

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, DC 20549**

FORM 10-K

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Fiscal Year Ended December 31, 2010
- OR
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Commission File Number 000-25032



UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.

(Exact name of Registrant as specified in its charter)

DELAWARE
(State or other jurisdiction of
incorporation or organization)

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

25-1724540
(IRS Employer
Identification No.)

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

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

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

Title of Class

Common Stock, par value \$.001 per share

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data file required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

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

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

The aggregate market value of the voting stock held by non-affiliates of the registrant on June 30, 2010, based on the closing price of \$15.99 per share on that date, was \$51,432,000. For the purposes of this disclosure only, the registrant has assumed that its directors, executive officers, and beneficial owners of 5% or more of the registrant's Common Stock are the affiliates of the registrant. The registrant has made no determination that such persons are "affiliates" within the meaning of Rule 405 under the Securities Act of 1933.

As of February 28, 2011, there were 6,881,464 shares of the Registrant's Common Stock issued and outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Part III of this Form 10-K incorporates by reference portions of the Company's definitive Proxy Statement for the 2011 Annual Meeting of Stockholders.

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PART I

ITEM 1. BUSINESS

GENERAL

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

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

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

INDUSTRY OVERVIEW

The specialty steel industry is a relatively small but distinct segment of the overall steel industry. Specialty steels include stainless steels, high-speed and tool steels, electrical steels, high-temperature alloys, magnetic alloys and electronic alloys. Specialty steels are made with a high alloy content, which enables their use in environments that demand exceptional hardness, toughness, strength and resistance to heat, corrosion or abrasion, or combinations thereof. Specialty steels generally must conform to more demanding customer specifications for consistency, straightness and surface finish than carbon steels. According to the Specialty Steel Industry of North America (“SSINA”), annual domestic consumption of specialty steels approximated 1.6 million tons in 2009 compared with 2.3 million tons in 2008. Of the 2009 amount, approximately 1.2 million tons of specialty steels consumed domestically represented stainless steel sheet and strip and electrical alloy products which the Company does not produce. Also, according to SSINA data through October 31, 2010, U.S. consumption of total specialty steel products in 2010 increased 32% from 2009 levels. The consumption of those products in the Company’s addressable market, comprising stainless steel bar, rod and wire products, increased by 44%, 89% and 14%, respectively.

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

Stainless Steel. Stainless steel, which represents the largest part of the specialty steel market, contains elements such as nickel, chrome and molybdenum that give it the unique qualities of high strength, good wear characteristics, natural attractiveness, ease of maintenance and resistance to rust, corrosion and heat. Stainless steel is used, among other applications, in the automotive, aerospace and power generation industries, as well as

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in the manufacture of food handling, health and medical, chemical processing and pollution control equipment. The increased number of applications for stainless steel has resulted in the development of a greater variety of stainless steel metallurgical grades than carbon steel.

Net sales by principal product line were as follows:

| <u>For the years ended December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|--|-------------------|-------------------|-------------------|
| Stainless steel | \$ 142,302 | \$ 98,069 | \$ 172,222 |
| Tool steel | 26,196 | 9,413 | 39,046 |
| High-strength low alloy steel | 10,310 | 9,235 | 11,936 |
| High-temperature alloy steel | 5,853 | 5,567 | 7,931 |
| Conversion service | 2,719 | 1,203 | 1,941 |
| Scrap sales and other | 2,043 | 1,420 | 2,030 |
| Total net sales | \$ 189,423 | \$ 124,907 | \$ 235,106 |

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

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

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

RAW MATERIALS

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

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

The cost of raw materials represents more than 50% of the Company's total cost of products sold in 2010 and 2009. Raw material costs can be impacted by significant price changes. Raw material prices vary based on numerous factors, including quality, and are subject to frequent market fluctuations. Future raw material prices cannot be predicted with any degree of certainty. The Company does not maintain any long-term agreements with any of its raw material suppliers.

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

ENERGY AGREEMENTS

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

CUSTOMERS

The Company's customer base increased from 568 customers at December 31, 2009 to 595 customers at December 31, 2010. The Company's five largest customers in the aggregate accounted for approximately 45% and 38% of sales for the years ended December 31, 2010 and 2009, respectively. For the year ended December 31, 2010, sales to Carpenter Technology Corporation ("CRS") accounted for 14% of the Company's sales and 17% of accounts receivable. No other customer accounted for more than 10% of the Company's sales for the year ended December 31, 2010. Sales outside of the United States approximated 5% of 2010, 10% of 2009 and 4% of 2008 sales, respectively.

BACKLOG

The Company's backlog of orders on hand, considered to be firm, as of December 31, 2010 was approximately \$69 million as compared to approximately \$36 million at the same time in 2009. The 93% increase in the backlog is primarily due to increased demand primarily caused by improving economic and credit conditions which started to impact order entry levels during the first quarter of 2010. The December 31, 2010 backlog has no promise dates beyond the year 2011. The Company's backlog may not be indicative of actual sales because certain surcharges are not determinable until the order is shipped to the customer and therefore should not be used as a direct measure of future revenue.

COMPETITION

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

Annual domestic U.S. consumption of specialty steel products of the type manufactured by the Company approximated 400,000 tons in 2009 compared with 600,000 tons in 2008. The Company chooses to restrict its participation in this market by limiting the volume of commodity stainless steel products it markets because of the highly competitive nature of the commodity business.

The Company believes that twelve companies that manufacture one or more similar specialty steel products are significant competitors. There are many smaller producing companies and material converters that are also considered to be competitors of the Company.

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High import penetration of specialty steel products, especially stainless and tool steels, also impacts the competitive nature within the United States. Unfair pricing practices by foreign producers have resulted in high import penetration into the U.S. markets in which the Company participates. According to SSINA, import penetration for the years ended December 31, 2009 and 2008 was 51% and 53%, respectively, for stainless bar, and 39% and 49%, respectively, for stainless rod. Import penetration during the first ten months of 2010 for stainless bar and rod was 49% and 36%, respectively, according to SSINA.

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

In December 2010, the Company received an import duty net payment of \$32,000, and, in December 2009, the Company received a net payment of \$551,000. Benefits awarded from the CDSOA expired on September 30, 2007. Future benefits are dependent on the amount of undistributed import duties collected as of September 30, 2007 and the relationship of Dunkirk Specialty Steel’s claim in relation to claims filed by other domestic specialty steel producers. The Company expects minimal distributions in the future.

EMPLOYEE RELATIONS

The Company considers the maintenance of good relations with its employees to be important to the successful conduct of its business. The Company has profit-sharing plans for certain salaried employees and for all of its employees represented by United Steelworkers (the “USW”) and has equity ownership programs for all of its eligible employees, in an effort to forge an alliance between its employees’ interests and those of the Company’s stockholders. At December 31, 2010, the Company had 298 employees at its Bridgeville facility, 38 employees at its Titusville facility and 182 employees at its Dunkirk facility, of which 237, 32 and 158 were USW members, respectively.

Collective Bargaining Agreements

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

| <u>Facility</u> | <u>Commencement Date</u> | <u>Expiration Date</u> |
|-----------------|--------------------------|------------------------|
| Dunkirk | November 2007 | October 2012 |
| Bridgeville | September 2008 | August 2013 |
| Titusville | October 2010 | September 2015 |

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

Employee Benefit Plans

The Company also maintains a 401(k) retirement plan for its hourly and salaried employees. Pursuant to the 401(k) plan, participants may elect to make pre-tax and after-tax contributions, subject to certain limitations imposed under the Internal Revenue Code of 1986, as amended. In addition, the Company makes periodic contributions to the 401(k) plan for the hourly employees employed at the Dunkirk and Titusville facilities, based on service. The Company makes periodic contributions for the salaried employees, the amount of the contribution is dependent upon their individual contribution to the 401(k) retirement plan.

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The Company also participates in the Steelworkers Pension Trust (the “Trust”), a multi-employer defined-benefit pension plan that is open to all hourly and salaried employees associated with the Bridgeville facility. The Company makes periodic contributions to the Trust based on hours worked at a fixed rate for each hourly employee and a fixed monthly contribution on behalf of each salaried employee.

The Company also provides group life and health insurance plans for its hourly and salaried employees.

Employee Stock Purchase Plan

Under the 1996 Employee Stock Purchase Plan, as amended (the “Plan”), the Company is authorized to issue up to 150,000 shares of Common Stock to its full-time employees, nearly all of whom are eligible to participate. Under the terms of the Plan, employees can choose as of January 1 and July 1 of each year to have up to 10% of their total earnings withheld to purchase up to 100 shares of the Company’s Common Stock each six-month period. The purchase price of the stock is 85% of the lower of its beginning-of-the-period or end-of-the-period market prices. At December 31, 2010, the Company had issued 122,933 shares of Common Stock since the plan’s inception.

ENVIRONMENTAL

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

EXECUTIVE OFFICERS

The following table sets forth, as of February 28, 2011, certain information with respect to the executive officers of the Company:

| <u>NAME (AGE)</u> | <u>EXECUTIVE OFFICER SINCE</u> | <u>POSITION</u> |
|-----------------------------|--------------------------------|---|
| Dennis M. Oates (58) | 2008 | Chairman, President and Chief Executive Officer |
| William W. Beible, Jr. (59) | 2009 | Senior Vice President of Operations |
| Paul McGrath (59) | 1996 | Vice President of Administration, General Counsel and Secretary |
| Douglas McSorley (45) | 2010 | Vice President of Finance, Chief Financial Officer and Treasurer |
| Christopher M. Zimmer (37) | 2010 | Vice President of Sales and Marketing |

Dennis M. Oates has been President and Chief Executive Officer of the Company since January 2008. Mr. Oates was named to the Company’s Board of Directors in October 2007. Mr. Oates previously served as Senior Vice

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President of the Specialty Alloys Operations of Carpenter Technology Corporation from 2003 to July 2007. Mr. Oates also served as President and Chief Executive Officer of TW Metals, Inc. from 1998 to 2003. In May 2010, the Board of Directors elected Mr. Oates to the additional position of Chairman.

William W. Beible, Jr. has been Senior Vice President of Operations of the Company since February 2009. Mr. Beible was employed by Carpenter Technology Corporation from 2006 to 2008 and served in several positions, including Vice President of Manufacturing—Specialty Alloys Operations. Mr. Beible also served as Vice President of Business Improvement and of Information Technology at P.H. Glatfelter Company, a global supplier of specialty papers and engineered products, from 2003 to 2005.

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

Douglas McSorley has been Vice President of Finance, Chief Financial Officer and Treasurer since July 2010. Mr. McSorley was previously employed as Chief Financial Officer of PSC Metals, Inc., an Icahn Enterprises L.P. scrap metal recycling company operating in the United States and Canada from 1999 to 2009. He joined a predecessor company to PSC as Controller in 1994, after serving five years with Deloitte & Touche LLP in Ontario, Canada, where he worked as a Chartered Accountant with a broad spectrum of industrial clients.

Christopher M. Zimmer has been Vice President of Sales and Marketing since April 2008. Mr. Zimmer previously served as Vice President of Sales and Marketing for Schmoltz+Bickenbach USA from 1995 to 2008. He held positions of increasing responsibility including inside sales, commercial manager—stainless bar, general manager—nickel alloy products, and National Sales Manager.

PATENTS AND TRADEMARKS

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

AVAILABLE INFORMATION

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

ITEM 1A. RISK FACTORS

The Company's business and results of operations are subject to a wide range of substantial business and economic factors including, but not limited to, the factors discussed below, many of which are not within the Company's control. Other factors of which the Company is unaware or which the Company does not consider to be material at this time also may impact the Company's business and results of operations. See the information

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under the heading “Forward-Looking Information Safe Harbor” in Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations, of this Annual Report on Form 10-K.

SIGNIFICANT CUSTOMERS AND CONCENTRATED CUSTOMER BASE

Net sales to the Company’s largest 2010 customer accounted for 14% of 2010 sales. The accounts receivable balance from this largest customer comprised approximately 17% of total accounts receivable at December 31, 2010. An adverse change in, or termination of, the Company’s relationship with one or more of its major customers or one or more of its market segments could have a material adverse effect upon the Company. See the information under the heading “Customers” in Item 1, Business, of this Annual Report on Form 10-K.

COMPETITION

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

AEROSPACE MARKET

Approximately 35% of the Company’s sales and 27% of tons shipped represent products sold to customers in the aerospace market in 2010. The aerospace market is historically cyclical due to both external and internal market factors. These factors include general economic conditions, diminished credit availability, airline profitability, demand for air travel, age of fleets, varying fuel and labor costs, price competition, and international and domestic political conditions such as military conflict and the threat of terrorism. The length and degree of cyclical fluctuation can be influenced by any one or a combination of these factors and therefore are difficult to predict with certainty. A downturn in the aerospace industry would adversely affect the demand for products and/or the prices at which the Company is able to sell its products, and its results of operations, business and financial condition could be materially adversely affected.

SUPPLY OF RAW MATERIALS AND COST OF RAW MATERIALS

The Company purchases scrap metal and alloy additives, principally nickel, chrome and molybdenum, for its melting operation. A substantial portion of the alloy additives is available only from foreign sources, some of which are located in countries that may be subject to unstable political and economic conditions. Those conditions might disrupt supplies or affect the prices of the raw materials used by the Company. The Company maintains sales price surcharges to help offset the impact of raw material price fluctuations.

The Company does not maintain long-term supply agreements with any of its raw material suppliers. If its supply of raw materials were interrupted, the Company might not be able to obtain sufficient quantities of raw materials, or obtain sufficient quantities of such materials at satisfactory prices, which, in either case, could adversely affect the Company’s results of operations. In addition, significant volatility in the price of the Company’s principal raw materials could adversely affect the Company’s financial results and there can be no assurance that the raw material surcharge mechanism employed by the Company will completely offset immediate changes in the Company’s raw material costs. See the information under the headings “Raw Materials” in Item 1, Business, and “Liquidity and Capital Resources” and “Future Outlook” in Item 7, Management’s Discussion and Analysis of Financial Condition and Results of Operations, of this Annual Report on Form 10-K.

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GLOBAL ECONOMIC AND MARKET FACTORS

Our results of operations are affected directly by the level of business activity of our customers, which in turn is affected by global economic and market factors impacting the industries and markets that they serve. We are susceptible to macroeconomic downturns in the United States and abroad that may affect the general economic climate, our performance and the demand of our customers. The continuing turmoil in the global financial system has had and may continue to have, an impact on our business and our financial condition. In addition to the impact that the global financial crisis has already had, we may face significant challenges if conditions in the financial markets deteriorate. There can be no assurance that global economic and market conditions will not adversely impact our results of operations, cash flow or financial position in the future.

RELIANCE ON ENERGY AGREEMENTS

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

KEY PERSONNEL

The Company depends on the continued service, availability and ability to attract skilled personnel, including members of our executive management team, management, metallurgists, maintenance and production positions. The inability of the Company and industry to attract and retain such people may adversely impact our ability to fill existing roles and support growth. Further, the loss of key personnel could adversely affect our ability to perform until suitable replacements are found.

LABOR MATTERS

The Company has 427 employees out of a total of 518 who are covered under collective bargaining agreements. There can be no assurance that the Company will be successful in timely concluding collective bargaining agreements with the USW to succeed the agreements that expire.

RELIANCE ON CRITICAL MANUFACTURING EQUIPMENT

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

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

The Company owns its Bridgeville facility, which consists of approximately 760,000 square feet of floor space and the Company’s executive offices on approximately 74 acres. The Bridgeville facility contains melting, remelting, conditioning, rolling, annealing and various other processing equipment. Substantially all products shipped from the Bridgeville facility are processed through its melt shop and universal rolling mill operations.

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

The Company owns its Dunkirk facility, which consists of approximately 680,000 square feet of floor space on approximately 81 acres. The Dunkirk facility processes semi-finished billet and bar stock through one or more of its four rolling mills, a high temperature annealing facility and/or a round bar facility. The products are then finished and shipped as finished bar, rod and wire products.

Specialty steel production is a capital-intensive industry. The Company believes that its facilities and equipment are suitable for its present needs. The Company believes, however, that it will continue to require capital from time to time to add new equipment and to repair or replace existing equipment to remain competitive and to enable it to manufacture quality products and provide delivery and other support service assurances to its customers. See *Capital Expenditures and Investments*, page 18.

ITEM 3. LEGAL PROCEEDINGS

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

ITEM 4. [Removed and Reserved]

PART II

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

At December 31, 2010, a total of 7,094,314 shares of the Company's Common Stock, par value \$.001 per share, were issued and held by approximately 154 holders of record. There were 282,850 shares of the issued Common Stock of the Company held in treasury at December 31, 2010.

Certain holders of Common Stock and the Company are party to a stockholder agreement. That agreement maintains in effect certain registration rights granted to non-management stockholders and provides to them two demand registration rights exercisable at any time upon written request for the registration of shares of Common Stock having an aggregate net offering price of at least \$5.0 million.

PRICE RANGE OF COMMON STOCK

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

| | 2010 | | 2009 | |
|----------------|---------|---------|---------|---------|
| | High | Low | High | Low |
| First quarter | \$24.09 | \$17.07 | \$16.32 | \$ 7.98 |
| Second quarter | \$25.37 | \$15.83 | \$16.86 | \$ 9.48 |
| Third quarter | \$25.06 | \$15.68 | \$21.23 | \$14.68 |
| Fourth quarter | \$33.50 | \$23.80 | \$19.41 | \$14.48 |

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EQUITY COMPENSATION PLAN INFORMATION

Securities authorized for issuance under equity compensation plans at December 31, 2010 are as follows:

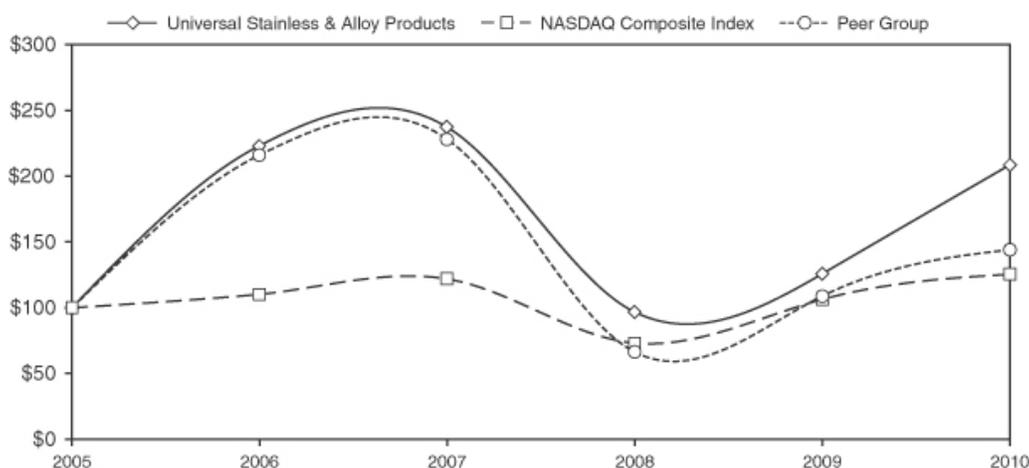
| <u>Plan Category</u> | <u>Number of shares to be issued upon exercise of outstanding options</u> | <u>Weighted-average exercise price of outstanding options</u> | <u>Number of shares remaining available for future issuance under equity compensation plans ^A</u> |
|--|---|---|--|
| Equity compensation plans approved by security holders | 605,600 | \$ 22.02 | 481,385 |
| Equity compensation plans not approved by security holders | — | — | — |
| Total | 605,600 | \$ 22.02 | 481,385 |

^A Includes 454,318 shares of Common Stock on stock options not issued under the Stock Incentive Plan and 27,067 available under the 1996 Employee Stock Purchase Plan, as amended.

PERFORMANCE GRAPH

The performance graph below compares the cumulative total shareholder return on the Company's stock with the cumulative total return on the equity securities of NASDAQ Composite Index and a peer group selected by the Company. The peer group consists of domestic specialty steel producers: Allegheny Technologies, Inc.; Brush Engineered Materials Inc.; Carpenter Technology Corp.; Haynes International Inc.; and RTI International Metals, Inc. The graph assumes an investment of \$100 on December 31, 2005 reinvestment of dividends, if any, on the date of dividend payment and the peer group is weighted by each company's market capitalization. The performance graph represents past performance and should not be considered to be an indication of future performance.

Comparison of 5-Year Cumulative Total Shareholder Return among Universal Stainless & Alloy Products, Inc., the NASDAQ Composite Index and a Peer Group



| <u>Company/Peer/Market</u> | <u>Fiscal Year Ending December 31,</u> | | | | | |
|--|--|-------------|-------------|-------------|-------------|-----------------|
| | <u>2005</u> | <u>2006</u> | <u>2007</u> | <u>2008</u> | <u>2009</u> | <u>2010</u> |
| Universal Stainless & Alloy Products, Inc. | \$100.00 | \$223.20 | \$237.13 | \$96.60 | \$125.73 | \$208.53 |
| Peer Group | 100.00 | 215.83 | 228.07 | 66.24 | 108.71 | 143.89 |
| NASDAQ Composite Index | 100.00 | 110.25 | 121.88 | 73.10 | 106.22 | 125.36 |

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PREFERRED STOCK

The Company's Certificate of Incorporation provides that the Company may, by vote of its Board of Directors, issue up to 1,980,000 shares of Preferred Stock. The Preferred Stock may have rights, preferences, privileges and restrictions thereon, including dividend rights, dividend rates, conversion rights, voting rights, terms of redemption, redemption prices, liquidation preferences and the number of shares constituting any series or designation of such series, without further vote or action by the stockholders. The issuance of Preferred Stock may have the effect of delaying, deferring or preventing a change in control of the Company without further action by the stockholders and may adversely affect the voting and other rights of the holders of Common Stock. The issuance of Preferred Stock with voting and conversion rights may adversely affect the voting power of the holders of Common Stock, including the loss of voting control to others. The Company has no outstanding Preferred Stock and has no current plans to issue any of the authorized Preferred Stock.

DIVIDENDS

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

ITEM 6. SELECTED FINANCIAL DATA

| <u>For the years ended December 31,</u> | <u>2010</u> | <u>2009</u> | <u>2008</u> | <u>2007</u> | <u>2006</u> |
|---|------------------|-------------|-------------|-------------|-------------|
| <i>(dollars in thousands, except per share amounts)</i> | | | | | |
| SUMMARY OF OPERATIONS | | | | | |
| Net sales | \$189,423 | \$124,907 | \$235,106 | \$229,936 | \$203,873 |
| Operating income (loss) | 20,423 | (4,657) | 19,092 | 33,407 | 32,359 |
| Net income (loss) | 13,242 | (2,958) | 13,950 | 22,504 | 20,590 |
| FINANCIAL POSITION AT YEAR-END | | | | | |
| Cash and cash equivalents | \$ 34,944 | \$ 42,349 | \$ 14,812 | \$ 10,648 | \$ 2,909 |
| Total assets | 212,668 | 181,714 | 182,944 | 164,296 | 155,287 |
| Long-term debt | 7,990 | 10,823 | 1,046 | 1,453 | 17,228 |
| Stockholders' equity | 159,623 | 144,226 | 145,700 | 129,602 | 104,654 |
| COMMON SHARE DATA | | | | | |
| Basic earnings (loss) per share | \$ 1.95 | \$ (0.44) | \$ 2.08 | \$ 3.39 | \$ 3.19 |
| Diluted earnings (loss) per share | 1.93 | (0.44) | 2.05 | 3.32 | 3.11 |

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

ITEMS AFFECTING COMPARABILITY OF RESULTS

The Company recorded net income for the year ended December 31, 2010 of \$13.2 million. These results include a favorable third quarter 2010 inventory adjustment of \$976,000 for additional metal recovered as a result of a capital project streamlining the scrap loading area, and a \$647,000 increase in stock option compensation as a result of changes in estimated forfeiture rates and to fully expense vested options.

The Company recorded a net loss of \$3.0 million for the year ended December 31, 2009. These results include a \$742,000 negative tax adjustment primarily for the reconciliation of tax balances at June 30, 2009 to the 2008 tax returns prepared during the second quarter 2009 and the following unusual charges (totaling \$6.0 million pre-tax) recorded during the three-month period ended March 31, 2009, primarily due to the deepening recession and economic uncertainty:

- \$1.9 million increase to the bad debt reserve due to the inability of a privately held service center customer to pay amounts owed on 2008 purchases and a related \$0.5 million increase to inventory reserves on “made to order” specialty material produced for the same customer and held at our plant due to their inability to pay for the 2008 purchases. Once the Company determined that the customer could not pay for either the 2008 purchases or the held material, the held material was reclassified to stock inventory, and because the material was unique to that specific customer and was unlikely to be shipped, inventory reserves were increased by \$0.5 million;
- \$1.5 million due to a decline in raw material values and the consumption of high cost material during the quarter;
- \$1.0 million write-down of stock inventory;
- \$0.9 million attributed to the reduction of operating levels; and
- \$0.2 million resulting from a 20% reduction in salaried employees.

RESULTS OF OPERATIONS

Universal Stainless & Alloy Products, Inc., headquartered in Bridgeville, Pa., manufactures and markets a broad line of semi-finished and finished specialty steels, including stainless steel, tool steel and certain other alloyed steels. The Company’s products are sold to rollers, forgers, service centers, OEMs and wire redrawers.

An analysis of the Company’s operations is as follows:

| | 2010 | | 2009 | | 2008 | |
|---|-----------|-------|------------|--------|-----------|-------|
| | Amount | % | Amount | % | Amount | % |
| For the years ended December 31, | | | | | | |
| <i>(dollars in thousands; percentages are of total net sales)</i> | | | | | | |
| NET SALES | | | | | | |
| Stainless steel | \$142,302 | 75.1% | \$ 98,069 | 78.5% | \$172,222 | 73.2% |
| Tool steel | 26,196 | 13.8 | 9,413 | 7.5 | 39,046 | 16.6 |
| High-strength low alloy steel | 10,310 | 5.5 | 9,235 | 7.4 | 11,936 | 5.1 |
| High-temperature alloy steel | 5,853 | 3.1 | 5,567 | 4.5 | 7,931 | 3.4 |
| Conversion services | 2,719 | 1.4 | 1,203 | 1.0 | 1,941 | 0.8 |
| Scrap sales and other | 2,043 | 1.1 | 1,420 | 1.1 | 2,030 | 0.9 |
| Total net sales | 189,423 | 100.0 | 124,907 | 100.0 | 235,106 | 100.0 |
| Total cost of products sold | 155,651 | 82.2 | 117,901 | 94.4 | 204,929 | 87.2 |
| Selling and administrative expenses | 13,349 | 7.0 | 11,663 | 9.3 | 11,085 | 4.7 |
| Operating income (loss) | \$ 20,423 | 10.8% | \$ (4,657) | (3.7)% | \$ 19,092 | 8.1% |

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2010 Results as Compared to 2009

Net sales for the year ended December 31, 2010 increased \$64.5 million as compared to 2009. The increase is primarily due to a 54% increase in tonnage shipped as well as price increases realized in 2010. The year over year increase in net sales due to increased shipment volume was \$52.7 million. The increase in shipments is attributed to improved economic conditions and market demand which continued to recover throughout 2010 as compared to 2009. During 2009, weaker economic conditions resulted in “destocking” in the service center industry to bring inventory levels in line with significantly lower end-user demand.

Cost of products sold, as a percentage of net sales, was 82.2% and 94.4% for 2010 and 2009, respectively. The results for 2010 and 2009 include a \$976,000 favorable inventory adjustment in 2010, as described above, and \$3.9 million of the 2009 unusual charges outlined above, representing 0.5% and 3.1% of net sales, respectively. Excluding these adjustments, gross margin was 17.3% of sales in 2010 compared to 8.7% for 2009. The improved proportion of cost of sales to sales in 2010 is also attributable to fixed operating costs being spread over higher production volumes as a result of increased product orders.

Net sales by market segment are as follows:

| For the years ended December 31, <i>(dollars in thousands; percentages are of total net sales)</i> | 2010 | | 2009 | | 2008 | |
|---|------------------|---------------|------------------|---------------|------------------|---------------|
| | Amount | % | Amount | % | Amount | % |
| Service centers | \$ 88,948 | 47.0% | \$ 50,355 | 40.3% | \$110,889 | 47.2% |
| Forgers | 41,793 | 22.0 | 39,821 | 31.9 | 52,551 | 22.4 |
| Rerollers | 36,515 | 19.3 | 12,174 | 9.7 | 41,660 | 17.7 |
| Original equipment manufacturers | 13,800 | 7.3 | 16,089 | 12.9 | 18,955 | 8.1 |
| Wire redrawers | 4,132 | 2.2 | 3,845 | 3.1 | 7,129 | 3.0 |
| Conversion services | 2,719 | 1.4 | 1,203 | 1.0 | 1,941 | 0.8 |
| Scrap sales and other | 1,516 | 0.8 | 1,420 | 1.1 | 1,981 | 0.8 |
| Net sales | <u>\$189,423</u> | <u>100.0%</u> | <u>\$124,907</u> | <u>100.0%</u> | <u>\$235,106</u> | <u>100.0%</u> |
| Tons shipped | <u>43,373</u> | | <u>28,182</u> | | <u>45,679</u> | |

Selling and administrative expenses increased in 2010 to \$13.3 million, or 7.0% of sales, from \$11.7 million, or 9.3% of sales in 2009. The increased cost in 2010 is primarily due to a \$2.1 million increase in accrued variable compensation, the \$647,000 increase in stock option compensation, as described above, and by a \$408,000 increase in salary and benefit expenses in 2010, which were partially offset by \$2.1 million of the 2009 unusual charges outlined above.

The effective income tax rate in 2010 was 34.0% as compared to a benefit of (27.0)% for 2009. The effective income tax rate in the current year reflects taxable income and benefits from the domestic manufacturing deduction, whereas the prior year reflected a net operating loss, benefits related to a federal loss carryback and state loss carryforwards. The Company has \$2.0 million of state tax carryforwards at December 31, 2010 and \$2.2 million at December 31, 2009 that represent New York Empire Zone tax credits with no expiration date and various state net operating loss carryforwards expiring in 2029. The Company believes it will generate sufficient income in addition to taxable income generated from the reversal of its temporary differences to utilize these tax credits and losses.

In 2009, the Company recorded a \$742,000 negative tax adjustment primarily for the reconciliation of tax balances to 2008 federal and state income tax returns. The Company determined that \$370,000 of this adjustment related to prior periods and was not considered material to any prior period or to 2009 that would require the restatement of prior period financial statements. The remaining \$172,000 of adjustments consisted of \$48,000 relating to 2009 tax provision-to-tax return adjustments to properly report state tax credits, and the remaining \$124,000 related to other timing differences, primarily state bonus depreciation adjustments.

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2009 Results as Compared to 2008

The decrease in net sales in 2009 is primarily due to a 38% decline in tonnage shipped, partially offset by base price increases realized in 2009. The lower demand for the Company's products was primarily a result of an oversupply of product within the service center industry resulting from deteriorating economic and credit conditions which started to impact order entry levels during the fourth quarter of 2008.

Cost of products sold, as a percentage of net sales, increased in 2009 as compared to 2008. Cost of products sold for 2009 include \$3.9 million of the unusual charges outlined above, representing 3.1% of net sales. The remaining increase is primarily due to higher operation costs resulting from lower production volumes.

Selling and administrative expenses increased in 2009 to \$11.7 million, or 9.3% of net sales from \$11.1 million, or 4.7% of net sales in 2008. The increased cost in 2009 relates to \$2.1 million of the unusual charges outlined above. These costs were partially offset by an \$867,000 decrease in labor costs, primarily resulting from a 20% workforce reduction implemented in March 2009 and a reduction in the accrual for incentive compensation. In addition, other discretionary expenditures were curtailed as a result of lower production volumes.

In 2009, as previously discussed, the Company recorded a \$742,000 negative tax adjustment primarily for the reconciliation of tax balances to 2008 federal and state income tax returns. The effective income tax benefit in 2009 was (27%) compared with an effective income tax rate of 29.9% in 2008. The effective income tax rate in 2009 reflected a net operating loss and benefits related to a federal loss carryback and state loss carryforwards, whereas the prior year had taxable income and benefited from the domestic manufacturing deduction and investment tax credits generated from capital improvements made at the Dunkirk facility in 2008.

Business Segment Results

The Company is comprised of three operating locations and one corporate headquarters. For segment reporting, the Bridgeville and Titusville facilities have been aggregated into one reportable segment, Universal Stainless & Alloy Products. The Universal Stainless & Alloy Products manufacturing process involves melting, remelting, treating and hot and cold rolling of semi-finished and finished specialty steels. Dunkirk Specialty Steel's manufacturing process involves hot rolling and finishing specialty steel bar, rod and wire products.

UNIVERSAL STAINLESS & ALLOY PRODUCTS SEGMENT

An analysis of the segment's operations is as follows:

| For the years ended December 31, <i>(dollars in thousands; percentages are of total net sales)</i> | 2010 | | 2009 | | 2008 | |
|---|------------------|--------------|-------------------|---------------|------------------|--------------|
| | Amount | % | Amount | % | Amount | % |
| NET SALES | | | | | | |
| Stainless steel | \$ 99,092 | 57.2% | \$ 71,670 | 66.2% | \$121,612 | 58.9% |
| Tool steel | 25,325 | 14.6 | 9,146 | 8.4 | 37,631 | 18.2 |
| High-strength low alloy steel | 2,091 | 1.2 | 3,017 | 2.8 | 3,881 | 1.9 |
| High-temperature alloy steel | 2,427 | 1.4 | 1,988 | 1.8 | 2,977 | 1.4 |
| Conversion service | 2,110 | 1.2 | 763 | 0.7 | 1,278 | 0.6 |
| Scrap sales and other | 1,928 | 1.1 | 1,391 | 1.3 | 1,875 | 0.9 |
| | <u>132,973</u> | <u>76.7</u> | <u>87,975</u> | <u>81.2</u> | <u>169,254</u> | <u>81.9</u> |
| Intersegment | <u>40,321</u> | <u>23.3</u> | <u>20,344</u> | <u>18.8</u> | <u>37,384</u> | <u>18.1</u> |
| Total net sales | <u>173,294</u> | <u>100.0</u> | <u>108,319</u> | <u>100.0</u> | <u>206,638</u> | <u>100.0</u> |
| Material cost of sales | <u>85,507</u> | <u>49.3</u> | <u>49,592</u> | <u>45.8</u> | <u>114,930</u> | <u>55.6</u> |
| Operation cost of sales | <u>61,428</u> | <u>35.5</u> | <u>52,656</u> | <u>48.6</u> | <u>68,415</u> | <u>33.1</u> |
| Selling and administrative expenses | <u>9,048</u> | <u>5.2</u> | <u>8,467</u> | <u>7.8</u> | <u>7,613</u> | <u>3.7</u> |
| Operating income (loss) | <u>\$ 17,311</u> | <u>10.0%</u> | <u>\$ (2,396)</u> | <u>(2.2)%</u> | <u>\$ 15,680</u> | <u>7.6%</u> |

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Net sales for the year ended December 31, 2010 increased by \$65.0 million, or 60.0%, in comparison to the year ended December 31, 2009 primarily due to a 57.5% increase in tonnage shipped, and base price increases realized in 2010. The increase in shipments is attributed to improved economic conditions and market demand which continued to recover throughout 2010 as compared to 2009. During 2009, weaker economic conditions resulted in 'destocking' in the service center industry to bring inventory levels in line with significantly lower end-user demand. A 144% increase in reroller shipments was accompanied by a 111% increase in service center plate shipments, a 23.1% increase in service center long products shipments, and a 10.5% increase in forger shipments. Shipments of service center plate products, petrochemical products, aerospace products and power generation products increased 111%, 70%, 47% and 41%, respectively, over 2009.

Net sales for the year ended December 31, 2009 decreased by \$98.3 million, or 47.6%, in comparison to the year ended December 31, 2008 primarily due to a 37% decline in tonnage shipped, partially offset by base price increases realized in 2009. Shipments of service center plate products, petrochemical products, aerospace products and power generation products decreased 64%, 43%, 29% and 14%, respectively, over 2008.

Operating income for year ended December 31, 2010 increased by \$19.7 million compared to the year ended December 31, 2009. The 2010 results include a \$976,000 favorable inventory adjustment, as described above, and \$5.0 million of the 2009 unusual charges outlined above, representing 0.6% and 4.6% of net sales, respectively. Excluding the impact of the unusual charges, material costs, as a percentage of sales, increased to 49.9% from 43.7% for the years ended December 31, 2010 and 2009, respectively, as a result of higher material costs in the year 2010, and operation costs, as a percentage of sales, decreased to 35.4% from 48.0% for the same years, respectively. The improved proportion of cost of sales to sales in 2010 is also attributable to fixed operating costs being spread over higher production volumes as a result of increased product orders.

Operating income for the year ended December 31, 2009 decreased by \$18.1 million from 2008 primarily due to the impact of the unusual charges and lower production volumes. The 2009 results include \$5.0 million of the unusual charges outlined above, representing 4.6% of net sales. Excluding the impact of the unusual charges, material costs, as a percentage of sales, dropped from 55.6% to 43.7% reflecting a better alignment of material costs and related sales prices and yield improvements recognized on 2009 shipments of semi-finished products.

DUNKIRK SPECIALTY STEEL SEGMENT

An analysis of the segment's operations is as follows:

| For the years ended December 31, <i>(dollars in thousands; percentages are of total net sales)</i> | 2010 | | 2009 | | 2008 | |
|---|-----------------|--------------|-------------------|---------------|-----------------|--------------|
| | Amount | % | Amount | % | Amount | % |
| NET SALES | | | | | | |
| Stainless steel | \$43,211 | 76.3% | \$26,399 | 70.9% | \$50,610 | 76.4% |
| High-strength low alloy steel | 8,219 | 14.5 | 6,218 | 16.7 | 8,055 | 12.2 |
| High-temperature alloy steel | 3,426 | 6.1 | 3,579 | 9.6 | 4,954 | 7.5 |
| Tool steel | 871 | 1.5 | 267 | 0.7 | 1,415 | 2.1 |
| Conversion services | 609 | 1.1 | 440 | 1.2 | 663 | 1.0 |
| Scrap sales and other | 114 | 0.2 | 29 | 0.1 | 155 | 0.2 |
| | 56,450 | 99.7 | 36,932 | 99.2 | 65,852 | 99.4 |
| Intersegment | 150 | 0.3 | 313 | 0.8 | 396 | 0.6 |
| Total net sales | 56,600 | 100.0 | 37,245 | 100.0 | 66,248 | 100.0 |
| Material cost of sales | 33,003 | 58.3 | 23,221 | 62.3 | 40,899 | 61.7 |
| Operation cost of sales | 15,000 | 26.5 | 13,089 | 35.2 | 18,465 | 27.9 |
| Selling and administrative expense | 4,301 | 7.6 | 3,196 | 8.6 | 3,472 | 5.2 |
| Operating income (loss) | \$ 4,296 | 7.6% | \$ (2,261) | (6.1)% | \$ 3,412 | 5.2% |

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Net sales for the year ended December 31, 2010 increased by \$19.4 million, or 52.0%, in comparison to the year ended December 31, 2009 primarily due to a 35% increase in tonnage shipped and base price increases realized in 2010. The increase in shipments is attributed to improved economic conditions and market demand which continued to recover throughout 2010 as compared to 2009. During 2009, weaker economic conditions resulted in 'destocking' in the service center industry to bring inventory levels in line with significantly lower end-user demand. Sales to service centers in 2010 comprised 82.0% of external sales and 76.6% of external shipments. Service center sales increased by \$17.5 million over the similar 2009 period. Shipments of aerospace products, general industrial products and petrochemical products increased 50%, 41% and 22%, respectively, over 2009.

Net sales for the year ended December 31, 2009 decreased by \$31.0 million, or 44.5%, in comparison to the year ended December 31, 2008 primarily due to a 26% decline in tonnage shipped, partially offset by base price increases realized in 2009. Shipments of general industrial products, petrochemical products and aerospace products decreased 34%, 31% and 19%, respectively, over 2008.

Operating income increased by \$6.6 million for the year ended December 31, 2010 as compared to the 2009 year. The results for the year ended December 31, 2009 include \$1.0 million of the unusual charges outlined above, representing 2.9% of net sales. Excluding the impact of the unusual charges, material costs, as a percentage of sales, decreased to 58.3% from 60.4% of sales for the years ended December 31, 2010 and 2009, respectively, and operation costs, as a percentage of sales, decreased to 26.5% from 34.7% for the same years, respectively. This improvement is partially attributable to fixed operating costs being spread over higher production volumes.

Operating income for the year ended December 31, 2009 decreased by \$5.7 million compared to the similar period in 2008 primarily due to the impact of the unusual charges and lower production volumes. The 2009 results include \$1.0 million of the unusual charges outlined above, representing 2.5% of net sales.

Liquidity and Capital Resources

The Company has financed its operating activities through cash on hand at the beginning of the period and cash provided by operations. Working capital increased \$12.5 million to \$110.1 million at December 31, 2010 compared to \$97.6 million at December 31, 2009. Accounts receivable increased \$12.2 million as a result of increased sales for the three-month period ended December 31, 2010 in comparison to the three-month period ended December 31, 2009. The \$28.4 million increase in inventory at December 31, 2010 compared to December 31, 2009 is due principally to an 88% increase in the volume of work-in-process applied to inventory in response to the rise in the Company's backlog. The backlog increased from \$36 million at December 31, 2009 to \$69 million at December 31, 2010, an increase of 93%. The raw material inventory increased 29% due to significantly higher raw material purchase prices partially offset by an 8% decrease in the volume of raw material on hand. The Company received a \$4.1 million federal income tax refund in 2010. Accounts payable increased \$12.2 million, or 157%, related to the increase in production levels and raw material price increases. Accrued employment costs increased \$4.3 million, comprised of increases of \$3.9 million for incentive compensation and profit sharing accruals and \$383,000 for accrued wages, as compared to December 31, 2009, which resulted from increased profitability and production levels.

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The Company generated cash from operations of \$1.3 million, \$27.9 million, and \$16.1 million in the years ended December 31, 2010, 2009 and 2008, respectively. Cash received from sales of \$177.2 million, \$139.5 million, and \$228.7 million for the years ended December 31, 2010, 2009 and 2008, respectively, represent the primary source of cash from operations. An analysis of the primary uses of cash is as follows:

| For the years ended December 31, <i>(dollars in thousands; percentages are of total uses of cash)</i> | 2010 | | 2009 | | 2008 | |
|--|------------------|---------------|------------------|---------------|------------------|---------------|
| | Amount | % | Amount | % | Amount | % |
| Raw material purchases | \$ 93,625 | 53.2% | \$ 40,699 | 36.4% | \$111,212 | 52.3% |
| Employment costs | 32,768 | 18.6 | 27,840 | 25.0 | 38,380 | 18.1 |
| Utilities | 14,240 | 8.1 | 14,891 | 13.3 | 19,915 | 9.4 |
| Capital expenditures | 7,481 | 4.3 | 12,394 | 11.1 | 12,905 | 6.0 |
| Other | 27,762 | 15.8 | 15,746 | 14.2 | 30,166 | 14.2 |
| Total uses of cash | <u>\$175,876</u> | <u>100.0%</u> | <u>\$111,570</u> | <u>100.0%</u> | <u>\$212,578</u> | <u>100.0%</u> |

Cash used for raw material purchases increased in 2010 in comparison to 2009 primarily due to increased production and higher purchase prices. The Company continuously monitors market price fluctuations of its key raw materials.

The following table reflects the average market values per pound for key raw materials for selected months during the last three-year period.

| | December 2010 | June 2010 | December 2009 | June 2009 | December 2008 | June 2008 |
|--------------|------------------|--------------|------------------|--------------|------------------|--------------|
| Nickel | \$ 10.94 | \$ 8.79 | \$ 7.74 | \$ 6.79 | \$ 4.39 | \$10.23 |
| Chrome | \$ 1.31 | \$ 1.33 | \$ 0.89 | \$ 0.78 | \$ 0.96 | \$ 2.19 |
| Molybdenum | \$ 16.17 | \$14.73 | \$ 11.47 | \$10.34 | \$ 9.85 | \$33.22 |
| Carbon scrap | \$ 0.19 | \$ 0.20 | \$ 0.15 | \$ 0.10 | \$ 0.11 | \$ 0.34 |

The market values for these raw materials and others continue to fluctuate based on supply and demand, market disruptions and other factors. The Company maintains sales price surcharge mechanisms, priced at time of shipment, to mitigate the risk of substantial raw material cost fluctuations. There can be no assurance that these sales price adjustments will completely offset the Company's raw material.

The average price of nickel was \$9.89, \$6.65 and \$9.58 per pound for the years 2010, 2009 and 2008, respectively. The average price of chrome was \$1.26, \$0.82 and \$1.84 per pound for the years 2010, 2009 and 2008, respectively. The average price of carbon scrap was \$0.19, \$0.11 and \$0.23 per pound for the years 2010, 2009 and 2008, respectively. The significantly higher prices in 2008 were believed to be due to increased demand from foreign and domestic sources coupled with supply volatility. The global economic and market factors that impacted the fourth quarter of 2008 and the first quarter of 2009 weakened demand for raw materials and depressed prices. Prices for raw materials have continued to increase since the second quarter of 2009.

While the material surcharge mechanism is designed to offset modest fluctuations in raw material prices, it cannot immediately absorb significant spikes in raw material prices. There can be no assurance that the raw material surcharge mechanism will completely offset immediate changes in the Company's raw material costs. A material decline in raw material prices within a short period of time could have a material adverse effect on the financial results of the Company.

Cash payments in 2010 for employment costs were \$4.9 million higher than 2009 primarily due to higher production volumes and higher payouts under the Company's profit-sharing plan and variable compensation. The decrease in employment costs in 2009 compared to 2008 were primarily due to lower production volumes and lower payouts under the Company's profit-sharing plans, which were partially offset by higher wage and benefit rates.

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Utility costs for 2010 were flat compared to 2009 costs as a result of a reduction in natural gas costs that were offset by an increase in electricity costs. The electricity increase in 2010 was a result of higher usage related to higher production levels, partially offset by lower rates. The overall natural gas cost was lower in 2010 largely a result of lower gas prices, partially offset by increased consumption compared to 2009.

Other uses of cash, the majority of which is cash for production supplies, plant maintenance, outside conversion services, insurance and freight, increases or decreases in relation to production volume. Maintenance expenses in 2009 decreased by \$3.6 million in comparison to 2008, followed by a \$2.4 million increase in 2010 in response to increased production levels. In addition, payments for federal and state income taxes, net of refunds received decreased \$7.7 million in 2009 as a result of tax payments of \$6.3 million in 2008 compared to a net refund of \$1.4 million in 2009. Income tax payments increased by \$3.1 million in 2010 as a result of net taxes paid in 2010 of \$1.8 million compared with the \$1.4 million refund in 2009.

Capital Expenditures and Investments. The Company's capital expenditures were approximately \$7.4 million and \$12.4 million in 2010 and 2009, respectively. The 2010 expenditures included \$2.6 million for the Bridgeville melt shop project and several other smaller projects, while the 2009 expenditures included \$9.6 million for the melt shop project with the balance of the 2009 expenditures primarily used for the addition of annealing and finishing equipment.

In January 2009, the Company announced that it would invest \$13 million in its Bridgeville melt shop. The investment includes major upgrades in equipment, automation and plant layout designed to: cut production cycle times and customer lead times; improve on-time delivery performance; increase material yields; reduce operating costs and enhance working capital management. The spending is substantially complete, and the Company funded the investment with the Term Loan (as defined below).

Capital expenditures are expected to approximate \$10 to \$15 million in 2011, of which \$5.6 million is for remelt expansion.

Capital Resources Including Off-Balance Sheet Arrangements. The Company does not maintain off-balance sheet arrangements, nor does it participate in non-exchange traded contracts requiring fair value accounting treatment, or material related-party transaction arrangements.

PNC Credit Agreement. During 2009, the Company entered into a new unsecured credit agreement with PNC Bank (the "PNC Credit Agreement"), which provides for a \$12.0 million term loan scheduled to mature on February 28, 2014 ("Term Loan") and a \$15.0 million revolving credit facility with a term expiring on June 30, 2012 (the "PNC Line"). At December 31, 2010, the Company had its entire PNC Line available for borrowings.

The Company also executed an interest rate swap with PNC Bank, with a notional amount of \$12.0 million, to convert the LIBOR floating rate under the Term Loan to a fixed interest rate for the life of the loan. Under the agreement, the Company's interest rate is currently fixed at 4.515%. The notional amount of the interest rate swap decreases ratably over its term, as does the Term Loan, and was \$10.2 million at December 31, 2010. The Company recorded a liability of \$287,000, equal to the fair value of the swap agreement at December 31, 2010. This fair value, net of tax, is reported as accumulated other comprehensive loss within stockholders' equity. Changes in market interest rates will be reflected as changes to the fair value of the corresponding liability or receivable, although the Company's actual interest rate payments will continue to be fixed at 4.515%.

The Company pays a commitment fee on the unused portion of the PNC Line of 0.25%, provided it maintains certain financial ratios. Interest on borrowings under the PNC Line is based on short-term market rates, which may be further adjusted, based upon the Company maintaining certain financial ratios. The Company is required to be in compliance with three financial covenants: a minimum leverage ratio of 2.5:1.0 or less; a minimum debt service ratio of 2.5:1.0 or greater; and a minimum tangible net worth of \$159.6 million as of December 31, 2010. The Company was in compliance with all financial ratios and restrictive covenants it is required to maintain under the credit agreement at December 31, 2010. The Company believes it will maintain compliance with the financial covenants in effect throughout 2011.

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Government Financing Programs. The Company maintains two loan agreements with the Commonwealth of Pennsylvania's Department of Commerce, originally aggregating \$600,000. A \$200,000 15-year loan bears interest at 5% per annum with the term ending in 2011, and a \$400,000 20-year loan bears interest at 6% per annum with the term ending in 2016. In 2002, Dunkirk Specialty Steel issued two ten-year, 5% interest-bearing notes payable to the New York Job Development Authority for the combined amount of \$3.0 million. As of December 31, 2010, the total principal balance of all government-financed debt instruments is \$0.6 million.

Share-based Financing Activity. The Company issued 50,415 and 40,820 shares of its Common Stock for the years ended December 31, 2010 and 2009, respectively, through its two share-based compensation plans. In 2010, 40,550 stock options issued under the Stock Incentive Plan were exercised for \$466,000 plus related tax benefits of \$143,000. In 2009, 32,000 stock options were issued for \$253,000 plus related tax benefits of \$86,000. The remaining shares were issued to participants of the Employee Stock Purchase Plan.

In October 1998, the Company initiated a stock repurchase program to repurchase up to 315,000 shares of its outstanding Common Stock in open market transactions at market prices. The Company has not repurchased any shares under the program since 2001. The Company is authorized to repurchase 45,100 remaining shares of Common Stock under this program as of December 31, 2010.

Short- and Long-Term Liquidity. The Company expects to meet substantially all of its short-term liquidity requirements resulting from operations and current capital investment plans with internally generated funds and borrowings under the PNC Credit Agreement. At December 31, 2010, the Company had \$34.9 million in cash and \$15.0 million available under the PNC Line. In addition, the ratio of current assets to current liabilities at December 31, 2010 was 4.7:1 compared with 8.8:1 at December 31, 2009, and the debt to total capitalization ratio was 6.3% compared with 8.3%, due to making \$2.2 million in principal repayments and the increase in Stockholders' Equity. The Company's long-term liquidity depends upon its ability to obtain additional orders from its existing customers, attract new customers and control costs. Additional sources of financing may be required to fund growth initiatives identified by the Company.

Contractual Obligations. At December 31, 2010, the Company had the following contractual principal and interest obligations:

| <i>(dollars in thousands)</i> | Total | Payments Due by Period | | | |
|-------------------------------|-----------------|------------------------|----------------|----------------|----------------------|
| | | Less than 1 Year | 1-3 Years | 3-5 Years | More than 5 Years |
| Long-term debt | \$11,897 | \$ 3,281 | \$7,601 | \$1,010 | \$ 5 |
| Operating lease obligations | 68 | 31 | 37 | — | — |
| Purchase obligations | 12,197 | 12,197 | — | — | — |
| Total contractual obligations | <u>\$24,162</u> | <u>\$15,509</u> | <u>\$7,638</u> | <u>\$1,010</u> | <u>\$ 5</u> |

Long-term debt does not include any outstanding balance on the PNC Line, currently due to expire on June 30, 2012, since there was no outstanding balance on December 31, 2010. Purchase obligations include the value of all open purchase orders with established quantities and purchase prices as well as minimum purchase commitments.

Import Protections. The CDSOA provides for payment of import duties collected by the U.S. Treasury Department to domestic companies injured by unfair foreign trade practices. The assets purchased by Dunkirk Specialty Steel were previously owned and operated by AL Tech Specialty Steel, Inc. and Empire Specialty Steel, Inc. During their ownership, both organizations participated in several anti-dumping lawsuits with other domestic specialty steel producers. In accordance with the CDSOA, which expired September 30, 2007, the Company filed claims to receive their appropriate share of the import duties collected and received a net payment of \$32,000 in 2010. Future benefits are dependent on the amount of undistributed import duties collected as of September 30, 2007 and the relationship of Dunkirk Specialty Steel's claim in relation to claims filed by other domestic specialty steel producers. The Company expects minimal distributions in the future.

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EFFECTS OF INFLATION

Despite modest inflation in recent years, rising costs, in particular increasing wage and benefit rates, continue to affect operations. The Company strives to mitigate the effects of inflation through cost containment, productivity improvements and sales price increases.

CONTINGENT ITEMS

Product Claims. The Company is subject to various claims and legal actions that arise in the normal course of conducting business. There were no material product claims outstanding at December 31, 2010.

Environmental Matters. The Company, as well as other steel companies, is subject to demanding environmental standards imposed by federal, state and local environmental laws and regulations. The Company is not aware of any environmental condition that currently exists at any of its facilities that are probable or reasonably possible of having a material impact on the Company's results of operations or liquidity.

The Company is aware of energy usage concerns relating to climate change; however, the Company is not aware of any pending regulations that are expected to have a material impact on the Company's results of operations or liquidity.

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

CRITICAL ACCOUNTING POLICIES AND NEW ACCOUNTING PRONOUNCEMENTS

Critical Accounting Policies. Revenue recognition is the most critical accounting policy of the Company. Revenue from the sale of products is recognized when both risk of loss and title have transferred to the customer, which in most cases coincides with shipment of the related products, and collection is reasonably assured. The Company manufactures specialty steel product to customer purchase order specifications and in recognition of requirements for product acceptance. Material certification forms are executed, indicating compliance with the customer purchase orders, before the specialty steel products are packed and shipped to the customer.

Revenue from conversion services is recognized when the performance of the service is complete. Invoiced shipping and handling costs are also accounted for as revenue. Customer claims, which are not material, are accounted for primarily as a reduction to gross sales after the matter has been researched and an acceptable resolution has been reached.

In addition, management constantly monitors the ability to collect its unpaid sales invoices and the valuation of its receivables. The allowance for doubtful accounts includes specific reserves for the value of outstanding invoices issued to customers currently operating under the protection of the federal bankruptcy law and other amounts that are deemed potentially not collectible with a reserve equal to 15% of 90-day or older balances. However, the total allowance will not be less than 1% of total accounts receivable.

The cost of inventory is principally determined by the average cost method for material costs and operation costs. An inventory reserve is provided for material on hand for which management believes cost exceeds net realizable value and for material on hand for more than one year not assigned to a specific customer order.

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Long-lived assets, including property, plant and equipment, are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable in relation to the operating performance and future undiscounted cash flows of the underlying assets. Adjustments are made if the sum of expected future cash flows is less than book value. At December 31, 2009 and 2008, the Company's stock price was below book value per share. In management's judgment, a significant portion of the decline in the Company's stock price was related to the unprecedented liquidity crisis and the overall economic recession, which began in 2008, and was not reflective of the underlying cash flows of the Company. Based on management's assessment of the carrying values of long-lived assets, no impairment reserve had been deemed necessary as of December 31, 2010, 2009 and 2008. Retirements and disposals are removed from cost and accumulated depreciation accounts, with the gain or loss reflected in operating income.

In addition, management assesses the need to record a valuation allowance to reduce deferred tax assets to the amount that is more likely than not to be realized. The Company believes it will generate sufficient income in addition to taxable income generated from the reversal of its temporary differences to utilize the deferred tax assets recorded at December 31, 2010.

Derivative Financial Instruments. The Company's current risk management strategies include the use of derivative instruments to minimize the risk of significant changes to interest rates used in long-term agreements. In 2009, the Company entered into an interest rate swap that effectively converts the floating-rate Term Loan into a fixed-rate debt instrument. Also, in 2009, the Company entered into nickel futures contracts, the last of which matured March 31, 2010, to minimize the price change impact of anticipated purchases of nickel over the life of a customer short-term supply agreement. The interest rate swap and nickel futures contracts qualify as cash flow hedges and have been marked-to-market at each reporting period date with unrealized gains and losses included in other comprehensive income (loss) ("OCI") to the extent effective, and reclassified to interest expense or cost of sales in the period during which the hedged transaction affects earnings.

New Accounting Pronouncements. See information under the heading "Note 1: Significant Accounting Policies" within "Notes to Consolidated Financial Statements" in Item 8, Financial Statements and Supplementary Data, in this Annual Report on Form 10-K for details of recently issued accounting pronouncements and their expected impact on the Company's financial statements.

FUTURE OUTLOOK

The Company entered 2011 with a total backlog of approximately \$69 million, which is 93% higher than the \$36 million backlog at the beginning of 2010. The current backlog mainly consists of semi-finished products for rollers and forgers and tool steel plate and finished bar for service centers. The increase is primarily due to stronger end-market demand within each of the Company's end markets. End-market demand is expected to gradually increase from current levels during 2011. The Company expects orders for its products will improve in 2011 as demand increases. Our ability to make scheduled payments of principal, or to pay the interest on or to refinance our indebtedness, or to fund planned capital expenditures will depend on our future performance, which, to a certain extent, is subject to general economic, financial, competitive, legislative, regulatory and other factors that are beyond our control. Based upon the current level of operations and our current expectations for future periods in light of the current economic environment, we believe that cash flow from operations and available cash, together with available borrowings under the line of credit agreement, will be adequate to meet the future liquidity needs during the one year following December 31, 2010.

FORWARD-LOOKING INFORMATION SAFE HARBOR

The Management's Discussion and Analysis and other sections of this Annual Report on Form 10-K contain forward-looking statements that reflect the Company's current views with respect to future events and financial performance. Statements looking forward in time, including statements regarding future growth, cost savings, expanded production capacity, broader product lines, greater capacity to meet customer quality reliability, price

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and delivery needs, enhanced competitive posture, effect of new accounting pronouncements and no material financial impact from litigation or contingencies are included in this Annual Report on Form 10-K pursuant to the “safe harbor” provision of the Private Securities Litigation Reform Act of 1995.

The Company’s actual results will be affected by a wide range of factors, including those items described in Item 1A, Risk Factors. Many of these factors are not within the Company’s control and involve known and unknown risks and uncertainties that may cause the Company’s actual results in future periods to be materially different from any future performance suggested herein. Any unfavorable change in the foregoing or other factors could have a material adverse effect on the Company’s business, financial condition and results of operations. Further, the Company operates in an industry sector where securities values may be volatile and may be influenced by economic and other factors beyond the Company’s control.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's customers and suppliers absorb fluctuations in foreign currency exchange rates. Prices for the Company's raw materials and natural gas requirements are subject to frequent market fluctuations, and profit margins may decline in the event market prices increase. Selling price increases and surcharges are implemented to offset raw material and natural gas market price increases.

The cost of raw materials represented 57% of the Company's total cost of products sold in 2010 due to increases in prices for raw materials purchased compared with approximately 52% of the total cost of products sold in 2009 due to lower raw material prices, compared with 63% in 2008. Raw material prices vary based on numerous factors, including quality, and are subject to frequent market fluctuations. Future raw material prices cannot be predicted with any degree of certainty. The Company does not maintain any long-term agreements with any of its raw material suppliers.

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

The Company may use derivative financial instruments to reduce certain types of financial risk. Fixed-price sales arrangements involve a risk of profit margin fluctuations particularly as raw material prices have been volatile. In order to reduce the risk of fluctuating profit margins on firm price sales, the Company, in 2009, entered into commodity futures contracts, the last of which matured March 31, 2010, to purchase certain critical raw materials necessary to produce the products sold under a fixed-price sales arrangement. To manage interest rate risk, the Company has entered into an interest rate swap that effectively converts the floating-rate Term Loan into a fixed-rate debt instrument. The interest rate swap agreement minimizes the impact of interest rate changes on the Company's floating-rate debt and is designated and accounted for as a cash flow hedge. The Company utilizes the interest rate swap to maintain a fixed-rate of 4.515% on the Term Loan until its maturity on February 28, 2014. The notional amount of the interest rate swap decreases ratably over its term, as does the Term Loan, and was \$10.2 million at December 31, 2010.

All hedging strategies are reviewed and approved by senior financial management before being implemented. Management has established policies regarding the use of derivative instruments that prohibit the use of speculative or leveraged derivatives. Market valuations are performed at least quarterly to monitor the effectiveness of our risk management programs.

The Company currently is not exposed to market risk from changes in interest rates related to its government long-term debt. At December 31, 2010, all of the Company's \$623,000 of government long-term debt had fixed interest rates.

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ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

MANAGEMENT’S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for establishing and maintaining adequate internal control over financial reporting (as defined in Rules 13a-15(f) under the Securities Exchange Act of 1934). Our internal control over financial reporting is designed to provide reasonable assurance to management and the board of directors regarding the preparation and fair presentation of published financial statements. Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation. Based on our assessment, we believe that, as of December 31, 2010, our internal control over financial reporting is effective.

The effectiveness of internal control over financial reporting as of December 31, 2010 has been audited by Schneider Downs & Co. Inc., an independent registered public accounting firm which also audited our consolidated financial statements. Schneider Downs’ attestation report on the consolidated financial statements and management’s maintenance of effective internal control over financial reporting is included under the heading “Report of Independent Registered Public Accounting Firm.”

/s/ Dennis M. Oates

Dennis M. Oates

Chairman, President and Chief Executive Officer

/s/ Douglas M. McSorley

Douglas M. McSorley

Vice President of Finance, Chief Financial Officer and Treasurer

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders of Universal Stainless & Alloy Products, Inc.

We have audited the accompanying consolidated balance sheets of Universal Stainless & Alloy Products, Inc. and subsidiaries (the Company) as of December 31, 2010 and 2009, and the related consolidated statements of operations, comprehensive income (loss) and cash flows for each of the years in the three-year period ended December 31, 2010. In addition, our audit included the financial statement schedule listed in the index at Item 15 (2). We also have audited the Company’s internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company’s management is responsible for these consolidated financial statements and financial statement schedule, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management’s Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on these consolidated financial statements, the consolidated financial statement schedule, and an opinion on the Company’s internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

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A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the consolidated financial statements, referred to above present fairly, in all material respects, the financial position of the Company as of December 31, 2010 and 2009, and the results of its operations, comprehensive income (loss) and its cash flows for each of the years in the three-year period ended December 31, 2010, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, the related financial statement schedule, when considered in relation to the consolidated financial statements as a whole, presents fairly, in all material respects, the information set forth therein. Also, in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2010, based on criteria established in *Internal Control – Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

/s/ _____
Schneider Downs & Co., Inc.

Pittsburgh, Pennsylvania
March 3, 2011

[Table of Contents](#)**CONSOLIDATED STATEMENTS OF OPERATIONS**

| <u>For the years ended December 31,</u> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|--|-------------|-------------|-------------|
| <i>(dollars in thousands, except per share information)</i> | | | |
| Net sales | \$ 189,423 | \$ 124,907 | \$ 235,106 |
| Cost of products sold | 155,651 | 117,901 | 204,929 |
| Selling and administrative expenses | 13,349 | 11,663 | 11,085 |
| Operating income (loss) | 20,423 | (4,657) | 19,092 |
| Interest expense and other financing costs | (452) | (89) | (105) |
| Other income, net | 92 | 695 | 911 |
| Income (loss) before income tax expense | 20,063 | (4,051) | 19,898 |
| Provision (benefit) for income taxes | 6,821 | (1,093) | 5,948 |
| Net income (loss) | \$ 13,242 | \$ (2,958) | \$ 13,950 |
| EARNINGS (LOSS) PER COMMON SHARE | | | |
| Basic | \$ 1.95 | \$ (0.44) | \$ 2.08 |
| Diluted | \$ 1.93 | \$ (0.44) | \$ 2.05 |
| WEIGHTED-AVERAGE COMMON SHARES USED TO COMPUTE EARNINGS PER SHARE | | | |
| Basic | 6,782,576 | 6,755,560 | 6,706,535 |
| Diluted | 6,868,255 | 6,755,560 | 6,801,203 |

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

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

| <u>For the years ended December 31,</u> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|--|-------------|-------------|-------------|
| <i>(dollars in thousands)</i> | | | |
| Net income (loss) | \$13,242 | \$(2,958) | \$13,950 |
| Net change in fair market value of cash flow hedges: | | | |
| Interest rate swap | (142) | (145) | — |
| Nickel hedge contracts | (94) | 94 | — |
| Tax effect | 86 | 19 | — |
| Comprehensive income (loss) | \$13,092 | \$(2,990) | \$13,950 |

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

[Table of Contents](#)**CONSOLIDATED BALANCE SHEETS**

| <u>December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> |
|--|------------------|------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 34,944 | \$ 42,349 |
| Accounts receivable (less allowance for doubtful accounts of \$2,134 and \$2,132) | 29,273 | 17,028 |
| Inventory, net | 69,710 | 41,322 |
| Other current assets | 5,661 | 9,344 |
| Total current assets | 139,588 | 110,043 |
| Property, plant and equipment, net | 71,581 | 70,085 |
| Other assets | 1,499 | 1,586 |
| Total assets | <u>\$212,668</u> | <u>\$181,714</u> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Trade accounts payable | \$ 20,022 | \$ 7,783 |
| Outstanding checks in excess of bank balance | 544 | 734 |
| Accrued employment costs | 5,488 | 1,178 |
| Current portion of long-term debt | 2,833 | 2,223 |
| Other current liabilities | 605 | 553 |
| Total current liabilities | 29,492 | 12,471 |
| Long-term debt | 7,990 | 10,823 |
| Deferred taxes | 15,276 | 14,049 |
| Other liabilities | 287 | 145 |
| Total liabilities | <u>53,045</u> | <u>37,488</u> |
| COMMITMENTS AND CONTINGENCIES | | |
| STOCKHOLDERS' EQUITY | | |
| Senior Preferred Stock, par value \$0.001 per share; 1,980,000 shares authorized; 0 shares outstanding | — | — |
| Common Stock, par value \$0.001 per share; 10,000,000 shares authorized; 7,094,314 and 7,043,899 shares issued | 7 | 7 |
| Additional paid-in capital | 41,341 | 38,776 |
| Retained earnings | 120,376 | 107,134 |
| Treasury Stock at cost; 282,850 and 270,795 common shares held | (1,919) | (1,659) |
| Accumulated other comprehensive loss | (182) | (32) |
| Total stockholders' equity | <u>159,623</u> | <u>144,226</u> |
| Total liabilities and stockholders' equity | <u>\$212,668</u> | <u>\$181,714</u> |

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

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CONSOLIDATED STATEMENTS OF CASH FLOWS

| <u>For the years ended December 31,</u> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|---|------------------|------------------|------------------|
| <i>(dollars in thousands, except per share information)</i> | | | |
| CASH FLOWS FROM OPERATING ACTIVITIES | | | |
| Net income (loss) | \$ 13,242 | \$ (2,958) | \$ 13,950 |
| Adjustments to reconcile to net cash and cash equivalents provided by operating activities: | | | |
| Depreciation and amortization | 5,486 | 4,859 | 4,167 |
| Loss on retirement of fixed assets | 17 | 84 | 402 |
| Deferred income tax | 730 | 1,853 | 558 |
| Share-based compensation expense | 1,819 | 1,058 | 838 |
| Tax benefit from share-based payment arrangements | (143) | (86) | (529) |
| Changes in assets and liabilities: | | | |
| Accounts receivable, net | (12,245) | 16,029 | (5,556) |
| Inventory, net | (28,388) | 21,900 | 2,350 |
| Trade accounts payable | 12,239 | (11,567) | 5,367 |
| Outstanding checks in excess of bank balance | (190) | 194 | (1,524) |
| Accrued employment costs | 4,310 | (2,617) | (1,512) |
| Current income tax, net | 4,175 | (1,613) | (1,491) |
| Other, net | 243 | 764 | (874) |
| Net cash provided by operating activities | <u>1,295</u> | <u>27,900</u> | <u>16,146</u> |
| CASH FLOWS USED IN INVESTING ACTIVITIES | | | |
| Proceeds from sale of fixed assets | 18 | 60 | — |
| Capital expenditures | (7,481) | (12,394) | (12,905) |
| Net cash used in investing activities | <u>(7,463)</u> | <u>(12,334)</u> | <u>(12,905)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES | | | |
| Long-term debt issuance | — | 12,000 | — |
| State grant funding the purchase of new equipment | 500 | — | — |
| Long-term debt repayment | (2,223) | (403) | (387) |
| Deferred financing costs | — | (84) | — |
| Proceeds from issuance of Common Stock | 603 | 372 | 781 |
| Purchase of treasury stock | (260) | — | — |
| Tax benefit from share-based payment arrangements | 143 | 86 | 529 |
| Net cash (used in) provided by financing activities | <u>(1,237)</u> | <u>11,971</u> | <u>923</u> |
| Net (decrease) increase in cash and cash equivalents | <u>(7,405)</u> | <u>27,537</u> | <u>4,164</u> |
| Cash and cash equivalents at beginning of period | <u>42,349</u> | <u>14,812</u> | <u>10,648</u> |
| Cash and cash equivalents at end of period | <u>\$ 34,944</u> | <u>\$ 42,349</u> | <u>\$ 14,812</u> |
| SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION | | | |
| Interest paid, net of amount capitalized | \$ 446 | \$ 65 | \$ 91 |
| Income taxes paid (refunded), net | \$ 1,774 | \$ (1,368) | \$ 6,351 |

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

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1: Significant Accounting Policies

Basis of Consolidation. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. The Company has no interests in any unconsolidated entity.

Use of Estimates. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. The estimates and assumptions used in these consolidated financial statements are based on known information available as of the balance sheet date. Actual results could differ from those estimates.

Concentration of Credit Risk. Financial instruments that potentially subject the Company to concentrations of credit risk are cash and cash equivalents and accounts receivable. The Company limits its credit risk associated with cash and cash equivalents by placing its investments in high-grade short-term instruments or in bank transaction accounts with full FDIC insurance protection, regardless of amount. With respect to accounts receivable, the Company limits its credit risk by performing ongoing credit evaluations and, when deemed necessary, requiring letters of credit, guarantees or cash collateral. The allowance for doubtful accounts includes specific reserves for the value of outstanding invoices issued to customers currently operating under the protection of the federal bankruptcy law and other amounts that are deemed potentially not collectible with a reserve equal to 15% of 90-day or older balances. However, the total allowance will not be less than 1% of total accounts receivable. Receivables are charged-off to the allowance when they are deemed to be uncollectible. Bad debt expense for fiscal years 2010, 2009 and 2008 was \$4,000, \$1.8 million and \$13,000, respectively.

Inventories. Inventories are stated at the lower of cost or market with cost principally determined by the weighted average cost method. Such costs include the acquisition cost for raw materials and supplies, direct labor and applied manufacturing overhead within the guidelines of normal plant capacity. The Company changed its method of stating the raw material inventory from the first-in-first-out method to the weighted average cost method. The Company believes the change is preferable as the average cost method better reflects the current value of the co-mingled raw material inventory and provides a consistent better reflection of periodic income. The change did not have a material impact due to the rapid turn-over rate of the raw material inventory. Provisions are made for slow-moving inventory based upon management's expected method of disposition. The net change in inventory reserves for fiscal years 2010, 2009 and 2008 was a \$166,000 decrease, a \$2.0 million decrease, and a \$1.0 million increase, respectively.

Included in inventory are operating materials consisting of production molds and rolls that will normally be consumed within one year.

Property, Plant and Equipment. Property, plant and equipment is recorded at cost. Costs incurred in connection with the construction or major rebuild of facilities, including interest directly related to the project, are capitalized as construction in progress. No depreciation is recognized on these assets until placed in service. Retirements and disposals are removed from cost and accumulated depreciation accounts, with the gain or loss reflected in operating income. Material major equipment maintenance costs are capitalized as incurred and amortized into expense over the subsequent six-month period, while other maintenance costs are expensed as incurred. Costs of improvements and renewals are capitalized. Maintenance expense for the fiscal year 2010, 2009 and 2008 was \$11.9 million, \$9.4 million and \$13.1 million, respectively.

Depreciation and amortization are computed using the straight-line method based on the estimated useful lives of the related assets. The estimated useful lives of buildings and land improvements are between 10 and 39 years, and the estimated useful lives of machinery and equipment are between 5 and 20 years. Direct costs incurred in the development and implementation of internal-use software are capitalized and recorded within property, plant

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and equipment, and amortized on a straight-line basis over its anticipated useful life, which is generally three to five years. Depreciation and amortization expense for fiscal year 2010, 2009 and 2008 was \$5.5 million, \$4.8 million and \$4.1 million, respectively.

Long-Lived Asset Impairment. Long-lived assets, including property, plant and equipment, are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable in relation to the operating performance and future undiscounted cash flows of the underlying assets. Adjustments are made if the sum of expected future cash flows is less than book value. Based on management's assessment of the carrying values of long-lived assets, no impairment reserve has been deemed necessary as of December 31, 2010, 2009 and 2008.

Revenue Recognition. Revenue from the sale of products is recognized when both risk of loss and title have transferred to the customer, which in most cases coincides with shipment of the related products, and collection is reasonably assured. Revenue from conversion services is recognized when the performance of the service is complete. Invoiced shipping and handling costs are also accounted for as revenue. Customer claims, which are not material, are accounted for primarily as a reduction to gross sales after the matter has been researched and an acceptable resolution has been reached.

Income Taxes. Deferred income taxes are provided for unused tax credits earned and the tax effect of temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements. The Company uses the liability method to account for income taxes, which requires deferred taxes to be recorded at the statutory rate expected to be in effect when the taxes are paid. Valuation allowances are provided for a deferred tax asset when it is more likely than not that such asset will not be realized. Income tax penalties and interest are included in the provision for income tax expense.

In addition, the Company evaluates the tax positions taken or expected to be taken in its tax returns. A tax position should only be recognized in the financial statements if the Company determines that it is more-likely-than-not that the tax position will be sustained upon examination by the tax authorities, based upon the technical merits of the position. For those tax positions that should be recognized, the measurement of a tax position is determined as being the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. The Company believes there are no known uncertain tax positions at December 31, 2010, 2009 and 2008.

Share-based Compensation Plans. The Company recognizes compensation expense based on the grant-date fair value of the awards. The fair value of the option grants is estimated on the date of grant using the Black-Scholes option-pricing model, and is recognized ratably over the service/vesting period of the award. The tax effects of exercising stock options are added to additional paid-in capital at the exercise date.

Earnings Per Common Share. Basic earnings per common share is computed by dividing net income (loss) by the weighted-average number of common shares outstanding during the period. Diluted earnings per common share is computed by dividing net income by the weighted-average number of common shares outstanding plus all dilutive potential common shares outstanding during the period. Dilutive common shares are determined using the treasury stock method. Under the treasury stock method, exercise of options is assumed at the beginning of the period when the average stock price during the period exceeds the exercise price of outstanding options, and common shares are assumed issued. The assumed proceeds from the exercise of stock options are used to purchase common stock at the average market price during the period. The incremental shares to be issued are considered to be the dilutive potential common shares outstanding.

Derivatives. In March 2008, the Financial Accounting Standards Board ("FASB") issued "Disclosures about Derivative Instruments and Hedging Activities", which changes the disclosure requirements for derivative instruments and hedging activities. Enhanced disclosures are required to provide information about (a) how and why an entity uses derivative instruments, (b) how derivative instruments and related hedged items are accounted

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for and (c) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. Adoption of the standard, effective January 1, 2009, did not have a material impact on the Company's financial statements.

In June 2009, the FASB issued "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles". The standard establishes the FASB Accounting Standards Codification as the source of authoritative accounting principles recognized by the FASB to be applied in the preparation of financial statements in conformity with GAAP in the United States. The Company adopted the standard effective June 30, 2009.

Reclassifications. Certain prior year amounts have been reclassified to conform to the 2010 presentation.

Note 2: Inventory

The major classes of inventory are as follows:

| <u>December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> |
|--|-----------------|-----------------|
| Raw materials and supplies | \$ 7,141 | \$ 5,585 |
| Semi-finished and finished steel products | 58,899 | 32,969 |
| Inventory reserves | (986) | (1,152) |
| Operating materials | 4,656 | 3,920 |
| Total inventory | <u>\$69,710</u> | <u>\$41,322</u> |

Note 3: Property, Plant and Equipment

Property, plant and equipment consists of the following:

| <u>December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> |
|--|------------------|------------------|
| Land and land improvements | \$ 2,772 | \$ 2,603 |
| Buildings | 16,313 | 14,479 |
| Machinery and equipment | 90,909 | 86,276 |
| Construction in progress | 4,606 | 4,284 |
| | 114,600 | 107,642 |
| Accumulated depreciation | (43,019) | (37,557) |
| Property, plant and equipment, net | <u>\$ 71,581</u> | <u>\$ 70,085</u> |

Note 4: Long-Term Debt and Other Financing

Long-term debt consists of the following:

| <u>December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> |
|--|-----------------|-----------------|
| Term Loan | \$10,200 | \$12,000 |
| Government debt | 623 | 1,046 |
| Less amounts due within one year | (2,833) | (2,223) |
| Total long-term debt | <u>\$ 7,990</u> | <u>\$10,823</u> |

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In February 2009, the Company executed an unsecured credit agreement with PNC Bank which provides for a \$12.0 million term loan (“Term Loan”) scheduled to mature on February 28, 2014 and a \$15.0 million revolving credit facility with a term expiring on June 30, 2012. There was no balance outstanding under the revolver at December 31, 2010 or December 31, 2009. The Term Loan was used to fund the capital expenditures for the Bridgeville melt shop upgrade. Accordingly, all of the \$454,000 interest on the loan for 2009 was capitalized and \$132,000 of the 2010 interest was capitalized. Interest on both facilities is based on short-term market rates, which may be adjusted, based upon the Company maintaining certain financial ratios. PNC Bank also charges a commitment fee payable on the unused portion of the revolving credit facility of 0.25%, provided certain financial ratios are maintained. The Company is required to be in compliance with three financial covenants: a minimum leverage ratio, a minimum debt service ratio and a minimum tangible net worth. The Company was in compliance with all such covenants at December 31, 2010.

The Company maintains two separate loan agreements with the Commonwealth of Pennsylvania’s Department of Commerce, aggregating to \$600,000. A \$200,000 15-year loan bears interest at 5% per annum with the term ending in 2011, and a \$400,000 20-year loan bears interest at 6% per annum with the term ending in 2016. On February 14, 2002, Dunkirk Specialty Steel issued two ten-year, 5% interest-bearing notes payable to the New York Job Development Authority for the combined amount of \$3.0 million.

The Company leases certain office equipment and a vehicle. The aggregate annual principal payments due under the Company’s long-term debt and minimum lease payments under operating leases are as follows:

| <u>For the years ended December 31,</u> <i>(dollars in thousands)</i> | <u>2011</u> | <u>2012</u> | <u>2013</u> | <u>2014</u> | <u>2015</u> | <u>Thereafter</u> | <u>Total</u> |
|--|-------------|-------------|-------------|-------------|-------------|-------------------|--------------|
| Long-term debt principal payments | \$2,833 | \$3,391 | \$3,629 | \$931 | \$ 39 | \$ — | \$10,823 |
| Operating lease minimum payments | <u>30</u> | <u>25</u> | <u>13</u> | <u>—</u> | <u>—</u> | <u>—</u> | <u>68</u> |

Note 5: Derivatives and Hedging Activities

To manage interest rate risk, the Company has entered into an interest rate swap that effectively converts the floating-rate Term Loan into a fixed-rate debt instrument. The interest rate swap agreement minimizes the impact of interest rate changes on the Company’s floating-rate debt and is designated and accounted for as a cash flow hedge. The effective portion of the change in the fair value of the interest rate swap is recorded in accumulated other comprehensive income (loss) (“OCI”) and reflected a \$287,000 loss at December 31, 2010. The Company utilizes the interest rate swap to maintain a fixed-rate of 4.515% on the Term Loan until its maturity on February 28, 2014. The notional amount of the interest rate swap decreases ratably over its term, as does the Term Loan, and was \$10.2 million at December 31, 2010.

In July 2009, the Company entered into nickel futures contracts, the last of which matured March 31, 2010, to minimize the price change impact of anticipated purchases of nickel over the life of a customer fixed-price sales agreement which was designated as and accounted for as a cash flow hedge. The effective portion of the change in the fair value of the nickel hedge agreements was recorded in accumulated OCI and reflected a \$94,000 gain at December 31, 2009, which was realized in 2010.

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The interest rate swap and nickel futures contracts qualify as cash flow hedges and are marked-to-market at each reporting period date with unrealized gains and losses included in OCI to the extent effective, and reclassified to interest expense or cost of sales in the period during which the hedged transaction affects earnings. No cash flow hedges were discontinued and there was no ineffectiveness during the year. The location and amounts recorded in the Condensed Consolidated Balance Sheets for the derivative instruments are as follows:

| (dollars in thousands) | December 31, 2010 | December 31, 2009 |
|---|----------------------|----------------------|
| Other current assets | \$ — | \$ 94 |
| Other assets, deferred tax | 105 | 53 |
| Other current liabilities, deferred tax | — | (34) |
| Other liabilities | <u>(287)</u> | <u>(145)</u> |
| Shareholders equity, other comprehensive loss | <u>\$ (182)</u> | <u>\$ (32)</u> |

Note 6: Fair Value Measurements

The Company adopted “Topic 820 Fair Value Measurement and Disclosures” which defines fair value, establishes a framework for measuring fair value and expands disclosure requirements about fair value measurements. It also defines fair value as the price that would be received to sell an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The fair value hierarchy prescribed by the standard contains three levels as follows:

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

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

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

The fair value hierarchy requires the use of observable market data when available. In instances where the inputs used to measure fair value fall into different levels of the fair value hierarchy, the fair value measurement has been determined based on the lowest level input significant to the fair value measurement in its entirety. Our assessment of the significance of a particular item to the fair value measurement in its entirety requires judgment, including the consideration of inputs specific to the asset or liability. The interest rate swap is recorded at fair value based on Level 2 quoted LIBOR swap rates adjusted for credit and non-performance risk. The nickel futures contracts were recorded at fair value based on Level 2 quoted futures rates.

Financial instruments include cash, accounts receivable, other current assets, accounts payable, short-term debt, other current liabilities and long-term debt. The carrying amounts of these financial instruments approximated fair value at December 31, 2010 and December 31, 2009. The fair value of the Term Loan approximates the carrying amount based on the interest rate being based on one-month floating Libor rates.

[Table of Contents](#)**Note 7: Income Taxes**

Components of the provision for income taxes are as follows:

| <u>For the years ended December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|--|-----------------------|-------------------------|-----------------------|
| CURRENT PROVISION (BENEFIT) | | | |
| Federal | \$5,887 | \$(4,109) | \$5,553 |
| State | 205 | 1,164 | (163) |
| DEFERRED PROVISION (BENEFIT) | | | |
| Federal | 568 | 2,450 | 936 |
| State | 161 | (598) | (378) |
| Provision (benefit) for income taxes | <u>\$6,821</u> | <u>\$(1,093)</u> | <u>\$5,948</u> |

A reconciliation of the federal statutory tax rate and the Company's effective tax rate is as follows:

| <u>For the years ended December 31,</u> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|---|---------------------|-----------------------|---------------------|
| Federal statutory tax (benefit) rate | 35.0% | (35.0)% | 35.0% |
| Reconciliation of federal and state tax balances to tax returns | 0.0 | 13.4 | 0.0 |
| Statutory tax rate changes | 0.0 | (4.5) | (0.2) |
| Loss carryback realized at higher statutory rate | 0.0 | (1.9) | 0.0 |
| State government grants, net of federal tax impact | (0.1) | (1.2) | (2.4) |
| Domestic manufacturing deduction | (2.8) | 0.0 | (1.7) |
| State income taxes, net of federal tax impact | 1.6 | 0.0 | 0.0 |
| Other, net | 0.3 | 2.2 | (0.8) |
| Effective income tax (benefit) rate | <u>34.0%</u> | <u>(27.0)%</u> | <u>29.9%</u> |

Dunkirk Specialty Steel operates in a New York State Empire Zone and is qualified to benefit from investments made and employees hired at the Dunkirk, New York facility for up to 15 years from its 2002 acquisition date. The Company recognized tax credit benefits of \$43,000 and \$73,000 for fiscal years 2010 and 2009, respectively, none of which were applied against the respective year's current tax provision. The balance of the credits, which have no expiration date, will be applied against future tax liabilities for income apportioned to New York State. The Company believes it will generate sufficient income in addition to taxable income generated from the reversal of its temporary differences to utilize this tax credit.

The Company recognized a Pennsylvania Educational Improvement Tax Credit benefit ("PAEIT") of \$180,000 for 2008 which was applied against that year's current tax provision.

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Deferred taxes result from the following:

| <u>December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> |
|--|-----------------|-----------------|
| DEFERRED TAX ASSETS | | |
| Receivables | \$ 809 | \$ 837 |
| Inventory | 1,598 | 1,642 |
| Accrued liabilities | 386 | 288 |
| Share-based compensation expense | 1,443 | 848 |
| State tax carryforwards (noncurrent) | 1,294 | 1,416 |
| Other | 195 | 120 |
| | <u>\$ 5,725</u> | <u>\$ 5,151</u> |
| DEFERRED TAX LIABILITIES | | |
| Property, plant and equipment (noncurrent) | \$15,276 | \$14,049 |
| Other | 124 | 134 |
| | <u>\$15,400</u> | <u>\$14,183</u> |

State tax carryforwards represent New York Empire Zone tax credits with no expiration date and a state net operating loss carryforward expiring in 2029.

The Company is routinely under audit by federal or state authorities in the areas of income taxes and the remittance of sales and use taxes. The Company's tax returns for tax years 2007 through 2010 remain subject to examination by the Internal Revenue Service and from 2006 for state tax jurisdictions.

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Note 8: Stockholders' Equity

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

In October 1998, the Company initiated a stock repurchase program to repurchase up to 315,000 shares of its outstanding Common Stock in open market transactions at market prices. The Company is authorized to repurchase 45,100 remaining shares of Common Stock under this program as of December 31, 2010.

The Company has 1,980,000 authorized shares of Senior Preferred Stock. At December 31, 2010 and 2009, there were no preferred shares issued or outstanding.

| | <u>Common Shares Outstanding</u> | <u>Common Stock</u> | <u>Additional Paid-In Capital</u> | <u>Retained Earnings</u> | <u>Accumulated Other Comprehensive (Loss)</u> | <u>Treasury Shares</u> | <u>Treasury Stock</u> |
|--|--|-------------------------|---|------------------------------|---|----------------------------|---------------------------|
| <i>(dollars in thousands)</i> | | | | | | | |
| Balance at January 1, 2008 | 6,930,294 | \$ 7 | \$ 35,112 | \$ 96,142 | \$ — | 270,795 | \$(1,659) |
| Common Stock issuance under Employee Stock Purchase Plan | 7,935 | | 155 | | | | |
| Exercise of Stock Options | 64,850 | | 626 | | | | |
| Share-based compensation | | | 838 | | | | |
| Tax benefit on share-based compensation | | | 529 | | | | |
| Net income | | | | 13,950 | | | |
| Balance at December 31, 2008 | <u>7,003,079</u> | <u>\$ 7</u> | <u>\$ 37,260</u> | <u>\$110,092</u> | <u>\$ —</u> | <u>270,795</u> | <u>\$(1,659)</u> |
| Common Stock issuance under Employee Stock Purchase Plan | 8,820 | | 119 | | | | |
| Exercise of Stock Options | 32,000 | | 253 | | | | |
| Share-based compensation | | | 1,058 | | | | |
| Tax benefit on share-based compensation | | | 86 | | | | |
| Net (loss) | | | | (2,958) | | | |
| Net losses on derivative instruments, net of tax | | | | | (32) | | |
| Balance at December 31, 2009 | 7,043,899 | \$ 7 | \$ 38,776 | \$107,134 | \$ (32) | 270,795 | \$(1,659) |
| Common Stock issuance under Employee Stock Purchase Plan | 9,865 | | 137 | | | | |
| Exercise of stock options | 40,550 | | 466 | | | | |
| Share-based compensation | | | 1,819 | | | | |
| Tax benefit on share-based compensation | | | 143 | | | | |
| Net income | | | | 13,242 | | | |
| Net losses on derivative instruments, net of tax | | | | | (150) | | |
| Purchase of treasury stock | | | | | | 12,055 | (260) |
| Balance at December 31, 2010 | <u>7,094,314</u> | <u>\$ 7</u> | <u>\$ 41,341</u> | <u>\$120,376</u> | <u>\$ (182)</u> | <u>282,850</u> | <u>\$(1,919)</u> |

[Table of Contents](#)**Note 9: Basic and Diluted Earnings Per Share**

The computation of basic and diluted earnings per share for the years ended December 31, 2010, 2009 and 2008 is as follows:

| For the years ended December 31, <i>(dollars in thousands, except per share amounts)</i> | 2010 | | 2009 | | 2008 | |
|---|-----------------|------------------|------------------|------------------|-----------------|------------------|
| | Income | Shares | Income | Shares | Income | Shares |
| Income (loss) available to common Stockholders | \$13,242 | 6,782,576 | \$(2,958) | 6,755,560 | \$13,950 | 6,706,535 |
| Effect of dilutive securities | — | 85,679 | — | — | — | 94,668 |
| Income (loss) available to common Stockholders plus assumed conversion | <u>\$13,242</u> | <u>6,868,255</u> | <u>\$(2,958)</u> | <u>6,755,560</u> | <u>\$13,950</u> | <u>6,801,203</u> |
| EARNINGS (LOSS) PER COMMON SHARE | | | | | | |
| Basic | \$ 1.95 | | \$ (0.44) | | \$ 2.08 | |
| Diluted | <u>\$ 1.93</u> | | <u>\$ (0.44)</u> | | <u>\$ 2.05</u> | |

The Company had 38,028 common stock equivalents outstanding at December 31, 2009 which were not included in the common share computations for earnings (loss) per share as the common stock equivalents were anti-dilutive.

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Note 10: Share-based Compensation Plans

At December 31, 2010, the Company has three incentive compensation plans that are described below:

STOCK INCENTIVE PLAN

The Company maintains the Stock Incentive Plan that has been adopted and amended from time to time by the Company's Board of Directors and approved by its stockholders. The Stock Incentive Plan permits the issuance of stock options to non-employee directors, other than those directors owning more than 5% of the Company's outstanding Common Stock, officers and other key employees of the Company who are expected to contribute to the Company's future growth and success. The stockholders approved an increase of 400,000 reserved shares in 2010. The Company may grant options up to a maximum of 1,750,000 shares of Common Stock, of which 454,318 are available for grant at December 31, 2010. The option price is equal to the fair market value of the Common Stock at the date of grant. Options granted to non-employee directors vest over a three-year period, and options granted to employees vest over a four-year period. All options under the Stock Incentive Plan will expire no later than ten years after the grant date. Forfeited options may be reissued and are included in the amount available for grants.

A summary of the Stock Incentive Plan activity as of and for the years ended December 31, 2010, 2009 and 2008 is presented below:

| | Shares Available for Grant | Non-Vested Stock Options Outstanding | | Stock Options Outstanding | |
|-----------------------------------|-------------------------------|--|---|------------------------------|---|
| | | Number of Shares | Weighted- Average Grant Fair Value | Number of Shares | Weighted- Average Exercise Price |
| Balance, January 1, 2008 | 393,668 | 174,050 | \$ 14.80 | 403,650 | \$ 18.14 |
| Granted | (160,000) | 160,000 | 15.12 | 160,000 | 27.23 |
| Stock options exercised | | | | (64,850) | 9.64 |
| Stock options vested | | (63,225) | 12.00 | | |
| Forfeited | 19,250 | (19,250) | 18.57 | (19,250) | 32.07 |
| Balance, December 31, 2008 | 252,918 | 251,575 | 15.42 | 479,550 | 21.77 |
| Granted | (122,500) | 122,500 | 9.24 | 122,500 | 16.31 |
| Stock options exercised | | | | (32,000) | 7.90 |
| Stock options vested | | (84,250) | 14.80 | | |
| Forfeited | 8,750 | (5,750) | 15.07 | (8,750) | 30.00 |
| Balance, December 31, 2009 | 139,168 | 284,075 | 12.94 | 561,300 | 20.04 |
| Additional shares reserved | 400,000 | | | | |
| Granted | (130,000) | 130,000 | 12.49 | 130,000 | 22.10 |
| Stock options exercised | | | | (40,550) | 11.49 |
| Stock options vested | | (95,700) | 13.85 | | |
| Forfeited | 45,150 | (36,400) | 12.55 | (45,150) | 20.62 |
| Balance, December 31, 2010 | 454,318 | 281,975 | \$ 12.94 | 605,600 | \$ 22.02 |

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The following table summarizes information about stock options outstanding at December 31, 2010:

| Range of Exercise Prices | Options Outstanding | | | Options Exercisable | |
|-----------------------------------|---------------------|---|---------------------------------|---------------------|---------------------------------|
| | Number of Shares | Weighted-Average Remaining Years Contractual Life | Weighted-Average Exercise Price | Number of Shares | Weighted-Average Exercise Price |
| \$5.12 to \$13.89 | 121,300 | 4.2 | \$ 9.79 | 95,775 | \$ 9.16 |
| \$14.18 to \$16.98 | 113,500 | 6.9 | 16.14 | 66,550 | 15.64 |
| \$18.15 to \$30.97 | 189,000 | 8.9 | 21.37 | 36,050 | 20.41 |
| \$31.95 to \$34.80 | 136,000 | 6.8 | 33.12 | 94,050 | 32.84 |
| \$36.15 to \$42.50 | 45,800 | 7.1 | 38.73 | 33,200 | 39.28 |
| Outstanding at end of year | 605,600 | 7.0 | \$ 22.02 | 325,625 | \$ 21.64 |
| Exercisable at end of year | 325,625 | 5.5 | | | |

Proceeds from stock option exercises totaled \$466,000 in 2010, \$253,000 in 2009 and \$625,000 in 2008. Shares issued in connection with stock option exercises are issued from available authorized shares. Tax benefits realized from stock options exercised totaled \$143,000 in 2010, \$86,000 in 2009 and \$529,000 in 2008.

Based upon the closing stock price of \$31.28 at December 31, 2010, the aggregate intrinsic value of outstanding in-the-money stock options and outstanding exercisable in-the-money stock options was \$6.2 million and \$3.6 million, respectively. Intrinsic value of stock options is calculated as the amount by which the market price of the Company's Common Stock exceeds the exercise price of the options. The aggregate intrinsic value of stock options exercised was \$560,000 in 2010, \$239,000 in 2009 and \$1.5 million in 2008. The total fair value of share awards vested was \$1.3 million during 2010, \$1.2 million during 2009, and \$759,000 in 2008.

Share-based Compensation Expense. FASB Accounting Standards require that share-based compensation to employees and directors be recognized as compensation expense in the income statement based on their fair values on the measurement date, which is the date of the grant. The value of the portion of the award that is ultimately expected to vest is recognized as expense over the requisite service periods. The compensation expense recognized and its related tax effects are included in additional paid-in capital. Additional paid-in capital is further adjusted for the difference between compensation expense recorded under the accounting standard and compensation expense reported for tax purposes upon actual exercise of employee stock options.

Share-based compensation expense totaled \$1.8 million in 2010, \$1.1 million in 2009 and \$838,000 in 2008. Share-based compensation expense is recognized ratably over the requisite service period for all awards. The tax benefit associated with the stock compensation expense recognized in the accompanying Consolidated Statements of Operations was \$420,000 in 2010, \$394,000 in 2009 and \$305,000 in 2008. Unrecognized share-based compensation expense related to non-vested stock awards totaled \$4.9 million at December 31, 2010. At such date, the weighted-average period over which this unrecognized expense was expected to be recognized was 29 months.

Valuation of Share-based Compensation. The fair value of the Company's employee stock options granted is estimated on the measurement date, which, for the Company, is the date of grant. The Company uses the Black-Scholes option-pricing model. The weighted-average fair value of stock options granted was \$1.6 million for 2010, \$1.1 million for 2009, and \$2.4 million for 2008. The Company's determination of fair value of share-based payment awards on the date of grant is affected by the Company's stock price as well as assumptions regarding the Company's expected stock price volatility over the term of the awards, and actual and projected employee stock option exercise behaviors.

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The assumptions used to determine the fair value of options granted are detailed in the table below:

| | 2010 | 2009 | 2008 |
|---|------------------|------------------|------------------|
| Risk-free interest rate | 1.53 to 2.68% | 2.34 to 3.15% | 2.19 to 3.87% |
| Dividend yield | 0.0% | 0.0% | 0.0% |
| Expected market price volatility | 54 to 59% | 54 to 56% | 47 to 53% |
| Weighted-average expected market price volatility | 56.3% | 55.2% | 49.8% |
| Expected term | 6.0 to 7.8 years | 6.0 to 7.8 years | 5.8 to 8.2 years |

The risk-free interest rate was developed using the U.S. Treasury yield curve for periods equal to the expected life of the options at the grant date. No dividend yield was assumed because the Company does not pay cash dividends on Common Stock and currently has no plans to pay a dividend. Expected volatility is based on the long-term historical volatility (estimated over a period equal to the expected term of the options) of the Company's stock. In estimating the fair value of stock options under the Black-Scholes option-pricing model, separate groups of employees that have similar historical exercise behavior are considered separately. The expected term of options granted represents the period of time that options granted are expected to be outstanding.

EMPLOYEE STOCK PURCHASE PLAN

Under the 1996 Employee Stock Purchase Plan (the "Stock Purchase Plan"), the Company is authorized to issue up to 150,000 shares of Common Stock to its full-time employees, nearly all of whom are eligible to participate. Under the terms of the plan, employees can choose as of January 1 and July 1 of each year to have up to 10% of their total earnings withheld to purchase up to 100 shares of the Company's Common Stock each six-month period. The purchase price of the stock is 85% of the lower of its beginning-of-the-period or end-of-the-period market prices. At December 31, 2010, the Company has issued 122,933 shares of Common Stock since the plan's inception.

CASH INCENTIVE PLANS

The Company has a management cash incentive plan covering certain key executives and employees and profit-sharing plans that cover the remaining employees. The profit-sharing plans provide for the sharing of pre-tax profits in excess of specified amounts. For the years ended December 31, 2010, 2009 and 2008, the Company expensed \$5.0 million, \$252,000 and \$3.7 million, respectively, under these plans.

Note 11: Retirement Plans

The Company has a defined contribution retirement plan that covers substantially all employees. Pursuant to the 401(k) plan, participants may elect to make pre-tax and after-tax contributions, subject to certain limitations imposed under the Internal Revenue Code of 1986, as amended. In addition, the Company makes periodic contributions to the 401(k) plan based on service for the Titusville and Dunkirk hourly employees. The company makes periodic contributions for the salaried employees; the amount of the contribution is dependent upon their individual contribution to the 401(k) retirement plan.

The Company participates in the Steelworkers Pension Trust (the "Trust"), a multi-employer defined-benefit pension plan that is open to all hourly and salaried employees associated with the Bridgeville facility. The Company makes periodic contributions to the Trust based on hours worked at a fixed rate for each hourly employee and a fixed monthly contribution on behalf of each salaried employee. The company has the option and right to terminate participation in the Trust if the withdrawal liability ratio of assets to liabilities is below 100%.

The total expense for the years ended December 31, 2010, 2009 and 2008 was \$937,000, \$743,000 and \$972,000, respectively, including \$567,000, \$438,000 and \$494,000, respectively, for the multi-employer Trust. No other post-retirement benefit plans exist.

Note 12: Commitments and Contingencies

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

The Company, as well as other steel companies, is subject to demanding environmental standards imposed by federal, state and local environmental laws and regulations. The Company is not aware of any environmental condition that currently exists at any of its facilities that would cause a material adverse effect on the financial condition of the Company, results of operations or liquidity in a particular future quarter or year.

The CDSOA provides for payment of import duties collected by the U.S. Treasury to domestic companies injured by unfair foreign trade practices. In accordance with the CDSOA, which expired in 2007, the Company filed claims to receive its appropriate share of the import duties collected. In 2010, 2009 and 2008 the Company received \$32,000, \$551,000 and \$599,000, respectively, from the U.S. Treasury net of expenses incurred. Future benefits are dependent on the amount of undistributed import duties collected as of September 30, 2007 and the relationship of Dunkirk Specialty Steel's claim in relation to claims filed by other domestic specialty steel producers. The Company expects minimal distributions in the future.

The Company's purchase obligations include the value of all open purchase orders with established quantities and purchase prices, as well as minimum purchase commitments, all made in the normal course of business. At December 31, 2010, the Company's total purchase obligations were \$12.0 million, all of which will be due in year 2011.

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Note 13: Segment and Related Information

The Company is comprised of three operating locations and the corporate headquarters. For segment reporting, the Bridgeville and Titusville facilities have been aggregated into one reportable segment, Universal Stainless & Alloy Products. The Universal Stainless & Alloy Products manufacturing process involves melting, remelting, treating and hot and cold rolling of semi-finished and finished specialty steels. A second reportable segment, Dunkirk Specialty Steel has a manufacturing process involving hot rolling and finishing specialty steel bar, rod and wire products. At December 31, 2010, 82% of the Company's 518 employees are covered by USW collective bargaining agreements.

The accounting policies of both reportable segments are the same as those described in Note 1: Significant Accounting Policies. Sales between the segments are generally made at market-related prices. Corporate assets are primarily cash and cash equivalents, prepaid expenses, deferred income taxes, and property, plant and equipment.

| <u>For the years ended December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|--|-------------------------|--------------------------|-------------------------|
| NET SALES | | | |
| Universal Stainless & Alloy Products | \$173,294 | \$108,319 | \$206,638 |
| Dunkirk Specialty Steel | 56,600 | 37,245 | 66,248 |
| Intersegment | (40,471) | (20,657) | (37,780) |
| | <u>\$189,423</u> | <u>\$124,907</u> | <u>\$235,106</u> |
| OPERATING INCOME (LOSS) | | | |
| Universal Stainless & Alloy Products | \$ 17,311 | \$ (2,396) | \$ 15,680 |
| Dunkirk Specialty Steel | 4,296 | (2,261) | 3,412 |
| Intersegment | (1,184) | — | — |
| | <u>\$ 20,423</u> | <u>\$ (4,657)</u> | <u>\$ 19,092</u> |
| INTEREST EXPENSE AND OTHER FINANCING COSTS ^A | | | |
| Universal Stainless & Alloy Products | \$ 412 | \$ 30 | \$ 28 |
| Dunkirk Specialty Steel | 40 | 59 | 77 |
| | <u>\$ 452</u> | <u>\$ 89</u> | <u>\$ 105</u> |
| OTHER INCOME, NET | | | |
| Universal Stainless & Alloy Products | \$ 40 | \$ 62 | \$ 221 |
| Dunkirk Specialty Steel ^B | 52 | 633 | 690 |
| | <u>\$ 92</u> | <u>\$ 695</u> | <u>\$ 911</u> |
| DEPRECIATION AND AMORTIZATION | | | |
| Universal Stainless & Alloy Products | \$ 4,210 | \$ 3,555 | \$ 3,454 |
| Dunkirk Specialty Steel | 1,162 | 1,187 | 605 |
| Corporate | 114 | 117 | 108 |
| | <u>\$ 5,486</u> | <u>\$ 4,859</u> | <u>\$ 4,167</u> |
| CAPITAL EXPENDITURES | | | |
| Universal Stainless & Alloy Products | \$ 6,831 | \$ 11,496 | \$ 6,496 |
| Dunkirk Specialty Steel | 425 | 874 | 6,236 |
| Corporate | 226 | 24 | 173 |
| | <u>\$ 7,482</u> | <u>\$ 12,394</u> | <u>\$ 12,905</u> |

^A Includes amortization of deferred financing costs of \$17,000, \$24,000 and \$19,000 for the years ended December 31, 2010, 2009 and 2008, respectively.

^B Includes net receipt of import duties of \$32,000 in 2010, \$551,000 in 2009 and \$599,000 in 2008.

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| <u>December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> |
|---|-------------------------|------------------|
| ASSETS | | |
| Universal Stainless & Alloy Products | \$128,281 | \$ 96,047 |
| Dunkirk Specialty Steel | 42,199 | 31,133 |
| Corporate (including cash of \$34.9 million and \$42.3 million) | 42,188 | 54,534 |
| | <u>\$212,668</u> | <u>\$181,714</u> |

The following table presents net sales by product line:

| <u>For the years ended December 31,</u> <i>(dollars in thousands)</i> | <u>2010</u> | <u>2009</u> | <u>2008</u> |
|--|-------------------------|------------------|------------------|
| Stainless steel | \$142,302 | \$ 98,069 | \$172,222 |
| Tool steel | 26,196 | 9,413 | 39,046 |
| High-strength low alloy steel | 10,310 | 9,235 | 11,936 |
| High-temperature alloy steel | 5,853 | 5,567 | 7,931 |
| Conversion services | 2,719 | 1,203 | 1,941 |
| Other | 2,043 | 1,420 | 2,030 |
| Total net sales | <u>\$189,423</u> | <u>\$124,907</u> | <u>\$235,106</u> |

Sales to the Company's largest customer Carpenter Technology Corporation (CRS) totaled \$25.9 million and accounted for 13.6% of total 2010 sales, and was included in the Universal Stainless & Alloy Products segment. The accounts receivable balances from CRS comprised 19% of total accounts receivable at December 31, 2010.

In 2010, the Company derived 5% of its revenues from markets outside of the United States compared with 10% in 2009 and 4% in 2008. The Company has no assets located outside the United States.

Note 14: Selected Quarterly Financial Data (unaudited)

| <i>(dollars in thousands, except per share amounts)</i> | <u>First Quarter</u> | <u>Second Quarter</u> | <u>Third Quarter</u> | <u>Fourth Quarter</u> |
|---|----------------------|-----------------------|----------------------|-----------------------|
| 2010 DATA | | | | |
| Net sales | \$ 34,679 | \$ 51,291 | \$ 51,870 | \$ 51,583 |
| Gross profit margin | 4,919 | 9,697 | 10,315 | 8,841 |
| Operating income | 2,259 | 6,397 | 6,314 | 5,453 |
| Provision for income taxes | 736 | 2,140 | 2,107 | 1,838 |
| Net income | 1,427 | 4,155 | 4,091 | 3,569 |
| Earnings per common share: | | | | |
| Basic | \$ 0.21 | \$ 0.61 | \$ 0.60 | \$ 0.53 |
| Diluted | \$ 0.21 | \$ 0.61 | \$ 0.60 | \$ 0.52 |
| 2009 DATA | | | | |
| Net sales | \$ 42,186 | \$ 30,763 | \$ 25,286 | \$ 26,672 |
| Gross profit margin | (1,678) | 2,671 | 2,715 | 3,298 |
| Operating income (loss) | (6,415) | 565 | 457 | 736 |
| Provision (benefit) for income taxes | (2,583) | 973 | 197 | 320 |
| Net income (loss) | (3,826) | (400) | 312 | 956 |
| Earnings (loss) per common share: | | | | |
| Basic | \$ (0.57) | \$ (0.06) | \$ 0.05 | \$ 0.14 |
| Diluted | \$ (0.57) | \$ (0.06) | \$ 0.05 | \$ 0.14 |

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The Company's fourth quarter 2010 sales increased 93% from the fourth quarter 2009 on an 84% increase in tons shipped as shipments to rerollers, service centers, and forgers increased substantially from the 2009 fourth quarter. In total, sales to rerollers, service centers, and forgers increased 446%, 98% and 17%, respectively, from the 2009 fourth quarter. The Company's 2010 fourth quarter earnings were positively impacted from the receipt of import duties of \$32,000. The Company's 2009 fourth quarter earnings were positively impacted by the receipt of import duties of \$551,000.

Earnings per share amounts for each quarter are required to be computed independently. As a result, their sum may not equal the total year earnings per share amounts.

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ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A. CONTROLS AND PROCEDURES

The Company's management, including the Company's Chairman, President and Chief Executive Officer and the Vice President of Finance, Chief Financial Officer and Treasurer, performed an evaluation of the effectiveness of the Company's disclosure controls and procedures. Based on that evaluation, the Company's Chairman, President and Chief Executive Officer and the Vice President of Finance, Chief Financial Officer and Treasurer concluded that, as of the end of the fiscal year covered by this Annual Report on Form 10-K, the Company's disclosure controls and procedures are effective. Management's Report on the Company's internal control over financial reporting is included in Item 8 of this Annual Report on Form 10-K under the caption "Management's Report on Internal Control Over Financial Reporting" and is incorporated herein by reference. The Company's independent registered public accounting firm has issued a report on management's maintenance of effective internal control over financial reporting and is set forth in Item 8 of this Annual Report on Form 10-K under the caption "Report of Independent Registered Public Accounting Firm" and is incorporated herein by reference.

During the last fiscal quarter of the fiscal year ended December 31, 2010, there were no changes in the Company's internal control over financial reporting which have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

ITEM 9B. OTHER INFORMATION

None.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information concerning the directors of the Company is set forth in the Proxy Statement for the 2011 Annual Meeting of Stockholders (the "Proxy Statement") to be sent to stockholders in connection with the Company's 2011 Annual Meeting of Stockholders, under the heading "Proposal No. 1— Election of Directors," which information is incorporated by reference. With the exception of the information specifically incorporated herein by reference, the Company's Proxy Statement is not to be deemed filed as part of this report for the purposes of this Item.

In addition to the information set forth under the caption "Executive Officers" in Part I of this report, the information concerning our directors required by this item is incorporated and made part hereof by reference to the material appearing under the heading "Nominees for Election as Directors" in the Company's Proxy Statement, which will be filed with the SEC, pursuant to Regulation 14A, not later than 120 days after the end of the 2010 fiscal year. Information concerning the Audit Committee and its "audit committee financial expert" required by this item is incorporated and made part hereof by reference to the material appearing under the heading "Committees of the Board of Directors" in the Proxy Statement. Information required by this item regarding compliance with Section 16(a) of the Exchange Act is incorporated and made a part hereof by reference to the material appearing under the heading "Security Ownership of Certain Beneficial Owners and Management" in the Proxy Statement. Information concerning the executive officers of the Company is contained in Part I of this Annual Report on Form 10-K under the caption "Executive Officers."

The Company has adopted a Code of Business Conduct and Ethics that applies to all directors and employees, including its principal executive officer and principal financial officer. A copy is available, free of charge, through the Company's website at <http://www.univstainless.com>. Information on the Company's website is not part of this Annual Report on Form 10-K. The Company intends to timely disclose any amendment of or waiver under the Code of Business Conduct and Ethics on its website and will retain such information on its website as required by applicable SEC rules.

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ITEM 11. EXECUTIVE COMPENSATION

The information concerning executive compensation is set forth in the Proxy Statement under the heading “Executive Compensation,” which information is incorporated by reference. With the exception of the information specifically incorporated herein by reference, the Proxy Statement is not to be deemed filed as part of this report for the purposes of this Item.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information concerning security ownership of certain beneficial owners and management is set forth in the Proxy Statement under the heading “Security Ownership of Certain Beneficial Owners and Management,” which information is incorporated by reference. With the exception of the information specifically incorporated herein by reference, the Proxy Statement is not to be deemed filed as part of this report for the purposes of this Item.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

The information concerning certain relationships and related transactions, and director independence is set forth in the Proxy Statement under the heading “The Board of Directors,” which information is incorporated by reference. With the exception of the information specifically incorporated herein by reference, the Proxy Statement is not to be deemed filed as part of this report for the purposes of this Item.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information concerning principal accountant fees and services is set forth in the Proxy Statement under the heading “Principal Accountant Fees and Services,” which information is incorporated by reference. With the exception of the information specifically incorporated herein by reference, the Proxy Statement is not to be deemed filed as part of this report for the purposes of this Item.

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PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

The following documents are filed as part of this Form 10-K:

1) Financial Statements

The list of financial statements required by this item is set forth in Item 8, "Financial Statements and Supplementary Data" and is incorporated herein by reference.

2) Consolidated Financial Statement Schedules

Schedule II – Valuation and Qualifying Accounts

| <u>For the Years Ended December 31, 2007, 2008 and 2009</u> <i>(Dollars in thousands)</i> | <u>Balance at</u> <u>Beginning of Year</u> | <u>Charged to Costs</u> <u>and Expenses</u> | <u>Deductions/</u> <u>Net</u> <u>Charge-</u> <u>Offs</u> | <u>Balance at</u> <u>End of Year</u> |
|--|---|--|---|---|
| INVENTORY RESERVES: | | | | |
| Year ended December 31, 2008 | \$ 2,195 | \$ 4,039 | \$ (3,038) | \$ 3,196 |
| Year ended December 31, 2009 | 3,196 | 1,292 | (3,336) | 1,152 |
| Year ended December 31, 2010 | <u>1,152</u> | <u>399</u> | <u>(565)</u> | <u>986</u> |
| ALLOWANCE FOR DOUBTFUL ACCOUNTS: | | | | |
| Year ended December 31, 2008 | \$ 311 | \$ 13 | \$ (6) | \$ 330 |
| Year ended December 31, 2009 | 330 | 1,823 | (21) | 2,132 |
| Year ended December 31, 2010 | <u>2,132</u> | <u>274</u> | <u>(272)</u> | <u>2,134</u> |

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3) Exhibits

| <u>EXHIBIT NUMBER</u> | <u>DESCRIPTION</u> | |
|-----------------------|--|---|
| 3.1 | Amended and Restated Certificate of Incorporation | Incorporated herein by reference to Exhibit 3.1 to Registration No. 33-85310. |
| 3.2 | Amended and Restated By-laws of the Company | Incorporated herein by reference to Exhibit 3.1 on Form 8-K filed November 27, 2007. |
| 4.1 | Specimen Copy of Stock Certificate for shares of Common Stock | Incorporated herein by reference to Exhibit 4.1 to the Company's Annual Report on Form 10-K for the year ended December 31, 1998. |
| 10.1 | Stockholders Agreement dated as of August 1, 1994, by and among the Company and its existing stockholders | Incorporated herein by reference to Exhibit 10.1 to Registration No. 33-85310. |
| 10.2 | Credit Agreement, dated as of February 27, 2009, between the Company and PNC Bank, National Association | Incorporated herein by reference to Exhibit 10.1 to the Company's Quarterly Report on Form 10-Q for the six-months ended June 30, 2010. |
| 10.3 | Employment Agreement dated December 21, 2007 between the Company and Dennis M. Oates | Incorporated herein by reference to Exhibit 10.7 to the Company's Annual Report on Form 10-K for the year ended December 31, 2007. |
| 10.4 | Employment Agreement dated February 21, 2008 between the Company and Paul McGrath | Incorporated herein by reference to Exhibit 10.4 to the Company's Annual Report on Form 10-K for the year ended December 31, 2007. |
| 10.5 | Employment Agreement dated July 12, 2010 between the Company and Douglas M. McSorley | Incorporated herein by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K dated July 19, 2010.. |
| 10.6 | Employment Agreement dated February 11, 2009 between the Company and William W. Beible, Jr. | Incorporated herein by reference to Exhibit 10.6 to the Company's Annual Report on Form 10-K for the year ended December 31, 2008. |
| 10.7 | Employment Agreement dated April 21, 2008 between the Company and Christopher M. Zimmer | Filed herewith. |
| 10.8 | Stock Incentive Plan | Incorporated herein by reference to Appendix A of the Company's Definitive Proxy Statement dated April 19, 2010. |
| 10.9 | Promissory Note, dated as of February 13, 2002, between the Company and New York Job Development Authority | Incorporated herein by reference to Exhibit 10.24 to the Company's Annual Report on Form 10-K for the year ended December 31, 2001. |
| 10.10 | Promissory Note, dated as of February 14, 2002, between the Company and New York Job Development Authority | Incorporated herein by reference to Exhibit 10.25 to the Company's Annual Report on Form 10-K for the year ended December 31, 2001. |
| 21.1 | Subsidiaries of Registrant | Filed herewith. |
| 23.1 | Consent of Schneider Downs & Co., Inc. | Filed herewith. |
| 24.1 | Powers of Attorney | Included on the signature page herein. |
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | Filed herewith. |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 | Filed herewith. |
| 32.1 | Certification of Chief Executive Officer and Chief Financial Officer pursuant to Rule 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 | Filed herewith. |

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SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Report on Form 10-K to be signed on its behalf by the undersigned, thereunto duly authorized, on March 3, 2011.

UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.

By: /s/ Dennis M. Oates
Dennis M. Oates
Chairman, President and Chief Executive Officer

POWER OF ATTORNEY

Each of the officers and directors of Universal Stainless & Alloy Products, Inc., whose signature appears below in so signing also makes, constitutes and appoints Dennis M. Oates and Paul A. McGrath, and each of them acting alone, his true and lawful attorney-in-fact, with full power of substitution, for him in any and all capacities, to execute and cause to be filed with the SEC any and all amendment or amendments to this Report on Form 10-K, with exhibits thereto and other documents connected therewith and to perform any acts necessary to be done in order to file such documents, and hereby ratifies and confirms all that said attorney-in-fact, or his substitute or substitutes, may do or cause to be done by virtue hereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the Registrant in the capacities and on the dates indicated.

| <u>SIGNATURE</u> | <u>TITLE</u> | <u>DATE</u> |
|---|---|---------------|
| <u>/s/ Dennis M. Oates</u> Dennis M. Oates | Chairman, President, Chief Executive Officer and Director (Principal Executive Officer) | March 3, 2011 |
| <u>/s/ Douglas M. McSorley</u> Douglas M. McSorley | Vice President of Finance, Chief Financial Officer and Treasurer (Principal Financial and Accounting Officer) | March 3, 2011 |
| <u>/s/ Christopher L. Ayers</u> Christopher L. Ayers | Director | March 3, 2011 |
| <u>/s/ Douglas M. Dunn</u> Douglas M. Dunn | Director | March 3, 2011 |
| <u>/s/ M. David Komblatt</u> M. David Komblatt | Director | March 3, 2011 |
| <u>/s/ Udi Toledano</u> Udi Toledano | Director | March 3, 2011 |

EMPLOYMENT AGREEMENT

THIS AGREEMENT made as of the 21st day of April 2008, by and between UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC., a Delaware corporation (the "Company"), and Christopher M. Zimmer (the "Executive").

WITNESSETH:

In consideration of the covenants and agreements herein contained, and intending to be legally bound hereby, the Company and Executive agree as follows:

Article 1. - Employment

1.1. **Employment.** The Company agrees to employ Executive, and Executive agrees to serve the Company, for the period stated in Article 2 hereof (the "Term of Employment") and upon the other terms and conditions herein provided.

1.2. **Position and Responsibilities.** The Company employs Executive, and Executive agrees to serve as Vice President of Sales & Marketing of the Company and to accept such other responsibilities as may be assigned to Executive by the Company from time to time during the Term of Employment.

1.3. **Duties.** During the Term of Employment, Executive shall devote all of his business time, attention, skill and efforts to the faithful performance of his duties hereunder.

Article 2. - Term

The Term of Employment shall commence as of April 28, 2008 (the "Effective Date"), and shall continue until April 31, 2009 (the "Initial Term"). Thereafter, subject to the termination provisions of this Agreement, this Agreement will be automatically extended for successive one year terms unless either party provides written notice to the other party on or before March 1 of any year, of his or its election not to extend the term of this Agreement.

Article 3. - Compensation

3.1. **Salary.** As compensation to the Executive for the performance of services hereunder, the Company shall pay to the Executive a base salary (the "Salary") of \$170,000.00. Installments of the Salary shall be paid to the Executive in accordance with the standard procedure of the Company, which at the present time is once every two weeks. During the period of this Agreement, Executive's salary shall be reviewed at least annually and may be increased if the Board of Directors of the Company (the "Board") acting after approval of the Compensation Committee (the "Compensation Committee"), determines that an increase is appropriate on the basis of the types of factors it generally takes into account in increasing the salaries of employees similarly situated in the Company.

3.2. **Reimbursement of Expenses.** The Company will reimburse the Executive for those customary and necessary business expenses incurred by him in the performance of his duties and activities on behalf of the Company. Except as provided in this Agreement, such expenses will be reimbursed only on presentation by the Executive of appropriate documentation to substantiate such expenses pursuant to the policies and procedures of the Company governing reimbursement of business expenses to its executives.

3.3. **Participation in Plans.** The Executive shall be entitled to participate in any life, medical, dental, health, hospitalization, travel, accident and/or disability insurance plans and in any sick leave and/or salary continuation plan, vacation (which shall not be less than three (3) weeks per year), holiday pay, retirement or employee benefit plan or program generally offered by the Company to its salaried employees. In addition, Executive shall be entitled to participate in the variable incentive compensation plan and the perquisites described on Schedule A attached hereto.

Article 4. - Termination of Employment

4.1. **Definitions.** For the purposes hereof:

(a) “**Disability**” shall be deemed to have occurred when the Executive is eligible, due to a health condition, to collect benefits under the Company’s short term disability plan and has been determined by the Board of Directors to be unable to perform substantially the duties associated with the Executives position for a period of three months.

(b) “**Cause**” shall mean any of the following: (i) Executive’s personal dishonesty or willful misconduct; (ii) Executive’s willful violation of any law or material rule or regulation, provided that such violation is demonstrably injurious to the assets, operations or business prospects of the Company; (iii) the conversion or embezzlement for the personal benefit of the Executive of corporate funds or property or a material business opportunity of the Company; (iv) the misuse by the Executive for his personal benefit of any trade secrets or other information of the Company in violation of the provisions of Article 7 of this Agreement; or (v) Executive’s material breach of any other provision of this Agreement which is not cured within thirty (30) days of receipt of notice of such breach from Company.

(c) “**Good Reason**” shall, absent the Executive’s consent to such action, mean the occurrence of any one of the following: (i) following a Change of Control, the removal of the Executive as Vice President of Sales & Marketing (by reason other than death, Disability or Cause); (ii) any breach by the Company of a material obligation under this Agreement; (iii) a substantial and material alteration in the nature or status of Executive’s duties and responsibilities that renders the Executive’s position to be of substantially less responsibility or scope; (iv) a material reduction by the Company in the Executive’s Salary, except for proportional across-the-board salary reductions similarly affecting all senior executives of the Company; or (v) any material reduction by the Company of the benefits, taken as a whole, enjoyed by the Executive on the date of this Agreement under any savings, life insurance, medical, health and accident, disability or other employee welfare benefit plans or programs, including vacation programs, provided that this paragraph (v) shall not apply to any proportional across the board reduction or action similarly affecting all senior executives of the Company.

Notwithstanding the foregoing, no event of “Good Reason” shall be deemed to have occurred unless Executive provides to the Chairman of the Compensation Committee of the Board of Directors of the Company written notice of the facts and circumstances which Executive believes constitutes Good Reason under this Section 4.1(c) within 30 days of such initial occurrence and such facts and circumstances are not corrected or otherwise cured by the Company within thirty (30) days of receipt thereof. Termination by Executive for Good Reason must occur within 90 days of the initial occurrence of the Good Reason event.

For purposes of this Agreement, a Change of Control shall be deemed to have occurred on the earlier of (x) if, in any transaction or series of related transactions consummated in a ninety day period, more than fifty percent (50%) of the then outstanding voting common stock of the Company is sold to a person or group; (y) a merger or consolidation of the Company and another entity in which the Company is not the surviving corporation or in which more than fifty percent(50%) of the equity ownership of the Company changes, or (z) the sale of 50% or more of all of the assets of the Company.

(d) “**Notice of Termination**” shall mean written notice which shall indicate the specific termination or resignation provisions in this Agreement relied upon and shall set forth in reasonable detail the facts and circumstances claimed to provide a basis for such termination or resignation under the provision so indicated and the Company shall submit to the Executive a certified statement signed by the Chairman of the Compensation Committee of the Board of Directors of the Company approving such termination in the case of a Termination by the Company for Cause or Without Cause.

(e) “**Date of Termination**” shall mean the date specified in the Notice of Termination as the effective date the Executive’s employment is terminated for any reason or the Executive’s effective date of resignation, which ever is earlier.

Article 5. - Compensation Upon Termination

5.1. **Death.** If the Executive’s employment hereunder terminates by reason of his death, his beneficiaries shall be entitled to receive from the Company such amounts as are then provided pursuant to plans, programs or arrangements currently in effect or as approved from time to time by the Board of Directors.

5.2. **Disability.** If the Executive’s employment hereunder terminates by reason of his Disability, the Executive shall be entitled to receive such amounts as are then provided pursuant to Company’s then existing disability plans, programs or arrangements. Notwithstanding any provisions herein to the contrary, the Executive shall be entitled to receive all benefits to which the Executive is entitled as a terminated employee under the terms of any of the Company’s qualified employee benefit plans and any other plan, program or arrangement relating to retirement or other benefits including, without limitation, any employee stock ownership plan or any plan now in effect or which is established (with approval of the Board of Directors) as a supplement to any of the forenamed plans, except as otherwise provided in such plans as a result of the Executive’s termination of employment.

5.3. Cause. If the Executive's employment hereunder is terminated by the Company for Cause, the Company shall pay to the Executive his full base Salary through the Date of Termination but at a rate no greater than that in effect at the time Notice of Termination is given, and the Company shall have no further obligations to the Executive under this Agreement.

5.4. By the Company Without Cause or by the Executive by Resignation for Good Reason. If the Executive's employment hereunder is terminated by the Company without Cause or is terminated by the Executive pursuant to his resignation for Good Reason, then the Executive shall be entitled to the benefits provided below, which shall constitute complete satisfaction of the obligations of the Company to the Executive under this Agreement:

(a) The Company shall pay the Executive his full annual base Salary through the Date of Termination at the rate in effect at the time Notice of Termination is given.

(b) Subsequent to the Date of Termination, the Company shall pay as severance pay to the Executive, a lump sum severance payment equal to 18 months of the Executive's base monthly Salary at the rate in effect at the time Notice of Termination is given. Such payment shall be less applicable taxes and mandatory deductions, paid on or before the 30th calendar day after the Date of Termination.

(c) The Company will provide health care benefits under the group policies covering the other corporate employees covering Medical, Dental, Vision and Prescription Drugs, subject to any changes made to the group policies, as provided prior to the Date of Termination for the Executive and eligible dependents, that were covered prior to any Date of Termination, for a period of eighteen (18) months at no cost to the Executive. This period will not reduce the eligible COBRA period.

(d) The Executive shall not be required to mitigate the amount of any payments provided for in this Agreement by seeking other employment or otherwise, nor shall the amount of any payment provided for in this Agreement be reduced by any compensation earned by the Executive as the result of employment by another employer, or otherwise.

(e) Notwithstanding any provisions herein to the contrary, the Executive shall be entitled to receive all benefits to which the Executive is entitled as a terminated employee under the terms of any of the Company's qualified employee benefit plans and any other plan, program or arrangement relating to retirement or other benefits including, without limitation, any employee stock ownership plan or any plan now in effect or which is established (with approval of the Board of Directors) as a supplement to any of the forenamed plans, except as otherwise provided in such plans as a result of the Executive's termination of employment.

Article 6. - Duties of Executive After Termination of Employment

Following any termination of Executive's employment and for a period of ninety (90) days thereafter, the Executive shall fully cooperate with the Company in all matters relating to the winding up and orderly transfer of the Executive's work on behalf of the Company. Not later than the effective date of any termination of the employment, the Executive will immediately deliver to the Company any and all of the Company's property of any kind or nature whatsoever in the Executive's possession, custody or control, including, without limitation any and all Confidential Information as that term is defined in Section 7 of this Agreement.

Article 7. - Confidential Information; Invention Assignment

7.1. Confidential Relationship. Executive understands and agrees that all company manuals, company policies, marketing plans and surveys, product designs, schematics, specifications and product location and installation data, formulae, processes, methods, machines, compositions, customer information, ideas, inventions, financial information and plans of the Company and all records, correspondence, files, customer lists, data and other information pertaining to or concerning the Company, its principals, vendors and customers (collectively the "**Confidential Information**") contain valuable confidential information that is owned by the Company, and, therefore, that during the period of employment hereunder and at all times thereafter, Executive shall not utilize such Confidential Information for his own benefit or for the benefit of any person or entity other than the Company, nor shall he divulge or communicate any such Confidential Information to any person or entity without the express authorization of the Company. Confidential Information shall not include any information that is or becomes generally available to the public other than as a result of a disclosure by Executive. The Executive agrees that, on the termination of his employment, he will immediately surrender to the Company any and all Confidential Information in his possession pertaining to the Company and its business.

7.2. Assignment of Rights. All inventions, discoveries, designs, developments, technology, computer programs, writings and reports that are made or conceived of by the Executive in the course of his employment with the Company, whether or not patentable or copyrightable, shall become and remain the sole property of the Company without additional compensation to Executive. The Executive recognizes that all such works shall be considered works-for-hire and hereby transfers and assigns any right, title, copyright

and interest that Executive acquires in such works to the Company and will, from time to time, give the Company all reasonable assistance, execute all papers and do all things that may reasonably be required to protect and preserve the rights of the Company in such works.

7.3. No Breach of Other Obligations. The Executive represents that, in the course of performing services for the Company, he will not breach any agreement he may have with others with respect to confidential information, and will not bring to the Company or use in any way any materials or documents obtained from others under an agreement of confidentiality.

Article 8. - Source of Payments

All payments provided for under this Agreement shall be paid in cash from the general funds of the Company and no special or separate fund shall be established and no other segregation of assets shall be made to assure payment. No trust or fiduciary relationship with respect to payments shall be deemed created hereby and, to the extent that any person acquires a right to receive payments hereunder, such right shall be no greater than the rights of a general creditor of the Company.

Article 9. - Miscellaneous

9.1. Indulgences, Etc. Neither the failure nor any delay on the part of either party to exercise any right, remedy, power or privilege under this Agreement shall operate as a waiver thereof, nor shall any single or partial exercise of any right, remedy, power or privilege preclude any other or further exercise of the same or of any other right, remedy, power or privilege, nor shall any waiver of any right, remedy, power or privilege with respect to any occurrence be construed as a waiver of such right, remedy, power or privilege with respect to any other occurrence.

9.2. Notices. All notices or communications hereunder shall be in writing, addressed as follows:

To the Company:

Dennis M. Oates, President and CEO
Universal Stainless & Alloy Products, Inc.
600 Mayer Street
Bridgeville, PA 15017

To the Executive:

Christopher Zimmer
4404 Sunflower Court
Doylestown, PA 18902

Any such notice or communication shall be sent by certified or registered mail, return receipt requested, postage prepaid, addressed as above (or to such other address as such party may designate in writing from time to time), and the actual date of receipt, as shown by the receipt therefor, shall determine the time at which notice was given.

9.3. Assignment; Agreement. This Agreement shall be binding upon and inure to the benefit of the heirs and personal representatives of the Executive and the successors and assigns of the Company, but neither this Agreement nor any rights hereunder shall be assignable or otherwise subject to hypothecation by the Executive.

9.4. Entire Agreement; Amendment. This Agreement represents the entire agreement of the parties with respect to the subject matter hereof. This Agreement may be amended or any provision hereof waived at any time only by written agreement of the parties hereto.

9.5. Governing Law. This Agreement and its validity, interpretation, performance and enforcement shall be governed by the laws of the Commonwealth of Pennsylvania, other than the conflict of laws provisions of such laws.

9.6. Severability. If, for any reason, any provision of this Agreement is held invalid, such invalidity shall not affect any other provision of this Agreement not held so invalid, and each such other provision shall to the full extent consistent with law continue in full force and effect. If any provision of this Agreement shall be held invalid in part, such invalidity shall in no way affect the remainder of such provision that is not held so invalid, and the remainder of such provision, together with all other provisions of this Agreement, shall to the full extent consistent with law continue in full force and effect.

9.7. Headings. The Article and Section headings in this Agreement are for convenience of reference only; they form no part of this Agreement and shall not affect its interpretation.

9.8. Counterparts. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, and all of which together shall constitute one and the same instrument.

IN WITNESS WHEREOF, the Company and the Executive have duly executed this Agreement as of the day and year first written above.

UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.

By: /s/ Dennis M. Oates

Title: President and CEO

EXECUTIVE

/s/ Christopher M. Zimmer

Christopher M. Zimmer

Schedule A
Incentive Compensation
And Perquisites

1. **Incentive Compensation.** Executive will be entitled to participate in the Company's variable incentive compensation plan. The maximum award under such plan for the Executive shall be 100% of his annual base Salary. A guaranteed minimum incentive compensation award based on continued employment for Executive shall be \$125,000.00. The payments of the guaranteed variable incentive compensation shall be as follows: \$25,000 payable upon hire, \$50,000 paid in the last pay of December 2008 and \$50,000 payable in the last pay of March 2009, subject to the terms and conditions of variable incentive compensation plan.

2. **Stock Options.** Executive shall be granted 15,000 stock options pursuant to the Company's stock option plan. The exercise price of the stock options will be the closing price of the Company's common stock on the Effective Date. One forth of the stock options will vest on each of the first four anniversaries of the Effective Date. All stock options shall be subject to the terms and conditions of a separate stock option agreement to be entered into by Executive and the Company.

3. **Automobile.** The Company shall provide the Executive with a monthly car allowance of \$550.00 per month.

4. **Moving Expenses.** A moving and relocation allowance will be provided as follows: \$100,000 (subject to mandatory withholdings) to be paid as follows: \$50,000 upon hire and \$50,000 upon Executive's closing on a residence in the Greater Pittsburgh metropolitan area.

The relocation allowance amount of \$100,000 is subject to your agreeing to work for Universal Stainless & Alloy Products, Inc., as the Vice President of Sales and Marketing for a period of at least two (2) years. Should you terminate your employment before that time, the relocation allowance amount of \$100,000 is to be returned to Universal Stainless & Alloy Products, Inc.

5. **Club Membership.** The Company shall pay the membership dues for Executive at South Point Golf Club. Charges related to the use of the Club shall be the responsibility of the Executive.

6. **Temporary Living Expense.** For a period of five (5) months starting with the commencement of employment the Company shall reimburse Executive for the cost of local extended stay hotel expenses and a per diem of \$25.00 for meals.

SUBSIDIARIES OF REGISTRANT

Below are the only active wholly-owned subsidiaries of the registrant and its jurisdiction of organization.

Doing Business As

Dunkirk Specialty Steel, LLC
USAP Holdings, Inc.

State of Incorporation

Delaware
Delaware

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (No. 33-90970, No. 333-13509, No. 333-13511, No. 333-13599, No. 333-100263 and No. 333-136984) of Universal Stainless & Alloy Products, Inc. of our report dated March 3, 2011 relating to the consolidated financial statements and financial statement schedule and the effectiveness of internal control over financial reporting, which appears in this Form 10-K for the year ended December 31, 2010.

/s/ Schneider Downs & Co., Inc.

Schneider Downs & Co., Inc.

Pittsburgh, Pennsylvania

March 3, 2011

CERTIFICATION

I, Dennis M. Oates, certify that:

1. I have reviewed this Annual Report on Form 10-K of Universal Stainless & Alloy Products, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 3, 2011

/s/ Dennis M. Oates

Dennis M. Oates

Chairman, President and Chief Executive Officer

(Principal Executive Officer)

CERTIFICATION

I, Douglas M. McSorley, certify that:

1. I have reviewed this Annual Report on Form 10-K of Universal Stainless & Alloy Products, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: March 3, 2011

/s/ Douglas M. McSorley

Douglas M. McSorley
Vice President of Finance,
Chief Financial Officer and Treasurer
(Principal Financial and Accounting Officer)

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350
AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report on Form 10-K of Universal Stainless & Alloy Products, Inc. (the "Company") for the year ended December 31, 2010 as filed with the SEC on the date hereof (the "Report"), each of the undersigned, in the capacities and on the dates indicated below, hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

UNIVERSAL STAINLESS & ALLOY PRODUCTS, INC.

Date: March 3, 2011

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

Date: March 3, 2011

/s/ Douglas M. McSorley
Douglas M. McSorley
Vice President of Finance,
Chief Financial Officer and Treasurer
(Principal Financial and Accounting Officer)