ended June 30, 2007**

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

**Commission File Number 0-23320**

**OLYMPIC STEEL, INC.**

(Exact name of registrant as specified in its charter)

Ohio

34-1245650

(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification Number)

5096 Richmond Road, Bedford Heights, Ohio

44146

(Address of principal executive offices)

(Zip Code)

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

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

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

Large accelerated filer ☐ Accelerated filer ☒ Non-accelerated filer ☐

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

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

Class  
Common stock, without par value

Outstanding as of August 8, 2007  
10,702,465

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

	June 30, 2007 (unaudited)	December 31, 2006
<b>Assets</b>		
Cash and cash equivalents	\$ 8,940	\$ 5,211
Accounts receivable, net	120,600	85,883
Inventories	197,021	210,738
Prepaid expenses and other	9,464	6,383
<b>Total current assets</b>	<b>336,025</b>	<b>308,215</b>
Property and equipment, at cost	179,237	173,745
Accumulated depreciation	(90,721)	(86,386)
<b>Net property and equipment</b>	<b>88,516</b>	<b>87,359</b>
Goodwill	6,583	6,583
Other long-term assets	6,292	3,163
<b>Total assets</b>	<b>\$ 437,416</b>	<b>\$ 405,320</b>
<b>Liabilities</b>		
Accounts payable	\$ 89,936	\$ 75,095
Accrued payroll	8,722	7,698
Other accrued liabilities	9,780	9,547
<b>Total current liabilities</b>	<b>108,438</b>	<b>92,340</b>
Credit facility revolver	64,296	68,328
Other long-term liabilities	8,014	6,664
Deferred income taxes	3,550	3,751
<b>Total liabilities</b>	<b>184,298</b>	<b>171,083</b>
<b>Shareholders' Equity</b>		
Preferred stock		
Common stock	113,893	109,075
Retained earnings	139,225	125,162
<b>Total shareholders' equity</b>	<b>253,118</b>	<b>234,237</b>

<b>Total liabilities and shareholders' equity</b>	<b>\$ 437,416</b>	<b>\$ 405,320</b>
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*The accompanying notes are an integral part of these balance sheets.*

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**Olympic Steel, Inc.**  
**Consolidated Statements of Operations**  
(in thousands, except per share and tonnage data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
	(unaudited)		(unaudited)	
<b>Tons sold</b>				
<b>Direct</b>	<b>296,849</b>	<b>287,810</b>	<b>570,175</b>	<b>569,615</b>
<b>Toll</b>	<b>39,276</b>	<b>54,775</b>	<b>77,539</b>	<b>111,139</b>
	<b>336,125</b>	<b>342,585</b>	<b>647,714</b>	<b>680,754</b>
 <b>Net sales</b>	 <b>\$ 277,413</b>	 <b>\$ 256,155</b>	 <b>\$ 536,818</b>	 <b>\$ 495,026</b>
 <b>Costs and expenses</b>				
<b>Cost of materials sold (exclusive of depreciation shown below)</b>	<b>221,729</b>	<b>202,795</b>	<b>433,760</b>	<b>394,508</b>
<b>Warehouse and processing</b>	<b>14,272</b>	<b>13,657</b>	<b>27,947</b>	<b>25,294</b>
<b>Administrative and general</b>	<b>11,271</b>	<b>9,743</b>	<b>21,535</b>	<b>19,047</b>
<b>Distribution</b>	<b>6,464</b>	<b>6,953</b>	<b>12,773</b>	<b>13,201</b>
<b>Selling</b>	<b>4,185</b>	<b>3,597</b>	<b>7,966</b>	<b>7,033</b>
<b>Occupancy</b>	<b>1,451</b>	<b>1,272</b>	<b>3,204</b>	<b>2,963</b>
<b>Depreciation</b>	<b>2,170</b>	<b>2,096</b>	<b>4,352</b>	<b>4,104</b>
 <b>Total costs and expenses</b>	 <b>261,542</b>	 <b>240,113</b>	 <b>511,537</b>	 <b>466,150</b>
 <b>Operating income</b>	 <b>15,871</b>	 <b>16,042</b>	 <b>25,281</b>	 <b>28,876</b>
<b>Loss from joint ventures</b>		<b>(30)</b>		<b>(137)</b>
<b>Loss from disposition of joint ventures</b>		<b>(2,000)</b>		<b>(2,000)</b>
 <b>Income before financing costs and income taxes</b>	 <b>15,871</b>	 <b>14,012</b>	 <b>25,281</b>	 <b>26,739</b>
<b>Interest and other expense on debt</b>	<b>853</b>	<b>345</b>	<b>1,880</b>	<b>499</b>
 <b>Income before income taxes</b>	 <b>15,018</b>	 <b>13,667</b>	 <b>23,401</b>	 <b>26,240</b>
<b>Income tax provision</b>	<b>5,572</b>	<b>5,296</b>	<b>8,703</b>	<b>9,888</b>
 <b>Net income</b>	 <b>\$ 9,446</b>	 <b>\$ 8,371</b>	 <b>\$ 14,698</b>	 <b>\$ 16,352</b>
 <b>Earnings per share:</b>				
<b>Net income per share basic</b>	<b>\$ 0.89</b>	<b>\$ 0.80</b>	<b>\$ 1.40</b>	<b>\$ 1.58</b>
 <b>Weighted average shares outstanding basic</b>	 <b>10,603</b>	 <b>10,416</b>	 <b>10,527</b>	 <b>10,338</b>
 <b>Net income per share diluted</b>	 <b>\$ 0.88</b>	 <b>\$ 0.79</b>	 <b>\$ 1.37</b>	 <b>\$ 1.54</b>

<b>Weighted average shares outstanding</b>	<b>diluted</b>	<b>10,753</b>	<b>10,661</b>	<b>10,716</b>	<b>10,615</b>
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*The accompanying notes are an integral part of these statements.*

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**Olympic Steel, Inc.**  
**Consolidated Statements of Cash Flows**  
**For the Six Months Ended June 30,**  
**(in thousands)**

	2007 (unaudited)	2006 (unaudited)
<b>Cash flows from (used for) operating activities:</b>		
Net income	\$ 14,698	\$ 16,352
Adjustments to reconcile net income to net cash from operating activities (net of effects from purchases of GSP and PS&W) -		
Depreciation	4,352	4,104
Loss from joint ventures, net of distributions		137
Gain on disposition of property and equipment	(5)	(3)
Stock-based compensation	154	112
Other long-term assets	(3,129)	(2,980)
Other long-term liabilities	1,350	1,430
Long-term deferred income taxes	(201)	(730)
	17,219	18,422
<b>Changes in working capital:</b>		
Accounts receivable	(34,717)	(23,056)
Inventories	13,717	(32,641)
Prepaid expenses and other	(3,081)	(917)
Accounts payable	15,700	6,358
Accrued payroll and other accrued liabilities	1,257	242
	(7,124)	(50,014)
<b>Net cash from (used for) operating activities</b>	<b>10,095</b>	<b>(31,592)</b>
<b>Cash flows from (used for) investing activities:</b>		
Purchase of GSP interest		(100)
Purchase of PS&W		(8,916)
Capital expenditures	(5,509)	(8,127)
Proceeds from disposition of property and equipment	5	3
<b>Net cash used for investing activities</b>	<b>(5,504)</b>	<b>(17,140)</b>
<b>Cash flows from (used for) financing activities:</b>		
Credit facility revolver borrowings (payments), net	(4,032)	41,632
Change in outstanding checks	(859)	574
Repayments of debt		(2,264)
Proceeds from exercise of stock options (including tax benefit) and employee stock purchases	4,664	3,959
Dividends paid	(635)	(625)



<b>Net cash from (used for) financing activities</b>	<b>(862)</b>	<b>43,276</b>
<b>Cash and cash equivalents:</b>		
<b>Net change</b>	<b>3,729</b>	<b>(5,456)</b>
<b>Beginning balance</b>	<b>5,211</b>	<b>9,555</b>
<b>Ending balance</b>	<b>\$ 8,940</b>	<b>\$ 4,099</b>

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

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**Olympic Steel, Inc.**  
**Notes to Consolidated Financial Statements**  
**June 30, 2007**

**(1) Basis of Presentation:**

The accompanying consolidated financial statements have been prepared from the financial records of Olympic Steel, Inc. and its wholly-owned subsidiaries (collectively Olympic or the Company), without audit and reflect all normal and recurring adjustments which are, in the opinion of management, necessary to fairly present the results of the interim periods covered by this report. Year-to-date results are not necessarily indicative of 2007 annual results and these financial statements should be read in conjunction with the Company's 2006 Annual Report on Form 10-K for the period ended December 31, 2006. All significant intercompany transactions and balances have been eliminated in consolidation.

**(2) Accounts Receivable:**

The Company maintained allowances for doubtful accounts and unissued credits of \$3.1 million and \$3.3 million at June 30, 2007 and December 31, 2006, respectively. The allowance for doubtful accounts is maintained at a level considered appropriate based on historical experience and specific customer collection issues that have been identified. Estimations are based upon a calculated percentage of accounts receivable, which remains fairly level from year to year, and judgments about the probable effects of economic conditions on certain customers, which can fluctuate significantly from year to year. The Company cannot guarantee that the rate of future credit losses will be similar to past experience. The Company considers all available information when assessing each quarter the adequacy of its allowance for doubtful accounts.

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**Table of Contents****(3) Inventories:**

Steel inventories consist of the following:

	<b>June 30, 2007</b>	<b>December 31, 2006</b>
(in thousands)		
Unprocessed	\$ 151,423	\$ 159,581
Processed and finished	45,598	51,157
Totals	\$ 197,021	\$ 210,738

**(4) Investments in Joint Ventures:**

The Company and the United States Steel Corporation (USS) each own 50% of Olympic Laser Processing (OLP), a company that produced laser welded sheet steel blanks for the automotive industry. In January 2006, the Company and USS announced the closing of OLP. In conjunction with the closing, during the fourth quarter of 2005, the Company recorded a \$3.5 million charge for the disposition of the joint venture, consisting of \$1.3 million for the impairment of the Company's investment in OLP and a then-estimated \$2.2 million to be paid pursuant to the Company's guarantee of OLP's debt. OLP ceased operations during the first quarter of 2006. Operating losses incurred by OLP during the first quarter of 2006 were recorded against the \$3.5 million reserve. During the second and third quarters of 2006, OLP began liquidating its remaining assets. Offers from third parties to purchase the remaining assets were less than anticipated and the Company recorded an additional \$2.0 million charge in the second quarter of 2006 to reflect additional expected obligations under the guarantee of OLP's debt. In December 2006, the Company and USS each advanced \$3.2 million to OLP in connection with a loan guarantee. The Company believes the underlying value of OLP's remaining assets, upon liquidation, will be sufficient to repay the advance at a later date. The Company recorded 50% of OLP's net income or loss to its Consolidated Statement of Operations as Income (Loss) from Joint Ventures.

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Prior to May 1, 2006, the Company held a 49% ownership interest in G.S.P., LLC (GSP), a venture to support the flat-rolled steel requirements of the automotive industry as a Minority Business Enterprise. In order to gain full control of GSP, on May 1, 2006, the Company purchased the remaining 51% ownership interest for \$100 thousand and GSP ceased qualification as a Minority Business Enterprise.

During 2006, all of GSP's bank debt was extinguished, thereby eliminating the Company's 49% guarantee of GSP's demand note bank agreement.

Since May 1, 2006, GSP's results have been fully consolidated in the Company's financial statements. Prior to May 1, 2006, the Company, using the equity method of accounting, recorded 49% of GSP's net income or loss to its Consolidated Statements of Operations as Income (Loss) from Joint Ventures.

**(5) Acquisition of Tinsley Group PS&W, Inc.:**

In order to further expand value-added and fabrication capabilities, on June 2, 2006, the Company purchased all of the outstanding stock of Tinsley Group PS&W, Inc. (PS&W) for a final purchase price of \$9.0 million, which included \$6.7 million of goodwill. The results of PS&W have been fully consolidated in the Company's financial results since June 2, 2006.

PS&W is a full service fabricating company located in North Carolina that utilizes burning, forming, machining and painting to produce a wide variety of fabrications for large original equipment manufacturers of heavy construction equipment.

**(6) Debt:**

The Company's secured bank-financing agreement (the Credit Facility) is a revolving credit facility collateralized by the Company's accounts receivable, inventories, and substantially all of its property and equipment. Borrowings are limited to the lesser of a borrowing base, comprised of eligible receivables and inventories or, effective with a July 2007 amendment, \$130 million in the aggregate. An April 2007 amendment extended the maturity date of the Credit Facility to December 15, 2010, with annual extensions at the bank's option. The Company has the option to borrow based on the agent's base rate or Eurodollar Rates (EURO) plus a premium.

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The Credit Facility requires the Company to comply with various covenants, the most significant of which include: (i) minimum availability of \$10 million, tested monthly, (ii) a minimum fixed charge coverage ratio of 1.25, and a maximum leverage ratio of 1.75, which are tested quarterly, (iii) restrictions on additional indebtedness, and (iv) limitations on dividends, capital expenditures and investments. At June 30, 2007, the Company had approximately \$64 million of availability under the Credit Facility and the Company was in compliance with its covenants. The Credit Facility also contains an accordion feature which allows the Company to add up to \$25 million of additional revolver capacity in certain circumstances.

Outstanding checks are included as part of Accounts Payable on the accompanying Consolidated Balance Sheets and such checks totaled \$16.0 million as of June 30, 2007 and \$16.9 million as of December 31, 2006.

**(7) Shares Outstanding and Earnings Per Share:**

Earnings per share have been calculated based on the weighted average number of shares outstanding as set forth below:

(in thousands, except per share data)	<b>For the Three Months Ended June 30,</b>		<b>For the Six Months Ended June 30,</b>	
	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Weighted average shares outstanding	10,603	10,416	10,527	10,338
Assumed exercise of stock options and issuance of stock awards	150	245	189	277
Weighted average diluted shares	10,753	10,661	10,716	10,615
Net income	\$ 9,446	\$ 8,371	\$ 14,698	\$ 16,352
Basic earnings per share	\$ 0.89	\$ 0.80	\$ 1.40	\$ 1.58
Diluted earnings per share	\$ 0.88	\$ 0.79	\$ 1.37	\$ 1.54

**(8) Stock Options:**

In January 1994, the Olympic Steel, Inc. Stock Option Plan (Option Plan) was adopted by the Board of Directors and approved by the shareholders of the Company. Pursuant to the provisions of the Option Plan, key employees of the Company, non-employee directors and

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consultants may be offered the opportunity to acquire shares of Common Stock by the grant of stock options, including both incentive stock options (ISOs) and nonqualified stock options. ISOs are not available to non-employee directors or consultants. A total of 1,300,000 shares of Common Stock were originally reserved for issuance under the Option Plan. To the extent possible, shares of treasury stock are used to satisfy shares resulting from the exercise of stock options. The purchase price of a share of Common Stock pursuant to an ISO will not be less than the fair market value of a share of Common Stock at the grant date. Options vest over periods ranging from six months to five years and all expire 10 years after the grant date.

The Option Plan terminates on January 5, 2009. Termination of the Option Plan will not affect outstanding options. As of June 30, 2007, there were no remaining shares of Common Stock available for grant under the Option Plan.

On January 1, 2006, the Company adopted the provisions of Statement of Financial Accounting Standards No. 123-R (SFAS No. 123-R) and elected to use the modified prospective transition method. The modified prospective transition method requires that compensation cost be recognized in the financial statements for all awards granted after the date of adoption as well as for existing awards for which the requisite service has not been rendered as of the date of the adoption. The modified prospective transition does not require prior periods to be restated. Prior to the adoption of SFAS No. 123-R, the Company accounted for stock-based compensation using the intrinsic value method prescribed in Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees, and related

Interpretations. The Company has elected to use the short-cut method to calculate the historical pool of windfall tax benefits upon adoption of SFAS No. 123-R. The election to use the short-cut method had no effect on the Company's financial statements.

Under the intrinsic value method used prior to January 1, 2006, compensation expense for stock-based compensation was not recognized in the Company's Consolidated Statements of Operations as all stock options granted by the Company had an exercise price equal or greater than the market value of the underlying Common Stock on the option grant date. The adoption of SFAS No. 123-R resulted in the following:

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	<b>For the Three Months Ended June 30,</b>		<b>For the Six Months Ended June 30,</b>	
(in thousands, except per share data)	<b>2007</b>	<b>2006</b>	<b>2007</b>	<b>2006</b>
Stock option expense before taxes	\$7	\$30	\$14	\$ 112
Stock option expense after taxes	5	18	9	69
Impact per basic share	\$	\$	\$	\$0.01
Impact per diluted share	\$	\$	\$	\$0.01

All pre-tax charges related to stock options were included in the caption Administrative and General on the accompanying Consolidated Statement of Operations.

The fair value of each option grant was estimated as of the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions:

	<b>2007</b>	<b>2006</b>
Risk-free interest rate	4.58%	N/A
Expected life in years	10	N/A
Expected volatility	57.7%	N/A
Expected dividend yield	0.4%	N/A

The expected volatility assumption was derived by referring to changes in the Company's historical Common Stock prices over a timeframe similar to that of the expected life of the award.

No options were granted during 2006. Options to purchase 24,170 shares of Common Stock were granted during the second quarter of 2007. The weighted-average fair value of options granted during 2007 was \$22.55.

The following table summarizes stock-based award activity during the six months ended June 30, 2007:

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	Number of  Shares	Weighted Average  Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2006	477,140	\$ 6.12		
Granted	24,170	32.63		
Exercised	(297,503)	4.94		
Canceled				
Outstanding at June 30, 2007	203,807	\$ 10.99	5.9 years	\$ 3,602
Exercisable at June 30, 2007	187,473	\$ 7.96	5.1 years	\$ 3,881

The total intrinsic value of stock options exercised during the six months ended June 30, 2007 and 2006 were \$8.3 million and \$6.3 million, respectively. Net cash proceeds from the exercise of stock options were \$1.5 million and \$1.6 million for the six months ended June 30, 2007 and 2006, respectively. Income tax benefits of \$3.2 million and \$2.4 million were realized from stock option exercises during the six months ended June 30, 2007 and 2006, respectively. The fair value of options vested during the six months ended June 30, 2007 and 2006 totaled \$45 thousand and \$132 thousand, respectively.

As of June 30, 2007, approximately \$617 thousand of expense, before taxes, with respect to non-vested stock-based awards has yet to be recognized and will be amortized into expense over a weighted-average period of 1.82 years.

**(9) Restricted Stock Units and Performance Share Units:**

At the Annual Meeting of Shareholders held on April 27, 2007, the shareholders of the Company approved the Olympic Steel 2007 Omnibus Incentive Plan (the Plan). The Plan authorizes the Company to grant stock options, stock appreciation rights, restricted shares, restricted share units, performance shares, and other stock- and cash-based awards to employees and Directors of, and consultants to, the Company and its affiliates. Under the plan, 500,000 shares of Common Stock are available for equity grants.

On May 1, 2007, the Compensation Committee of the Company's Board of Directors approved the grant of 1,800 restricted stock units (RSU) to each non-employee Director. Subject to the terms of the Plan and the RSU Agreement, the RSUs vest at the end of 2007. The RSUs are not converted into shares of Common Stock until the Board member either resigns or is terminated from the Board of Directors.



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On May 1, 2007, the Compensation Committee of the Company's Board of Directors also granted 32,378 performance-earned restricted stock units (PERSU) to the senior management of the Company. The PERSUs may be earned based on the Company's performance over a 32-month period, beginning May 1, 2007 and would be converted to shares of Common Stock in 2010, based on the achievement of two separate financial measures: (1) the Company's EBITDA (50% weighted); and (2) return on invested capital (50% weighted). No shares will be earned unless the threshold amounts for each performance measure are met. Up to 150% of the targeted amount of PERSUs may be earned.

The following table summarizes the activity related to RSUs and PERSUs for the six months ended June 30, 2007:

	<b>Number of Shares</b>
Unvested as of January 1, 2007	
Granted	41,378
Vested	
Forfeited	
Unvested as of June 30, 2007	41,378

Under SFAS No. 123-R, stock compensation expense recognized on RSUs and PERSUs is summarized in the following table:

	<b>For the Three and Six Months Ended June 30,</b>	
(in thousands, except per share data)	<b>2007</b>	<b>2006</b>
Stock award expense before taxes	\$ 139	\$
Stock award expense after taxes	88	
Impact per basic share	\$0.01	\$
Impact per diluted share	\$0.01	\$

All pre-tax charges related to RSUs and PERSUs were included in the caption, Administrative and General on the accompanying Consolidated Statement of Operations.

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**(10) Supplemental Cash Flow Information:**

Interest paid during the first six months of 2007 totaled \$2.1 million, compared to \$290 thousand in the first six months of 2006. Income taxes paid during the first six months of 2007 and 2006 totaled \$6.0 million and \$10.1 million, respectively.

**(11) Impact of Recently Issued Accounting Pronouncements:**

In July 2006, the FASB issued Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes: an interpretation of FASB Statement No. 109. This interpretation clarifies the accounting for uncertainty in income taxes recognized in an entity's financial statements in accordance with SFAS No. 109, Accounting for Income Taxes. FIN 48 prescribes a recognition threshold and measurement principles for financial statement disclosure of tax positions taken or expected to be taken on a tax return. The Company adopted FIN 48 on January 1, 2007. The adoption had no effect on the opening balance of retained earnings as of January 1, 2007.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157 (SFAS No. 157), Fair Value Measurements. This statement defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement applies under other accounting pronouncements that require or permit fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. We do not expect the adoption of SFAS No. 157 will have a material impact on our consolidated financial statements.

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**Item 2. *Management's Discussion and Analysis of Financial Condition and Results of Operations***

The following discussion and analysis should be read in conjunction with our unaudited consolidated financial statements and accompanying notes contained herein and our consolidated financial statements, accompanying notes and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended December 31, 2006. This discussion and analysis contains forward-looking statements that involve risks, uncertainties and assumptions. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of many factors, including those described in Item 1A, Risk Factors, of our Annual Report on Form 10-K and under the caption "Forward-Looking Information" below.

**Overview**

We are a leading U.S. steel service center with over 50 years of experience. Our primary focus is on the direct sale and distribution of large volumes of processed carbon, coated and stainless flat-rolled sheet, coil and plate products. We act as an intermediary between steel producers and manufacturers that require processed steel for their operations. We serve customers in most carbon steel consuming industries, including manufacturers and fabricators of transportation and material handling equipment, automobiles, construction and farm machinery, storage tanks, environmental and energy generation, food service and electrical equipment, as well as general and plate fabricators, and steel service centers. We distribute our products primarily through a direct sales force.

We operate as a single business segment with 16 strategically-located processing and distribution facilities in Connecticut, Georgia, Illinois, Iowa, Michigan, Minnesota, North Carolina, Ohio and Pennsylvania. This geographic footprint allows us to focus on regional customers and larger national and multi-national accounts, primarily located throughout the midwestern, eastern and southern United States.

We sell a broad range of steel products, many of which have different gross profits and margins. Products that have more value-added processing generally have a greater gross profit and higher margins. Accordingly, our overall gross profit is affected by, among other things, product mix, the amount of processing performed, the availability of steel, volatility in selling prices and

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material purchase costs. We also perform toll processing of customer-owned steel, the majority of which is performed by our Detroit and Georgia operations. We sell certain products internationally, primarily in Puerto Rico and Mexico. All international sales and payments are made in United States dollars. Recent international sales have been immaterial to our consolidated financial results.

Our results of operations are affected by numerous external factors including, but not limited to, general and global business, economic and political conditions, competition, steel pricing and availability, energy prices, pricing and availability of raw materials used in the production of steel, customer demand for steel, customers' ability to manage their credit line availability and layoffs or work stoppages by our own, our suppliers' or our customers' personnel. The steel industry also continues to be affected by the global consolidation of our suppliers, competitors, and end-use customers.

On May 1, 2006, we acquired the remaining 51% interest in GSP. Prior to May 1, 2006, our 49% interest in GSP was accounted for under the equity method. Since May 1, 2006, the results of GSP have been fully consolidated into our financial statements. In January 2006, we announced plans to close the OLP joint venture in Detroit, Michigan. OLP, which was a processor of laser welded steel blanks for the automotive industry, ceased operations in the first quarter of 2006. Our 50% interest in OLP is accounted for under the equity method.

In June 2006, we acquired all of the outstanding stock of PS&W, a North Carolina-based fabricator of heavy construction equipment components. Since June 2, 2006, the results of PS&W have been fully consolidated into our financial statements.

A collective bargaining agreement covering approximately five Detroit maintenance workers expired July 31, 2007. Employees covered under this agreement continue to operate as a new agreement is negotiated. While we expect to be able to negotiate a new agreement, there can be no assurances that such resolution will occur. Collective bargaining agreements covering our Minneapolis and other Detroit employees expire in 2009 and subsequent years. We have never experienced a work stoppage and we believe that our relationship with employees is good. However, any prolonged work stoppages by our personnel represented by collective bargaining units could have a material adverse impact on our business, financial condition, results of operations, and cash flows.

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**Critical Accounting Policies**

This discussion and analysis of financial condition and results of operations is based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires us to make estimates and assumptions that affect the amounts reported in the financial statements. Actual results could differ from these estimates under different assumptions or conditions. On an ongoing basis, we monitor and evaluate our estimates and assumptions.

For further information regarding the accounting policies that we believe to be critical accounting policies and that affect our more significant judgments and estimates used in preparing our consolidated financial statements, see Management's Discussion and Analysis of Financial Condition and Results of Operations contained in our Annual Report on Form 10-K for the year ended December 31, 2006.

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**Table of Contents****Results of Operations**

The following table sets forth certain income statement data for the three and six months ended June 30, 2007 and 2006 (dollars are shown in thousands):

	For the Three Months Ended June 30,				For the Six Months Ended June 30,			
	2007		2006		2007		2006	
	\$	% of net sales	\$	% of net sales	\$	% of net sales	\$	% of net sales
Net sales	\$277,413	100.0%	\$256,155	100.0%	\$536,818	100.0%	\$495,026	100.0%
Gross profit (1)	55,684	20.1%	53,360	20.8%	103,058	19.2%	100,518	20.3%
Operating expenses (2)	39,813	14.4%	37,318	14.6%	77,777	14.5%	71,642	14.5%
Operating income	\$ 15,871	5.7%	\$ 16,042	6.3%	\$ 25,281	4.7%	\$ 28,876	5.8%

(1) Gross profit is calculated as net sales less the cost of materials sold, exclusive of depreciation.

(2) Operating expenses are calculated as total costs and expenses less the cost of materials sold.

Tons sold decreased 1.9% to 336 thousand in the second quarter of 2007 from 343 thousand in the second quarter of 2006. Tons sold in the second quarter of 2007 included 297 thousand from direct sales and 39 thousand from toll processing, compared with 288 thousand direct tons and 55 thousand toll tons in the comparable period of last year. Tons sold decreased 4.9% to 648 thousand in the first six months of 2007 from 681 thousand in the first six months of 2006. Tons sold in the first six months of 2007 included 570 thousand direct tons and 78 thousand from toll processing, compared with 570 thousand direct tons and 111 thousand toll tons in the comparable period last year. The decrease in tons sold was primarily attributable to lower sales to other steel service centers and lower toll processing sales to domestic automotive customers. Tons sold in the third quarter of 2007 are expected to be lower than second quarter 2007 levels due to normal seasonal patterns.

Net sales increased 8.3% to \$277.4 million in the second quarter of 2007 from \$256.2 million in the second quarter of 2006. Net sales increased 8.4% to \$536.8 million in the first six months of 2007 from \$495.0 million in the first six months of 2006. Average selling prices for the second quarter of 2007 increased 10.4% from last year's second quarter and decreased 0.9% from the first quarter of 2007.

As a percentage of net sales, gross profit (exclusive of depreciation) decreased to 20.1% in the second quarter of 2007 from 20.8% in the second quarter of 2006. For the first six months of 2007, gross margin decreased to 19.2% from 20.3% in the first six months of 2006. Due to

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normal seasonal patterns, a decrease in customer demand could lead to more competition for sales, which could reduce our selling prices and our gross margin levels in the third quarter of 2007.

Operating expenses in the second quarter of 2007 increased 6.7% to \$39.8 million from \$37.3 million in last year's second quarter. Operating expenses in the first six months of 2007 increased 8.6% to \$77.8 million from \$71.6 million during the first six months of 2006. The increase in operating expenses was primarily attributable to the inclusion of PS&W's operating expenses in 2007 results and the costs associated with the implementation of our new information system, which commenced during the third quarter of 2006. As a percentage of net sales, operating expenses decreased to 14.4% for the second quarter of 2007 from 14.6% in the comparable 2006 period. Operating expenses during both the first six months of 2007 and 2006 were 14.5% of net sales.

During the second quarter of 2006, we recorded a \$2 million charge to increase the reserve associated with the closing of OLP. During 2007, all expenses associated with the closing of OLP have been charged against that reserve.

Financing costs totaled \$853 thousand for the second quarter of 2007 compared to \$345 thousand for the second quarter of 2006. Financing costs totaled \$1.9 million for the first six months of 2007, compared to \$499 thousand for the first six months of 2006. Our effective borrowing rate, inclusive of deferred financing fees and commitment fees, for the first six months of 2007 was 7.2% compared to 8.8% in the first six months of 2006. Debt levels in 2007 have been higher than 2006 due to higher working capital levels and increased capital expenditures.

For the second quarter of 2007, income before income taxes totaled \$15.0 million compared to \$13.7 million in the second quarter of 2006. For the first six months of 2007, income before taxes totaled \$23.4 million, compared to \$26.2 million in the first six months of 2006. An income tax provision of 37.2% was recorded for the first six months of 2007, compared to a provision of 37.7% for the first six months of 2006. We expect the effective tax rate to approximate 37% to 38% for the remainder of 2007. Income taxes paid totaled \$6.0 million and \$10.1 million for the first six months of 2007 and 2006, respectively.

Net income for the second quarter of 2007 totaled \$9.4 million or \$.88 per diluted share, compared to net income of \$8.4 million or \$.79 per diluted share for the second quarter of 2006. Net income for the first six months of 2007 totaled \$14.7 million or \$1.37 per diluted share,

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compared to net income of \$16.4 million or \$1.54 per diluted share for the first six months of 2006.

**Liquidity and Capital Resources**

Our principal capital requirements include funding working capital needs, purchasing and upgrading processing equipment and facilities, acquisitions, and paying dividends. We use cash generated from operations, leasing transactions, and our revolving credit facility to fund these requirements.

Working capital at June 30, 2007 totaled \$227.6 million, an \$11.7 million increase from the end of the prior year. Significant working capital changes included a \$34.7 million increase in accounts receivable, partially offset by a \$13.7 million decrease in inventories and a \$14.8 million increase in accounts payable.

For the six months ended June 30, 2007, we generated \$10.1 million of net cash from operations, of which \$17.2 million was derived from cash earnings and \$7.1 million was used for working capital.

During the first six months of 2007, we spent \$5.5 million on capital expenditures. We expect to spend between \$15 million and \$20 million on capital expenditures in 2007 and we anticipate using our financial position to participate in the consolidation of the service center and fabrication industries. In 2007, we will add a \$5.5 million stretcher-leveler cut-to-length line in Minneapolis and we have undertaken a \$2.9 million project to expand our Iowa facility by approximately 54,000 square feet in order to meet our customers' need for high quality sheet product. We have also installed additional laser and plasma cutting equipment in Cleveland, Chicago and Chambersburg to support our growing value-added services. In July 2006, we announced the beginning of a project to implement a new single information system to replace the three systems we currently use. The objective is to standardize and streamline business processes and improve support for our growing service center and fabrication business. The project will require a significant deployment of capital and will require a significant use of management's time. The total external costs associated with the new information system are expected to approximate \$14 million over a three-year phased implementation that began in July 2006.

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During the first six months of 2007, in financing activities, we generated \$4.7 million from the exercise of stock options, \$4.0 million of which was used to repay borrowings under our revolving credit facility.

In July 2007, our Board of Directors approved a regular quarterly dividend of \$.04 per share, which is payable on September 17, 2007 to shareholders of record as of September 3, 2007. The September quarterly dividend is \$.01 per share higher than in previous quarters. Our Board of Directors previously approved dividends of \$.03 per share, which were paid on March 15, 2007 and June 15, 2007. We expect to make regular dividend distributions in the future, subject to the availability of cash and continuing determination by our Board of Directors that the payment of dividends remains in the best interest of our shareholders.

Our secured bank-financing agreement (the Credit Facility) is a revolving credit facility collateralized by our accounts receivable, inventories, and substantially all of our property and equipment. Borrowings are limited to the lesser of a borrowing base, comprised of eligible receivables and inventories or, effective with a July 2007 amendment, \$130 million in the aggregate. An April 2007 amendment extended the maturity date of the Credit Facility to December 15, 2010, with annual extensions at the banks' option.

The Credit Facility requires us to comply with various covenants, the most significant of which include: (i) minimum availability of \$10 million, tested monthly, (ii) a minimum fixed charge coverage ratio of 1.25, and a maximum leverage ratio of 1.75, which are tested quarterly, (iii) restrictions on additional indebtedness, and (iv) limitations on dividends, capital expenditures and investments. At June 30, 2007, we had approximately \$64 million of availability under our Credit Facility and we were in compliance with our covenants. The Credit Facility also contains an accordion feature which allows us to add up to \$25 million of additional revolver capacity in certain circumstances. We believe that funds available under our Credit Facility and lease arrangements, together with funds generated from operations, will be sufficient to provide us with the liquidity necessary to fund anticipated working capital requirements and capital expenditure requirements over the next 12 months. In the future, we may, as part of our business strategy, acquire and dispose of other companies in the same or complementary lines of business, enter into and exit strategic alliances and joint ventures, and pursue other business ventures. Accordingly, the timing and size of our capital requirements are subject to change as business conditions warrant and opportunities arise.

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**Forward-Looking Information**

This Quarterly Report on Form 10-Q and other documents we file with the SEC contain various forward-looking statements that are based on current expectations, estimates, forecasts and projections about our future performance, business, our beliefs and management's assumptions. In addition, we, or others on our behalf, may make forward-looking statements in press releases or written statements, or in our communications and discussions with investors and analysts in the normal course of business through meetings, webcasts, phone calls and conference calls. Words such as may, will, anticipate, should, intend, expect, believe, estimate, project, plan, as the negative of these terms or similar expressions are intended to identify forward-looking statements, which are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Such statements are subject to certain risks, uncertainties and assumptions including, but not limited to those set forth in Item 1A, Risk Factors, as found in our Annual Report on

Form 10-K for the year ended December 31, 2006 and the following:

general and global business, economic and political conditions;

competitive factors such as availability and pricing of steel, industry inventory levels and rapid fluctuations in customer demand and pricing;

the cyclical and volatility within the steel industry;

the ability of customers (especially in the domestic automotive industry) to maintain their credit availability;

customer, supplier, and competitor consolidation, bankruptcy or insolvency;

layoffs or work stoppages by our own or our suppliers' or customers' personnel;

the availability and costs of transportation and logistical services;

equipment malfunctions or installation delays;

the successes of our capital investments;

the successes of our strategic efforts and initiatives to increase sales volumes, maintain cash turnover, maintain or improve inventory turns and reduce costs;

the adequacy of our information technology and business system software;

the successful implementation of our new information system;

the timing and outcome of OLP's efforts and ability to liquidate its remaining assets;

the post-acquisition integration of PS&W; and

our ability to pay regular quarterly cash dividends.

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Should one or more of these, or other risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual results may vary materially from those anticipated, intended expected, believed, estimated, projected or planned. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We undertake no obligation to republish revised forward-looking statements to reflect the occurrence of unanticipated events of circumstances after the date hereof, except as otherwise required by law.

**Item 3. *Qualitative and Quantitative Disclosures About Market Risk***

During the past several years, the base price of carbon flat-rolled steel has fluctuated significantly. Declining prices could reduce our gross profit margin percentages to levels that are lower than our historical levels. Higher levels of inventory held by us, other steel service centers, or end-use customers could cause competitive pressures which could also reduce gross margins. Higher raw material costs for steel producers could cause the price of steel to increase.

While we have generally been successful in the past in passing on producers' price increases and surcharges to our customers, there is no guarantee that we will be able to pass on price increases to our customers in the future.

Approximately 9% of our net sales in the first six months of 2007 were directly to automotive manufacturers or manufacturers of automotive components and parts. The automotive industry experiences significant fluctuations in demand based on numerous factors such as general economic conditions and consumer confidence. The automotive industry is also subject, from time to time, to labor work stoppages. The domestic automotive industry, which has experienced a number of bankruptcies, is currently involved in significant restructuring and labor contract negotiations, which has resulted in lower production volumes. Certain customers in this industry represent an increasing credit risk.

Inflation generally affects us by increasing the cost of employee wages and benefits, transportation services, processing equipment, purchased steel, energy and borrowings under our credit facility. General inflation has not had a material effect on our financial results during the past two years; however, we have experienced increased distribution expense as a result of higher fuel costs.

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When raw material prices increase, competitive conditions will influence how much of the steel price increase can be passed on to our customers. When raw material prices decline, customer demands for lower cost product result in lower selling prices. Declining steel prices have generally adversely affected our net sales and net income, while increasing steel prices favorably affect net sales and net income.

We are exposed to the impact of interest rate changes and fluctuating steel prices. We have not entered into any interest rate or steel commodity hedge transactions for speculative purposes or otherwise.

Our primary interest rate risk exposure results from variable rate debt. If interest rates in the future were to increase 100 basis points (1.0%) from June 30, 2007 rates and, assuming no change in total debt from June 30, 2007 levels, the additional annual interest expense to us would be approximately \$642 thousand. We currently do not hedge our exposure to variable interest rate risk. However, we do have the option to enter into 30- to 180- day fixed base rate EURO loans under the Credit Facility.

**Item 4. Controls and Procedures**

The evaluation required by Rule 13a-15 of the Securities Exchange Act of 1934 of the effectiveness of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934) as of the end of the period covered by this Report have been carried out under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer. These disclosure controls and procedures are designed to provide reasonable assurance that information required to be disclosed in reports that are filed with or submitted to the SEC is: (i) accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures; and (ii) recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC. Based on this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of June 30, 2007, our disclosure controls and procedures were effective.

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There were no changes in our internal controls over financial reporting that occurred during the second quarter of 2007 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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**Table of Contents****Part II. OTHER INFORMATION**

Items 1, 1A, 2, and 3 of this Part II are either inapplicable or are answered in the negative and are omitted pursuant to the instructions to Part II.

**Item 4. *Submission of Matters to a Vote of Security Holders***

(a) The Company's Annual Meeting of Shareholders was held on April 27, 2007.

(b) At the Annual Meeting, the Company's shareholders elected Michael D. Siegal, Thomas M. Forman, and James B. Meathe as Directors for a two-year term, which expires at the Annual Meeting of Shareholders in 2009.

The following tabulation represents voting for the Directors:

	<b>For</b>	<b>Withheld Authority</b>
Michael D. Siegal	8,812,643	1,385,480
Thomas M. Forman	8,810,943	1,388,880
James B. Meathe	8,987,366	1,036,034

(c) At the Annual Meeting, the Company's shareholders approved the adoption of the Olympic Steel, Inc. 2007 Omnibus Incentive Plan. The holders of 6,993,447 shares of common stock voted to approve the adoption, the holders of 967,757 shares voted against the adoption, the holders of 13,875 shares abstained from voting, and the holders of 2,467,499 shares did not vote.

(d) At the Annual Meeting, the Company's shareholders approved the amendment to the Company's Code of Regulations to allow uncertificated shares in accordance with Nasdaq requirements. The holders of 9,976,987 shares of common stock voted to approve the amendment, the holders of 31,783 shares voted against the amendment, the holders of 12,030 shares abstained, and the holders of 421,778 shares did not vote.

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**Item 6. Exhibits**

<b>Exhibit</b>	<b>Description of Document</b>	<b>Reference</b>
4.16	Amendment No. 14 to Amended and Restated Credit Agreement dated July 18, 2007 by and among the Registrant, five banks and Comerica Bank, as Administrative Agent.	Incorporated by reference to Exhibit 4.16 to Registrant's Form 8-K filed with the Commission on July 18, 2007.
10.22*	Form of Performance-Earned Restricted Stock Unit (PERS Unit) Agreement for Messrs. Siegal, Wolfort and Marabito.	Filed herewith
10.23*	Form of Performance-Earned Restricted Stock Unit (PERS Unit) Agreement for Mr. Manson and Ms. Potash.	Filed herewith
31.1	Certification of the Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed herewith
31.2	Certification of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.	Filed herewith
32.1	Certification of the Principal Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	Furnished herewith
32.2	Certification of the Principal Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	Furnished herewith
*	This Exhibit is a management contract or compensatory plan or arrangement.	

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**SIGNATURES**

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

**OLYMPIC STEEL, INC.**

(Registrant)

Date: August 8, 2007

By: /s/ Michael D. Siegal

**Michael D. Siegal**

Chairman of the Board and Chief Executive  
Officer

By: /s/ Richard T. Marabito

**Richard T. Marabito**

Chief Financial Officer  
(Principal Accounting Officer)

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