

SIFCO INDUSTRIES INC
Form 10-K
November 30, 2012

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For the fiscal year ended September 30, 2012

or

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

For the transition period from to

Commission file number 1-5978

SIFCO Industries, Inc.

(Exact name of registrant as specified in its charter)

Ohio
(State or other jurisdiction of
incorporation or organization)

34-0553950
(I.R.S. Employer
Identification No.)

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970 East 64th Street, Cleveland Ohio
(Address of principal executive offices)

44103
(Zip Code)

(216) 881-8600

(Registrant's telephone number, including area code)

Securities Registered Pursuant to Section 12(b) of the Act:

Common Shares, \$1 Par Value
(Title of each class)

NYSE MKT
(Name of each exchange on which registered)

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

None.

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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 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, a non-accelerated filer, or a smaller reporting company (as defined in Rule 12b-2 of the Exchange Act).

large accelerated filer accelerated filer
non-accelerated filer 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 and non-voting common equity held by non-affiliates computed by reference to the price at which the common equity was last sold, as of the last business day of the registrant's most recently completed second fiscal quarter is \$48,086,083.

The number of the Registrant's Common Shares outstanding at October 31, 2012 was 5,339,571.

Documents incorporated by reference: Portions of the definitive Proxy Statement for the Annual Meeting of Shareholders to be held on January 17, 2013 (Part III).

PART I

Item 1. Business

A. The Company

SIFCO Industries, Inc. (SIFCO or Company), an Ohio corporation, was incorporated in 1916. The executive offices of the Company are located at 970 East 64th Street, Cleveland, Ohio 44103, and its telephone number is (216) 881-8600.

The Company is engaged in the production and sale of a variety of metalworking processes, services and products produced primarily to the specific design requirements of its customers. The processes and services include forging, heat-treating, coating, welding, machining, and selective plating. The products include forged components (both conventional and precision), machined forged parts and other machined metal components, remanufactured component parts for aerospace turbine engines, and selective plating solutions and equipment. The Company's operations are conducted in three business segments: (i) Forged Components Group, (ii) Turbine Component Services and Repair Group and (iii) Applied Surface Concepts Group.

B. Principal Products and Services

1. Forged Components Group

The Forged Components Group (Forge Group) has multiple operations. SIFCO Forge is located in Cleveland, Ohio; T&W Forge (TWF) is located in Alliance, Ohio and Quality Aluminum Forge (QAF) is located in Orange, California. As discussed more fully in Note 12 to the consolidated financial statements included in Item 8, on October 28, 2011, SIFCO completed the purchase of the forging business and substantially all related operating assets from GEL Industries, Inc. (DBA Quality Aluminum Forge), which business is operated in QAF's Orange and Long Beach, California facilities. This segment of the Company's business consists principally of the manufacture of forged components for aerospace and energy applications. As a part of the Forge Group's manufacturing process, the business performs forging, heat-treating and precision component machining.

Operations

The Company's Forge Group is a manufacturer of forged components with capability ranging in size from 2 to 1,100 pounds (depending on configuration and alloy), primarily in various steel, titanium and aluminum alloys, utilizing a variety of processes for applications principally in the aerospace and energy markets. The Forge Group's products include: original equipment manufacturers (OEM) and aftermarket components for aircraft and industrial gas turbine engines; structural airframe components; aircraft landing gear components; wheels and brakes; critical rotating components for helicopters; and commercial/industrial products. The Forge Group also provides heat-treatment, surface-treatment, non-destructive testing and select machining of forged components.

The Forge Group generally has multiple sources for its raw materials, which consist primarily of high quality metals essential to this business. Suppliers of such materials are located throughout North and South America and Europe. The Forge Group generally does not depend on a single source for the supply of its materials. Due to the limited supply of certain raw materials, some material is provided by a small number of suppliers; however, the Forge Group believes that its sources are adequate for its business. SIFCO Forge, TWF and QAF are ISO 9001:2000 registered with SIFCO Forge and QAF also being AS 9100:2001 certified. In addition, the Forge Group's chemical etching/milling, non-destructive testing, and heat-treating facilities are NADCAP (National Aerospace and Defense Contractors Accreditation Program) accredited.

Industry

The performance of the domestic and international air transport industry as well as government defense spending and the energy industry directly and significantly impact the performance of the Forge Group.

The air transport industry's long-term outlook is for continued, steady growth. Such outlook suggests the need for additional aircraft and, therefore, growth in the requirement for airframe and turbine engine components. The financial condition of the global commercial airline industry continues to see improvement. This improvement is due to strong demand in both air freight and

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passenger traffic. The air transport industry has recently benefited from several favorable trends, including: (i) projected growth in air traffic and (ii) major replacement and refurbishment cycles driven by the desire for more fuel efficient aircraft and fleet commonality. There has been recent improvement in aircraft capacity utilization due to the increase in air freight and passenger traffic, which is driving demand for additional capacity. In addition to the traditional markets, emerging markets in Asia and the

Middle East are driving demand for aircraft as more people are flying today than has been the case in recent past. Aircraft capacity is returning to the market at about the same pace as the growth in demand for such capacity. The Forge Group believes this pattern should continue with the long-term steady growth projected by the air transport industry. The Forge Group also supplies new and spare components for military aircraft, including helicopters. Military spending has continued to be relatively strong and level in recent years. As a result of military initiatives, there has been continuing demand for both new and spare components for military customers. The Forge Group's current outlook for the air transport industry is cautiously optimistic while the military segment remains stable, yet subject to potential changes in defense spending decisions.

The long-term outlook for the energy industry is for steady, continued growth. The related demand for industrial gas turbine units will continue with the increased demand from developing countries. The need for electrical power generation will be satisfied, in part, by industrial gas turbines. While no one source will meet the world's power requirements, industrial gas turbines are increasingly being adapted to additional use applications to improve the efficiency and reliability of power projects.

It is difficult to determine at this time what the long-term impact of these factors may be on the demand for products provided by the Forge Group. Lack of continued improvement in the global economy could result in increased credit risk associated with serving the airlines and/or their suppliers. However, the Forge Group believes that it is poised to take advantage of improvement in order demand from the commercial airframe and engine manufacturers as well as the manufacturers of industrial gas turbine engines.

Competition

While there has been some consolidation in the forging industry, the Forge Group believes there is limited opportunity to increase prices, other than for the pass-through of raw material aluminum, steel and titanium alloy price increases. The Forge Group believes; however, that its demonstrated aerospace and energy expertise along with focus on quality, customer service, SMART (Streamlined Manufacturing Activities to Reduce Time/Cost) initiatives, as well as offering a broad range of capabilities that provide it with an advantage in the primary markets it serves. The Forge Group competes with both U.S. and non-U.S. suppliers of forgings, some of which are significantly larger than the Forge Group. As customers establish new facilities throughout the world, the Forge Group will continue to encounter non-U.S. competition. The Forge Group believes it can expand its markets by (i) acquiring additional forging operations, (ii) broadening its product lines through investment in equipment that expands its manufacturing capabilities and (iii) developing new customers in markets whose participants require similar technical competence and service (as the aerospace and energy industries) and are willing to pay a premium for quality and service.

Customers

During fiscal 2012, the Forge Group had three customers, consisting of various business units of United Technologies Corporation, Rolls-Royce Corporation, and General Electric Corporation, which accounted for 17%, 16% and 12%, respectively, of the Forge Group's net sales. The net sales to these three customers, and to their direct subcontractors, accounted for 55% of the Forge Group's net sales in fiscal 2012. The Forge Group believes that the loss of sales to such customers would result in a materially adverse impact on the business and income of the Forge Group. However, the Forge Group has maintained a business relationship with many of these customers for well over ten years and is currently conducting business with some of them under multi-year agreements. Although there is no assurance that this will continue, historically as one or more major customers have reduced their purchases, the Forge Group has generally been successful in replacing such reduced purchases, thereby avoiding a material adverse impact on the Forge Group. The Forge Group attempts to rely on its ability to adapt its services and operations to changing requirements of the market in general and its customers in particular. No material part of the Forge Group's business is seasonal.

Backlog of Orders

The Forge Group's backlog as of September 30, 2012 increased to \$106.0 million, of which \$87.8 million is scheduled for delivery during fiscal 2013, compared with \$92.2 million as of September 30, 2011, of which \$74.3 million was scheduled for delivery during fiscal 2012. The significant increase in the backlog as of September 30, 2012 compared to September 30, 2011, is primarily attributed to the addition of QAF, which accounted for \$18.1 million of the total backlog as of September 30, 2012. All orders are subject to modification or cancellation by the customer with limited charges. Delivery lead times for certain raw materials (e.g. aerospace grades of steel and titanium alloy) have shortened since the beginning of fiscal 2012 and the Forge Group believes that such lead time changes may ultimately result in a fundamental shift in the ordering pattern of its customers. The Forge Group believes that a likely consequence of such a shift is that customers may place orders later than they previously did, which may result in a decrease, relative to comparable prior year periods, in the Forge Group's backlog. Accordingly, such backlog decrease, to the extent it may occur, may not necessarily be indicative of a reduction in expected future sales.

2. Turbine Component Services and Repair Group

The Company's Turbine Component Services and Repair Group ("Repair Group") has a single operation in Minneapolis, Minnesota. This segment of the Company's business consists principally of the repair and remanufacture of small turbine engine components principally for aerospace applications. As a part of the repair and remanufacture process, the business performs precision component machining and applies high temperature-resistant coatings to turbine engine components.

Operations

The Repair Group requires the procurement of licenses/authority, which certifies that the Repair Group has obtained approval to perform certain proprietary repair processes. Such approvals are generally specific to an engine and its components, a repair process, and a repair facility/location. Without possession of such approvals, a company would be precluded from competing in the aerospace turbine engine component repair business. Approvals are issued by either the original equipment manufacturers ("OEM") of aerospace turbine engines or the Federal Aviation Administration ("FAA").

In general, the Company considers aerospace turbine engines that (i) possess a thrust of less than 17,500 pounds and/or (ii) are used to power aircraft that carry fewer than 100 passengers, to be small aerospace turbine engines. Historically, the Repair Group has elected to procure approvals primarily from the OEMs and currently maintains proprietary repair process approvals issued by certain of the primary small engine OEMs (e.g. Pratt & Whitney Canada, Rolls-Royce, Turbomeca, and Hamilton Sundstrand). In exchange for being granted an OEM approval, the Repair Group is obligated, in certain cases, to pay royalties to the OEM for each type of component repair that it performs utilizing the OEM-approved proprietary repair process. The Repair Group continues to be successful in procuring FAA repair process approvals. There is generally no royalty payment obligation associated with the use of a repair process approved by the FAA. To procure an OEM or FAA approval, the Repair Group is required to demonstrate its technical competence in the process of repairing such turbine engine components.

The development of remanufacturing and repair processes is an ordinary part of the Repair Group's business. The Repair Group continues to invest time and money on research and development activities. The Company's research and development activities in repair processes and high temperature-resistant coatings applied to super-alloy materials have applications in the small aerospace turbine engine markets. Operating costs related to such activities are expensed during the period in which they are incurred. The Repair Group's research and development expense was \$0.7 and \$0.5 million in fiscal 2012 and 2011, respectively.

The Repair Group generally has multiple sources for its raw materials, which consist primarily of investment castings and industrial coating materials essential to this business. Certain items are procured directly from the OEM, or from OEM-certified suppliers, to satisfy repair process requirements. Suppliers of such materials are located throughout North America and Europe. Although certain raw materials may be provided by a limited number of suppliers, the Repair Group generally does not depend on a single source for the supply of its materials and management believes that its sources are adequate for its business.

Industry

The performance of the air transport industry directly and significantly impacts the performance of the Repair Group. The air transport industry's long-term outlook is for continued, steady growth. Such outlook suggests the need for additional aircraft and, therefore, growth in the requirement for aerospace turbine engines and related engine repairs. The financial condition of the global commercial airline industry has improved. This improvement is due to strong demand in both air freight and passenger traffic. The air transport industry has recently benefited from several favorable trends, including: (i) projected growth in air traffic and (ii) the beginning of major replacement and refurbishment cycles driven by the desire for more fuel efficient aircraft and fleet commonality. It is difficult to determine at this time what the long-term impact of these factors may be on the demand for products and services provided by the Repair Group. Lack of continued improvement in the global economy could result in further reduced demand for the products and services that the Repair Group provides.

Competition

In recent years, while the absolute number of competitors has decreased as a result of industry consolidation and vertical integration, competition in the turbine engine component repair business has nevertheless increased, principally due to the increased direct involvement of the turbine engine manufacturers in the turbine engine overhaul and component repair businesses. With the presence of the OEMs in the market, there has been a general reluctance on the part of the OEMs to

issue, to independent component repair companies, approvals for the repair of their newer model engines and related components. The Company believes that the Repair Group will, more likely than not, become more dependent in the future on (i) its ability to successfully procure and market FAA approved licenses and related repair processes and/or (ii) close collaboration with engine manufacturers.

Customers

The identity and ranking of the Repair Group's principal customers can vary from year to year. The Repair Group attempts to rely on its ability to adapt its services and operations to changing requirements of the market in general and its customers in particular, rather than relying on high volume production of a particular item or group of items for a particular customer or customers. During fiscal 2012, the Repair Group had four customers, consisting of various business units of Rolls-Royce Corporation, Safran Group, ATC Aerospace and United Technologies Corporation, which accounted for 20%, 17%, 14% and 11%, respectively, of the Repair Group's net sales. Although there is no assurance that this will continue, historically as one or more major customers have reduced their purchases, the business has generally been successful in replacing such reduced purchases, thereby avoiding a material adverse impact on the business. No material part of the Repair Group's business is seasonal.

Backlog of Orders

The Repair Group's backlog as of September 30, 2012 decreased to \$1.0 million, of which \$0.1 million is scheduled for delivery during fiscal 2013 and \$0.9 million is on hold, compared with \$1.2 million as of September 30, 2011, of which \$0.3 million was scheduled for delivery during fiscal 2012 and \$0.9 million was on hold. All orders are subject to modification or cancellation by the customer with limited charges. The Repair Group believes that the backlog may not necessarily be indicative of actual sales for any succeeding period.

3. Applied Surface Concepts Group

The Company's Applied Surface Concepts Group (ASC Group) provides surface enhancement technologies principally related to selective plating and anodizing. Principal product offerings include (i) the development, production and sale of metal plating solutions and equipment required for selective plating and (ii) providing selective plating contract services.

Operations

Selective plating of a component is done without the use of an immersion tank. A wide variety of pure metals and alloys, principally determined by the customer's design requirements, can be used for applications including corrosion protection, wear resistance, anti-galling, increased lubricity, increased hardness, increased electrical conductivity, and re-sizing. SIFCO Process® metal solutions include: cadmium, cobalt, copper, nickel, tin and zinc. In addition, precious metal solutions such as gold, iridium, palladium, platinum, rhodium, and silver are also provided to customers. The ASC Group has also developed a number of alloy-plating solutions such as (i) nickel-tungsten, cobalt chromium carbide and nickel-cobalt solutions that can be used as more environmentally friendly alternatives for hexavalent chromium plating solutions and (ii) low hydrogen embrittlement zinc-nickel and tin-zinc solutions that can be used as more environmentally friendly alternatives for cadmium plating solutions.

The ASC Group can either (i) supply selective plating chemicals and equipment to customers desiring to perform selective plating in-house or (ii) provide manual or semi-automated contract selective plating services at either the customer's site or at one of the ASC Group's facilities. The ASC Group operates four U.S. facilities in geographic areas strategically located in proximity to its major customers (Cleveland, Ohio / Hartford, Connecticut / Norfolk, Virginia / Houston, Texas) and three in Europe (Birmingham, England / Paris, France / Rattvik, Sweden). The scope of selective plating work includes part salvage and repair, part refurbishment, and new part enhancement. Selective plating solutions are produced in the Cleveland, Ohio and Birmingham, England facilities.

The ASC Group generally has multiple sources available for its raw materials, which consist primarily of industrial chemicals and metal salts and, therefore, does not have a high dependence upon a single source for the supply of key raw materials. Management believes that its sources of raw materials are adequate to support its business.

The ASC Group maintains recognized industry brand names including: SIFCO Process®, Copper Select®, Dalic®, USDL® and Selectron®, all of which are specified in military and industrial specifications. The ASC Group's manufacturing operations have ISO 9001:2008 and AS 9100 certifications. In addition, two of its facilities are NADCAP (National Aerospace and Defense Contractors Accreditation Program) certified. Two of the service centers are FAA approved repair shops. The ASC Group is also registered with the ARR (American Railroad Registry) and KRS (Korean Registry of Shipping).

Industry

Selective plating occupies a niche within the broader metal finishing industry. The ASC Group's selective plating process is used to provide functional, engineered finishes rather than decorative finishes, and it serves many markets including aerospace, medical, electric power generation, and oil and gas. In its planning and decision making processes, management of the ASC Group monitors and evaluates precious metal prices, global manufacturing activity, internal labor capacity, technological developments in surface enhancement, and the exploration and production activities relative to oil and gas products. The diversity of industries served helps to mitigate the impact of economic cycles on the ASC Group.

Competition

Although the Company believes that the ASC Group is the world's largest selective plating company, there are several companies globally that manufacture and sell selective plating finishing solutions and equipment and/or provide contract selective plating services. The ASC Group seeks to differentiate itself through its technical support and research and development capabilities. The ASC Group also competes with other surface enhancement technologies such as welding and metal spray.

Customers

During fiscal 2012, the ASC Group had no customers which accounted for 10% or more of the ASC Group's net sales. The ASC Group has a customer base of over 1,000 customers. Approximately 10 customers, who operate in a variety of industries, accounted for approximately 29% of the ASC Group's fiscal 2012 net sales. No material part of the ASC Group's business is seasonal.

Backlog of Orders

Due to the nature of its business (i.e. shorter lead times for its products and services), the ASC Group had no material backlog at September 30, 2012 and 2011.

4. General

For financial information concerning the Company's reportable segments, see Management's Discussion and Analysis of Financial Condition and Results of Operations included in Item 7 and Note 11 to consolidated financial statements included in Item 8.

C. Environmental Regulations

In common with other companies engaged in similar businesses, the Company is required to comply with various laws and regulations relating to the protection of the environment. The costs of such compliance have not had, and are not presently expected to have, a material effect on the capital expenditures, earnings or competitive position of the Company and its subsidiaries under existing regulations and interpretations.

D. Employees

The number of the Company's employees increased from approximately 360 at the beginning of fiscal 2012 to approximately 565 employees at the end of fiscal 2012. The Company is party to collective bargaining agreements with certain employees located at its Forge Group's Cleveland, Ohio (expires in May 2015) and Alliance, Ohio (expires in July 2013) facilities and at its Repair Group's Minneapolis, Minnesota facility (expires in July 2014).

E. Non-U.S. Operations

The Company's products and services are distributed and performed in both U.S. and non-U.S. markets. The Company commenced its operations in the United Kingdom and France as a result of an acquisition of a business in 1992. The Company commenced its operations in Sweden as a result of an acquisition of a business in 2006. Wholly-owned subsidiaries operate the Company's service and distribution facilities in the United Kingdom, France and Sweden.

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Financial information about the Company's U.S. and non-U.S. operations and subsidiaries is set forth in Note 11 to the consolidated financial statements included in Item 8.

As of September 30, 2012, essentially all of the Company's cash and cash equivalents are in the possession of its non-U.S. subsidiaries and relate to undistributed earnings of these non-U.S. subsidiaries. Distributions from the Company's non-U.S. subsidiaries to the Company may be subject to statutory restrictions, adverse tax consequences or other limitations.

Item 2. Properties

The Company's property, plant and equipment include the facilities described below and a substantial quantity of machinery and equipment, most of which consists of industry specific machinery and equipment using special dies, jigs, tools and fixtures and in many instances having automatic control features and special adaptations. In general, the Company's property, plant and equipment are in good operating condition, are well maintained and substantially all of its facilities are in regular use. The Company considers its investment in property, plant and equipment as of September 30, 2012 suitable and adequate given the current product offerings for the respective business segments' operations in the current business environment. The square footage numbers set forth in the following paragraphs are approximations:

The Repair Group operates a single, owned facility in Minneapolis, Minnesota with a total of 59,000 square feet and is involved in the repair and remanufacture of principally small aerospace turbine engine components.

The Forge Group operates in multiple facilities (i) an owned 240,000 square foot facility located in Cleveland, Ohio, which is also the site of the Company's corporate headquarters, (ii) a leased 450,000 square foot facility located in Alliance, Ohio, and (iii) leased facilities aggregating approximately 67,000 square feet located in Orange and Long Beach, California.

The ASC Group is headquartered in an owned 34,000 square foot facility in Cleveland, Ohio. The ASC Group leases space aggregating 52,000 square feet for sales offices and/or for its contract selective plating services in Norfolk, Virginia; Hartford, Connecticut; Houston, Texas; Paris, France; and Birmingham, England. The ASC Group also operates in an owned 3,000 square foot facility in Rattvik, Sweden.

The Company owns a building located in Cork, Ireland (59,000 square feet) that is subject to a long-term lease arrangement with the acquirer of the Repair Group's industrial turbine engine component repair business that was sold.

Item 3. Legal Proceedings

In the normal course of business, the Company may be involved in ordinary, routine legal actions. The Company cannot reasonably estimate future costs, if any, related to these matters and does not believe any such matters are material to its financial condition or results of operations. The Company maintains various liability insurance coverages to protect its assets from losses arising out of or involving activities associated with ongoing and normal business operations; however, it is possible that the Company's future operating results could be affected by future costs of litigation.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The Company's Common Shares are traded on the NYSE MKT exchange under the symbol "SIF". The following table sets forth, for the periods indicated, the high and low closing sales price for the Company's Common Shares.

	Years Ended September 30,			
	2012		2011	
	High	Low	High	Low
First Quarter	\$ 19.93	\$ 17.81	\$ 16.97	\$ 12.06
Second Quarter	22.43	18.54	17.68	15.91
Third Quarter	22.98	18.06	17.88	15.63
Fourth Quarter	23.75	18.20	19.96	16.22

Dividends and Shares Outstanding

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The Company declared a cash dividend of \$0.20 per Common Share in fiscal 2012. While the Company does not necessarily anticipate paying regular annual dividends, the Company will continue to evaluate the payment of such

dividends annually based on its relative profitability and available resources. The Company currently intends to retain a significant majority of its earnings for the operation and growth of its businesses. The Company's ability to declare or pay cash dividends is limited by its credit agreement covenants. At October 31, 2012, there were approximately 550 shareholders of record of the Company's Common Shares, as reported by Computershare, Inc., the Company's Transfer Agent and Registrar, which maintains its U.S. corporate offices at 250 Royall Street, Canton, MA 02021.

Reference Part III, Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters for information related to the Company's equity compensation plans.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

This Form 10-K, including Management's Discussion and Analysis of Financial Condition and Results of Operations, may contain various forward-looking statements and includes assumptions concerning the Company's operations, future results and prospects. These forward-looking statements are based on current expectations and are subject to risk and uncertainties. In connection with the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, the Company provides this cautionary statement identifying important economic, political and technological factors, among others, the absence or effect of which could cause the actual results or events to differ materially from those set forth in or implied by the forward-looking statements and related assumptions. Such factors include the following: (1) the impact on business conditions in general, and on the demand for product in the aerospace and power generation industries in particular, of the global economic outlook, including the continuation of military spending at or near current levels and the availability of capital and liquidity from banks and other providers of credit; (2) future business environment, including capital and consumer spending; (3) competitive factors, including the ability to replace business which may be lost; (4) successful development of turbine component repair processes and/or procurement of new repair process licenses from turbine engine manufacturers and/or the Federal Aviation Administration; (5) metals and commodities price increases and the Company's ability to recover such price increases; (6) successful development and market introduction of new products and services; (7) continued reliance on consumer acceptance of regional and business aircraft powered by more fuel efficient turboprop engines; (8) continued reliance on military spending, in general, and/or several major customers, in particular, for revenues; (9) the impact on future contributions to the Company's defined benefit pension plans due to changes in actuarial assumptions, government regulations and the market value of plan assets; (10) stable governments, business conditions, laws, regulations and taxes in economies where business is conducted; and (11) the ability to successfully integrate businesses that may be acquired into the Company's operations.

The Company and its subsidiaries engage in the production and sale of a variety of metalworking processes, services and products produced primarily to the specific design requirements of its customers. The processes and services include both conventional and precision forging, heat-treating, coating, welding, precision component machining and selective plating. The products include conventional and precision forged components, machined forged components, other machined metal components, remanufactured component parts for turbine engines, and selective plating solutions and equipment. The Company's operations are conducted in three business segments: (1) Forged Components Group, (2) Turbine Component Services and Repair Group, and (3) Applied Surface Concepts Group.

The Company endeavors to plan and evaluate its businesses' operations while taking into consideration certain factors including the following (i) the projected build rate for commercial, business and military aircraft as well as the engines that power such aircraft, (ii) the projected build rate for industrial gas turbine engines, (iii) the projected maintenance, repair and overhaul schedules for commercial, business and military aircraft as well as the engines that power such aircraft, and (iv) anticipated exploration and production activities relative to oil and gas products, etc.

The primary factor that impacts the operating income of all three of the Company's business segments, in a similar manner, is net sales and related production volumes. This is due to the fact that each of the Company's segments operates within a cost structure that includes a significant fixed component. Therefore, higher net sales volumes are expected to result in greater operating income because such higher volumes allow the business segments' operations to better leverage the fixed component of their respective cost structures. Conversely, the opposite effect is expected to occur at lower net sales and related production volumes.

A. Results of Operations

Non-GAAP Financial Measures

Presented below is certain financial information based on our EBITDA and Adjusted EBITDA. References to EBITDA mean earnings before interest, taxes, depreciation and amortization, and references to Adjusted EBITDA mean EBITDA plus, as applicable for each relevant period, certain adjustments as set forth in the reconciliations of net income to EBITDA and Adjusted EBITDA.

Neither EBITDA nor Adjusted EBITDA is a measurement of financial performance under accounting principles generally accepted in the United States of America (GAAP). The Company presents EBITDA and Adjusted EBITDA because (i) it believes they are useful indicators for evaluating operating performance and liquidity, including the Company's ability to incur and service debt and (ii) it uses EBITDA to evaluate prospective acquisitions. Although the Company uses EBITDA and Adjusted EBITDA for the reasons noted, the use of these non-GAAP financial measures as analytical tools has limitations and, therefore, reviewers of the Company's financial information should not consider them in isolation, or as a substitute for analysis of its results of operations as reported in accordance with GAAP. Some of these limitations are:

Neither EBITDA nor Adjusted EBITDA reflects the interest expense, or the cash requirements necessary to service interest payments, on indebtedness;

Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized will often have to be replaced in the future, and neither EBITDA nor Adjusted EBITDA reflects any cash requirements for such replacements;

The omission of the substantial amortization expense associated with the Company's intangible assets further limits the usefulness of EBITDA and Adjusted EBITDA;

Neither EBITDA nor Adjusted EBITDA includes the payment of taxes, which is a necessary element of operations; and

Adjusted EBITDA excludes the cash expense the Company has incurred to acquire businesses.

Because of these limitations, EBITDA and Adjusted EBITDA should not be considered as measures of discretionary cash available to the Company to invest in the growth of its businesses. Management compensates for these limitations by not viewing EBITDA or Adjusted EBITDA in isolation and specifically by using other GAAP measures, such as net income, net sales and operating profit, to measure operating performance. Neither EBITDA nor Adjusted EBITDA is a measurement of financial performance under GAAP, and neither should be considered as an alternative to net income or cash flow from operations determined in accordance with GAAP. The Company's calculation of EBITDA and Adjusted EBITDA may not be comparable to the calculation of similarly titled measures reported by other companies.

The following table sets forth a reconciliation of net income to EBITDA and Adjusted EBITDA:

(Dollars in thousands)	September 30,	
	2012	2011
Net income	\$ 6,548	\$ 7,449
Adjustments:		
Depreciation and amortization expense	6,671	4,386
Interest expense, net	438	82
Income tax provision	2,852	3,789
EBITDA	16,509	15,706
Adjustments:		
Inventory purchase accounting adjustments (1)	437	202
Acquisition transaction-related expenses (2)	407	301
Equity compensation expense (3)	892	547
LIFO provision (4)	1,563	479
Adjusted EBITDA	\$ 19,808	\$ 17,235

(1)

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Represents accounting adjustments to inventory associated with acquisitions of businesses that were charged to cost of sales when the inventory was sold.

- (2) Represents transaction-related costs comprising legal, financial and tax due diligence expenses; and valuation services costs that are required to be expensed as incurred.
- (3) Represents the equity based compensation expense recognized by the Company under its 2007 Long-Term Incentive Plan.
- (4) Represents the increase in the reserve for inventories for which cost is determined using the last-in, first-out (LIFO) method.

Fiscal Year 2012 Compared with Fiscal Year 2011

Net sales in fiscal 2012 increased 16.5% to \$125.1 million, compared with \$107.4 million in fiscal 2011. Net income in fiscal 2012 was \$6.6 million, compared with \$7.4 million in fiscal 2011. EBITDA in fiscal 2012 was \$16.5 million, or 13.2% of net sales, compared with \$15.7 million, or 14.6% of net sales, in the comparable period in fiscal 2011. Adjusted EBITDA in fiscal 2012 was \$19.8 million, or 15.8% of net sales, compared with \$17.2 million, or 16.1% of net sales, in the comparable period in fiscal 2011. See *Non-GAAP Financial Measures* above for certain information regarding EBITDA and Adjusted EBITDA, including reconciliations of EBITDA and Adjusted EBITDA to net income. As discussed more fully in Note 12 to the consolidated financial statements, the Company completed the purchase of the forging businesses and substantially all related operating assets of QAF and TWF on October 28, 2011 and December 10, 2010, respectively.

Forged Components Group (Forge Group)

The Forge Group consists of the production, heat-treatment, surface-treatment, non-destructive testing, and machining of both conventional and precision forged components in various steel, titanium and aluminum alloys utilizing a variety of processes for application principally in the aerospace and power generation industries. The Forge Group's results for fiscal 2012 include the results of QAF from the date of its acquisition. The Forge Group's results for fiscal 2011 include the results of TWF from the date of acquisition. Net sales in fiscal 2012 increased 22.3% to \$102.9 million, compared with \$84.1 million in fiscal 2011. The Forge Group produces forged components for (i) turbine engines that power commercial business and regional aircraft as well as military aircraft and armored military vehicles; (ii) airframe applications for a variety of aircraft; (iii) industrial gas turbine engines for power generation units; and (iv) other commercial applications. Net sales comparative information for fiscal 2012 and 2011, respectively, is as follows:

(Dollars in millions)	Year Ended		Increase (Decrease)
	2012	September 30, 2011	
Net Sales			
Aerospace components for:			
Fixed wing aircraft	\$ 52.9	\$ 36.3	\$ 16.6
Rotorcraft	28.2	26.4	1.8
Components for power generation units	17.1	16.2	0.9
Commercial product sales and other revenue	4.7	5.2	(0.5)
Total	\$ 102.9	\$ 84.1	\$ 18.8

The increase in net sales of forged components for fixed wing aircraft and rotorcraft during fiscal 2012, compared with fiscal 2011, is principally due to the impact of the acquisition of QAF during the first quarter of fiscal 2012. The increase in net sales of components for power generation units is due to the full year impact in fiscal 2012 of the acquisition of TWF during the first quarter of fiscal 2011.

The Forge Group's aerospace components have both military and commercial applications. Net sales of such components that solely have military applications were \$35.5 million in fiscal 2012, compared with \$32.5 million in fiscal 2011. This increase is primarily attributable to the acquisition of QAF. Demand for additional military helicopters and related replacement components are the primary drivers of such military sales demand.

The Forge Group's cost of goods sold increased \$16.3 million to \$81.1 million, or 78.8% of net sales, during fiscal 2012, compared with \$64.8 million, or 77.0% of net sales in fiscal 2011. Cost of goods sold as a percentage of net sales reflected an increase in fiscal 2012, compared to fiscal 2011, due to the net impact of the changes in the following components of manufacturing related expenditures:

The material component of manufacturing costs was approximately 36.3% of net sales during fiscal 2012, compared with 39.1% of net sales in fiscal 2011, due primarily to the mix of product a higher concentration of products, with lower material content, were sold during the fiscal 2012, compared with fiscal 2011.

All other manufacturing costs were approximately 42.5% of net sales during fiscal 2012, compared with 37.9% of net sales in the comparable period in fiscal 2011. Labor costs, as a percentage of net sales, were higher principally due to the mix of product a higher concentration of products with higher labor content were sold during fiscal 2012, compared with the comparable period in fiscal 2011. The Forge Group also experienced a reduction in its labor efficiency during fiscal 2012, compared with fiscal 2011. The

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following changes in the components of the Forge Group's other manufacturing overhead expenditures during fiscal 2012 compared with fiscal 2011, a portion of which was due to the acquisitions of QAF and TWF, also impacted cost of goods sold:

(Dollars in millions)	Year Ended September 30,		Increase (Decrease)
	2012	2011	
Manufacturing expenditures			
Overhead:			
Utilities	\$ 4.7	\$ 4.4	\$ 0.3
Repairs, maintenance and supplies	4.6	3.4	1.2
Depreciation	2.9	1.5	1.4
Rent	0.5	0.0	0.5
Tooling	3.3	2.6	0.7

Manufacturing costs in fiscal 2012, compared with the same period in fiscal 2011, increased due to (i) an increase in manufacturing expenditures required to support the \$18.8 million of additional product sales volume for the Forge Group and (ii) an increase in depreciation and rent expense, all of which were primarily attributable to the acquisitions of TWF and QAF. These higher costs were partially offset by a decrease in the price paid for natural gas in fiscal 2012, compared with fiscal 2011.

The Forge Group's selling, general and administrative expenses increased \$2.4 million to \$8.9 million, or 8.6% of net sales, in fiscal 2012, compared with \$6.5 million, or 7.7% of net sales, in fiscal 2011. The increase in selling, general and administrative expenses is principally due to (i) a \$1.0 million increase in amortization of intangible assets related to the acquisitions of TWF and QAF and (ii) a \$1.2 million increase in relative spending levels due to the impact of the acquisitions of TWF and QAF. The Forge Group's selling, general and administrative expenses in fiscal 2012, before the impact of the amortization of intangible assets, was \$6.0 million, or 5.8% of net sales, compared with \$4.6 million, or 5.4% of net sales, in fiscal 2011.

The Forge Group's operating income decreased \$0.1 million to \$12.9 million in fiscal 2012, compared with \$13.0 million in fiscal 2011. The following is a comparison of operating income on both a LIFO and FIFO basis:

(Dollars in millions)	Year Ended September 30,		Increase (Decrease)
	2012	2011	
Operating Income			
Operating income	\$ 12.9	\$ 13.0	\$ (0.1)
LIFO expense	1.6	0.5	1.1
Operating income without LIFO expense	\$ 14.5	\$ 13.5	\$ 1.0

The Forge Group's operating income in fiscal 2012 was favorably impacted by the increase in gross profit generated from \$20.5 million of additional product sales volumes for TWF and QAF plus the net impact of the other cost of goods sold and selling, general and administrative expense factors noted above.

Turbine Component Services and Repair Group (Repair Group)

During fiscal 2012, net sales, which consist principally of component repair services (including precision component machining and industrial coatings) for small aerospace turbine engines, decreased 20.6% to \$7.2 million, compared with \$9.0 million in fiscal 2011. The decrease in net sales during fiscal 2012, compared with fiscal 2011, is attributable to a decrease in product sales volumes.

The Repair Group's cost of goods sold decreased \$0.5 million to \$7.2 million or 100.4% of net sales in fiscal 2012, compared with \$7.7 million or 85.6% of net sales fiscal 2011. Cost of goods sold as a percentage of net sales reflected an increase in fiscal 2012, compared to fiscal 2011, due principally to the Repair Group maintaining a minimum/base cost structure that has a large fixed component that is determined necessary to sustain an operation with relevant capabilities.

During fiscal 2012, the Repair Group's selling, general and administrative expenses were \$1.4 million, or 19.3% of net sales, compared with \$1.6 million, or 17.5% of net sales, in fiscal 2011. The Repair Group's decrease in selling, general and administrative expenses is principally attributable to \$0.2 million of expense related to the impairment of a long-lived asset recognized in fiscal 2011.

The Repair Group's operating loss in fiscal 2012 was \$1.4 million, compared to \$0.3 million in fiscal 2011. Operating results in fiscal 2012 were negatively impacted by the significantly lower product sales volumes in relation to the large fixed component of the Repair Group's operating cost structure. The Repair Group will need to increase its product sales volumes to increase its operating income.

Applied Surface Concepts Group (ASC Group)

Net sales in fiscal 2012 increased 6.1% to \$15.0 million, compared with \$14.2 million in fiscal 2011. For purposes of the following discussion, (i) product net sales consist of selective plating equipment and solutions and (ii) contract service net sales consist of customized selective plating services. Net sales comparative information for fiscal 2012 and 2011, respectively, is as follows:

(Dollars in millions)	Year Ended		Increase (Decrease)
	September 30, 2012	2011	
Net Sales			
Product	\$ 7.3	\$ 6.6	\$ 0.7
Contract service	7.5	7.4	0.1
Other	0.2	0.2	0.0
Total	\$ 15.0	\$ 14.2	\$ 0.8

The increase in product net sales in fiscal 2012, compared with fiscal 2011, is attributed to an increase in net sales volumes of selective plating equipment and solutions, as well as a general price increase implemented at the beginning of the second quarter of fiscal 2012. A portion of the ASC Group's business is conducted in Europe and is denominated in local European currencies. Fluctuations in currency exchange rates during fiscal 2012, compared with fiscal 2011, had a nominal impact on net sales.

The ASC Group's cost of goods sold increased \$0.3 million to \$8.7 million, or 58.1% of net sales, during fiscal 2012, compared with \$8.4 million, or 59.0% of net sales, in fiscal 2011. Cost of goods sold as a percentage of net sales reflected a decrease in fiscal 2012, compared to fiscal 2011, due principally to the following:

The material component of cost of goods sold was approximately 19.5% of net sales during fiscal 2012, compared with 18.5% of net sales in fiscal 2011, due principally to certain higher commodity prices and the mix of product a higher concentration of products and contract services, with higher material content, were sold during fiscal 2012, compared with fiscal 2011.

All other cost of goods sold were approximately 38.6% of net sales during fiscal 2012, compared with 40.5% of net sales in fiscal 2011. The primary reason for the reduction of all other cost of goods sold as a percentage of net sales is the impact of higher sales volumes during fiscal 2012, compared with fiscal 2011, which allowed the ASC Group to favorably leverage the fixed component of its operating cost structure.

The ASC Group's selling, general and administrative expenses were \$5.2 million, or 34.8% of net sales, in fiscal 2012, compared with \$4.8 million, or 33.7% of net sales in fiscal 2011. The \$0.4 million increase is due primarily to an increase in sales promotion efforts and the filling of an open sales position.

The ASC Group's operating income in fiscal 2012 was \$1.1 million, compared with \$1.0 million in fiscal 2011.

Corporate Unallocated Expenses

Corporate unallocated expenses, consisting of corporate salaries and benefits, legal and professional and other expenses that are not related to and, therefore, not allocated to the business segments, were \$3.2 in fiscal 2012, compared with \$2.9 million in fiscal 2011. The \$0.3 million increase is due to a \$0.2 million increase in legal and professional expenses principally to support the acquisition of QAF, a \$0.3 million increase in the Company's long-term equity incentive plan expense, partially offset by a \$0.3 million decrease in the Company's annual cash incentive plan expense.

Other/General

Interest expense was \$0.5 million in fiscal 2012, compared to \$0.1 million in fiscal 2011. As described more fully in note 6 to the consolidated financial statements included in Item 8, in connection with the October 2011 acquisition of the QAF business, the Company borrowed \$12.4 million from its revolving credit agreement and \$10.0 million on a term note, and issued a \$2.4 million promissory note to the seller of the QAF business. The following table sets forth the weighted average interest rates and weighted average outstanding balances under the Company's debt agreement in fiscal 2012 and 2011:

	Weighted Average		Weighted Average	
	Interest Rate		Outstanding Balance	
	Year Ended September 30, 2012	2011	Year Ended September 30, 2012	2011
Revolving credit agreement	1.3%	1.3%	\$ 11.9 million	\$ 4.0 million
Term note	2.9%	N/A	\$ 9.0 million	N/A
Promissory note	2.0%	N/A	\$ 2.3 million	N/A

Other income, net consists principally of \$0.4 million of rental income earned from the lease of the Cork, Ireland facility.

The Company believes that inflation did not materially affect its results of operations in either fiscal 2012 or 2011, and does not expect inflation to be a significant factor in fiscal 2013.

Income Tax Provision

The Company's effective tax rate in fiscal 2012 was 30%, compared to 34% in fiscal 2011, and differs from the U.S. federal statutory rate due primarily to (i) the impact of U.S. state and local taxes, (ii) domestic production activities deduction, (iii) application of tax credits, and (iv) the recognition of federal income taxes on undistributed earnings of non-U.S. subsidiaries.

B. Liquidity and Capital Resources

Cash and cash equivalents increased to \$7.2 million at September 30, 2012, compared with \$6.4 million at September 30, 2011. At September 30, 2012, essentially all of the \$7.2 million of the Company's cash and cash equivalents are in the possession of its non-U.S. subsidiaries for purposes of (i) funding the respective subsidiary businesses' current operations outside the U.S. and (ii) to fund potential future investment outside the U.S. In the future, if the Company determines that there is no longer a need to maintain such cash within its non-U.S. operations, it may elect to distribute such cash to its U.S. operations. Distributions from the Company's non-U.S. subsidiaries to the Company may be subject to adverse tax consequences.

The Company's operating activities provided \$9.8 million of cash in fiscal 2012 compared with \$10.2 million in fiscal 2011. The \$9.8 million of cash provided by operating activities in fiscal 2012 was primarily due to (i) net income of \$6.6 million, (ii) \$8.7 million from the net impact of such non-cash items as depreciation and amortization expense, deferred taxes, equity compensation expense and LIFO expense and (iii) a \$1.1 million decrease in accounts receivable. These items were partially offset by a \$6.1 million increase in inventories. These changes in the components of working capital do not reflect the impact of the opening balance sheet related to the acquisition of QAF and were due primarily to factors resulting from normal business conditions of the Company, including (i) building inventory in response to customer demand, (ii) the relative timing of collections from customers and (iii) the relative timing of payments to suppliers and tax authorities.

Capital expenditures were \$3.5 million in fiscal 2012 compared with \$3.3 million in fiscal 2011. Capital expenditures during fiscal 2012 consisted of \$2.9 million by the Forge Group, \$0.2 million by the ASC Group and \$0.4 million by the Repair Group. In addition to the \$3.5 million expended during fiscal 2012, \$0.2 million has been committed as of September 30, 2012. The Company anticipates that total fiscal 2013 capital expenditures will be within the range of \$4.0 to \$5.0 million and will relate principally to the further enhancement of production and product offering capabilities across all three of the Company's business groups.

In the fourth quarter of fiscal 2012, the Company declared a special cash dividend of \$0.20 per common share, which will result in a cash expenditure of \$1.1 million during first quarter of fiscal 2013.

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As described more fully in note 12 to the consolidated financial statements included in Item 8, the Company acquired a forging business in October 2011 for approximately \$24.8 million at closing. The acquisition was financed by borrowing

approximately \$22.4 million from its bank, which borrowing consisted of a new \$10.0 million term loan and drawing approximately \$12.4 million from its revolving credit facility. The balance of the acquisition was financed by the Company issuing a \$2.4 million promissory note to the seller, which note is payable by the Company in November 2013.

In October 2011, the Company entered into an amendment to its existing credit agreement with its bank increasing the maximum borrowing amount from \$30.0 million to \$40.0 million, of which \$10.0 million is a five (5) year term loan and \$30.0 million is a five (5) year revolving loan, secured by substantially all the assets of the Company and its U.S. subsidiaries and a pledge of 65% of the stock of its non-U.S. subsidiaries. The term loan is repayable in quarterly installments of \$0.5 million starting December 1, 2011.

The term loan has a variable interest rate based on Libor, which becomes an effective fixed rate of 2.9% after giving effect to an interest rate swap agreement. Borrowing under the revolving loan bears interest at a rate equal to Libor plus 0.75% to 1.75%, which percentage fluctuates based on the Company's leverage ratio of outstanding indebtedness to EBITDA. The bank loans are subject to certain customary financial covenants including, without limitation, covenants that require the Company to not exceed a maximum leverage ratio and to maintain a minimum fixed charge coverage ratio. There is also a commitment fee ranging from 0.10% to 0.25% to be incurred on the unused balance. The promissory note issued to the seller is non-interest bearing and is due in November of 2013. The Company was in compliance with all applicable loan covenants as of September 30, 2012.

Future cash flows from the Company's U.S. operations will be used to pay down amounts outstanding under the Company's credit agreement. The Company believes it has adequate cash available in the possession of its non-U.S. subsidiaries to finance its non-U.S. operations. The Company believes it has adequate cash/liquidity available to finance its U.S. operations from the combination of (i) the Company's expected cash flows from U.S. operations and (ii) funds available under its existing credit agreement.

C. Off-Balance Sheet Arrangements

Other than an interest rate swap agreement that the Company entered into with its bank, as described more fully in note 6 to the consolidated financial statements included in Item 8, the Company does not have any obligations that meet the definition of an off-balance sheet arrangement that have had, or are reasonably likely to have, a material effect on the Company's financial condition or results of operations.

D. Critical Accounting Policies and Estimates

Allowances for Doubtful Accounts

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of certain customers to make required payments. The Company evaluates the adequacy of its allowances for doubtful accounts each quarter based on the customers' credit-worthiness, current economic trends or market conditions, past collection history, aging of outstanding accounts receivable and specific identified risks. As these factors change, the Company's allowances for doubtful accounts may change in subsequent periods. Historically, losses have been within management's expectations and have not been significant.

Inventories

The Company maintains allowances for obsolete and excess inventory. The Company evaluates its allowances for obsolete and excess inventory each quarter. Each business segment maintains formal policies, which require at a minimum that reserves be established based on an analysis of the age of the inventory. In addition, if the Company learns of specific obsolescence, other than that identified by the aging criteria, an additional reserve will be recognized as well. Specific obsolescence may arise due to a technological or market change, or based on cancellation of an order. Management's judgment is necessary in determining the realizable value of these products to arrive at the proper allowance for obsolete and excess inventory.

Impairment of Long-Lived Assets

The Company reviews the carrying value of its long-lived assets, including property, plant and equipment, at least annually or when events and circumstances warrant such a review. This review involves judgment and is performed using estimates of future undiscounted cash flows, which include proceeds from disposal of assets and which the Company considers a critical accounting estimate. If the carrying value of a long-lived asset is greater than the estimated undiscounted future cash flows, then the long-lived asset is considered impaired and an impairment charge is recorded for the amount by which the carrying value of the long-lived asset exceeds its fair value.

In projecting future undiscounted cash flows, the Company relies on internal budgets and forecasts, and projected proceeds upon disposal of long-lived assets. The Company's budgets and forecasts are based on historical results and anticipated future market conditions, such as the general business climate and the effectiveness of competition. The Company believes that its estimates of future undiscounted cash flows and fair value are reasonable; however, changes in estimates of such undiscounted cash flows and fair value could change the Company's estimates of fair value, which could result in future impairment charges.

Impairment of Goodwill

Goodwill is the excess of the purchase price paid over the fair value of the net assets of an acquired business. The determination of the fair value of assets and liabilities acquired typically involves obtaining independent appraisals of certain tangible and intangible assets and may require management to make certain assumptions and estimates regarding future events. Goodwill is not amortized, but is subject to an impairment testing annually or more frequently if events or changes in circumstances indicate that goodwill may be impaired.

For the purposes of impairment testing, goodwill acquired in a business combination is allocated to the reporting entity expected to benefit from the business combination. Goodwill impairment testing involves the comparison of the fair value of a reporting unit, which is determined by its discounted cash flows, with its carrying value. The Company allocates the fair value of the reporting unit to all of its assets, other than goodwill, and liabilities. Any remaining unallocated fair value is then allocated to goodwill as its implied fair value. The amount of impairment loss is equal to the excess of the carrying value of goodwill over the implied fair value of goodwill.

Purchase Price Allocations

The costs of business acquisitions are allocated to the acquired assets and liabilities based on their respective fair value at the time of the acquisition. The determination of fair values typically involves obtaining independent appraisals of certain tangible and intangible assets and may require management to make certain assumptions and estimates regarding future events. In determining fair value, management may develop a number of possible future cash flow scenarios to which probabilities are judgmentally assigned and evaluated. This allocation process impacts the Company's reported assets and liabilities and future net income.

Defined Benefit Pension Plan Expense

The Company maintains three defined benefit pension plans in accordance with the requirements of the Employee Retirement Income Security Act of 1974 (ERISA). The amounts recognized in the consolidated financial statements for pension benefits under these three defined benefit pension plans are determined on an actuarial basis utilizing various assumptions. The discussion that follows provides information on the significant assumptions/elements associated with these defined benefit pension plans.

One significant assumption in determining net pension expense is the expected return on plan assets. The Company determines the expected return on plan assets principally based on (i) the expected return for the various asset classes in the respective plans' investment portfolios and (ii) the targeted allocation of the respective plans' assets. The expected return on plan assets is developed using historical asset return performance as well as current and anticipated market conditions such as inflation, interest rates and market performance. Should the actual rate of return differ materially from the assumed/expected rate, the Company could experience a material adverse effect on the funded status of its plans and, accordingly, on its related future net pension expense.

Another significant assumption in determining the net pension expense is the discount rate. The discount rate for each plan is determined, as of the fiscal year end measurement date, using prevailing market spot-rates (from an appropriate yield curve) with maturities corresponding to the expected timing/date of the future defined benefit payment amounts for each of the respective plans. Such corresponding spot-rates are used to discount future years' projected defined benefit payment amounts back to the fiscal year end measurement date as a present value. A composite discount rate is then developed for each plan by determining the single rate of discount that will produce the same present value as that obtained by applying the annual spot-rates. The discount rate may be further revised if the market environment indicates that the above methodology generates a discount rate that does not accurately reflect the prevailing interest rates as of the fiscal year end measurement date.

Deferred Tax Valuation Allowance

The Company accounts for deferred taxes in accordance with the provisions of the Accounting Standards Codification (ASC) guidance related to accounting for income taxes, whereby the Company recognizes an income tax benefit related to its consolidated net losses and other temporary differences between financial reporting basis and tax reporting basis.

E. Impact of Newly Issued Accounting Standards

In July 2012, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update (ASU) 2012-2, *Intangibles - Goodwill and Other*, which allows an entity to first assess qualitative factors to determine whether it is more likely than not that an indefinite-lived asset is impaired for determining whether it is necessary to perform the quantitative impairment test. The ASU is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The adoption of this ASU did not have an impact on the Company's consolidated financial statements.

In December 2011, the FASB issued ASU 2011-12, *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU 2011-05*, and as a result entities are required to continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before ASU 2011-05. This update is effective for public companies with fiscal years beginning after December 15, 2011. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements and disclosures.

Item 8. Financial Statements and Supplementary Data

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders of SIFCO Industries, Inc. and Subsidiaries:

We have audited the accompanying consolidated balance sheets of SIFCO Industries, Inc. (an Ohio Corporation) and Subsidiaries as of September 30, 2012 and 2011, and the related consolidated statements of operations, shareholders' equity and cash flows for each of the two years in the period ended September 30, 2012. Our audits of the basic financial statements included the financial statement schedule appearing under Schedule II. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule 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. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes 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, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of SIFCO Industries, Inc. and Subsidiaries as of September 30, 2012 and 2011, and the results of their operations and their cash flows for each of the two years in the period ended September 30, 2012 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 basic financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

/s/ GRANT THORNTON LLP

Cleveland, Ohio

November 30, 2012

SIFCO Industries, Inc. and Subsidiaries

Consolidated Statements of Operations

(Amounts in thousands, except per share data)

	Years Ended September 30,	
	2012	2011
Net sales	\$ 125,106	\$ 107,357
Operating expenses:		
Cost of goods sold	97,025	80,916
Selling, general and administrative expenses	15,846	13,582
Amortization of intangible assets	2,879	1,917
Loss on disposal or impairment of operating assets	10	87
Total operating expenses	115,760	96,502
Operating income	9,346	10,855
Interest income	(33)	(46)
Interest expense	471	128
Foreign currency exchange loss (gain)	(25)	5
Other income, net	(467)	(470)
Income before income tax provision	9,400	11,238
Income tax provision	2,852	3,789
Net income	\$ 6,548	\$ 7,449
Net income per share:		
Basic	\$ 1.23	\$ 1.41
Diluted	\$ 1.22	\$ 1.40
Weighted-average number of common shares:		
Basic	5,317	5,271
Diluted	5,380	5,324

See notes to consolidated financial statements.

SIFCO Industries, Inc. and Subsidiaries

Consolidated Balance Sheets

(Amounts in thousands, except per share data)

	September 30,	
	2012	2011
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 7,176	\$ 6,431
Receivables, net	23,354	20,739
Inventories	18,692	10,239
Refundable income taxes	0	281
Deferred income taxes	1,461	1,500
Prepaid expenses and other current assets	1,223	468
Total current assets	51,906	39,658
Property, plant and equipment:		
Land	579	579
Buildings	15,039	14,097
Machinery and equipment	59,769	52,894
Total property, plant and equipment	75,387	67,570
Accumulated depreciation	43,128	40,012
Property, plant and equipment, net	32,259	27,558
Intangible assets, net	14,627	8,506
Goodwill	7,015	3,493
Other assets	738	796
Total assets	\$ 106,545	\$ 80,011
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current maturities of long-term debt	\$ 2,002	\$ 30
Accounts payable	9,727	9,778
Accrued liabilities	4,953	4,626
Total current liabilities	16,682	14,434
Long-term debt, net of current maturities	19,683	1,186
Deferred income taxes	1,542	2,233
Other long-term liabilities	8,496	8,749
Shareholders' equity:		
Serial preferred shares, no par value, authorized 1,000 shares	0	0
Common shares, par value \$1 per share, authorized 10,000 shares; issued 5,366 shares in 2012 and 5,335 shares in 2011; outstanding 5,366 shares in 2012 and 5,299 shares in 2011	5,366	5,335
Additional paid-in capital	7,523	7,032
Retained earnings	59,597	54,122
Accumulated other comprehensive loss	(12,344)	(12,702)
Common shares held in treasury at cost, no shares in 2012 and 36 shares in 2011	0	(378)
Total shareholders' equity	60,142	53,409
Total liabilities and shareholders' equity	\$ 106,545	\$ 80,011

See notes to consolidated financial statements.

SIFCO Industries, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(Amounts in thousands)

	Years Ended September 30,	
	2012	2011
Cash flows from operating activities:		
Net income	\$ 6,548	\$ 7,449
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation expense	3,792	2,450
Amortization expense	2,879	1,936
Loss (gain) on disposal of property, plant and equipment	10	(132)
LIFO provision	1,563	479
Deferred income taxes	(427)	(108)
Share transactions under employee stock plan	900	373
Asset impairment charges	0	219
Changes in operating assets and liabilities:		
Receivables	1,065	(2,288)
Inventories	(6,055)	(1,621)
Refundable income taxes	281	411
Prepaid expenses and other current assets	(601)	276
Other assets	58	139
Accounts payable	(403)	215
Accrued liabilities	229	(98)
Other long-term liabilities	(72)	520
Net cash provided by operating activities	9,767	10,220
Cash flows from investing activities:		
Acquisition of businesses	(24,886)	(22,566)
Maturity of short-term investments	0	3,000
Capital expenditures	(3,521)	(3,293)
Proceeds from disposal of property, plant and equipment	10	146
Net cash used for investing activities	(28,397)	(22,713)
Cash flows from financing activities:		
Proceeds from term note	10,000	0
Repayments of term note	(2,000)	0
Proceeds from revolving credit agreement	59,671	33,844
Repayments of revolving credit agreement	(49,517)	(32,660)
Proceeds from other debt	2,302	0
Dividends paid	(1,060)	(789)
Repayments of capital lease obligations and other long-term debt	(29)	(112)
Net cash provided by financing activities	19,367	283
Increase (decrease) in cash and cash equivalents	737	(12,210)
Cash and cash equivalents at beginning of year	6,431	18,671
Effect of exchange rate changes on cash and cash equivalents	8	(30)
Cash and cash equivalents at end of year	\$ 7,176	\$ 6,431
Supplemental disclosure of cash flow information:		
Cash paid for interest	\$ (393)	\$ (125)

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Cash paid for income taxes, net	\$ (3,037)	\$ (2,721)
Non-cash financing transactions:		
Dividends declared but not paid	\$ (1,073)	\$ (1,060)
See notes to consolidated financial statements.		

SIFCO Industries, Inc. and Subsidiaries

Consolidated Statements of Shareholders' Equity

(Amounts in thousands)

	Common Shares	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Common Shares Held in Treasury	Total Shareholders Equity
Balance September 30, 2010	\$ 5,325	\$ 6,983	\$ 47,733	\$ (11,310)	\$ (692)	\$ 48,039
Comprehensive income:						
Net income	0	0	7,449	0	0	7,449
Foreign currency translation adjustment	0	0	0	(45)	0	(45)
Retirement liability adjustment, net of tax	0	0	0	(1,347)	0	(1,347)
Total comprehensive income						6,057
Dividend declared	0	0	(1,060)	0	0	(1,060)
Performance share expense	0	373	0	0	0	373
Share transactions under employee stock plans	10	(324)	0	0	314	0
Balance September 30, 2011	\$ 5,335	\$ 7,032	\$ 54,122	\$ (12,702)	\$ (378)	\$ 53,409
Comprehensive income:						
Net income	0	0	6,548	0	0	6,548
Foreign currency translation adjustment	0	0	0	204	0	204
Retirement liability adjustment, net of tax	0	0	0	212	0	212
Interest rate Swap Agreement adjustment, net of tax	0	0	0	(58)	0	(58)
Total comprehensive income						6,906
Dividend declared	0	0	(1,073)	0	0	(1,073)
Performance and restricted share expense	0	936	0	0	0	936
Share transactions under employee stock plans	31	(445)	0	0	378	(36)
Balance September 30, 2012	\$ 5,366	\$ 7,523	\$ 59,597	\$ (12,344)	\$ 0	\$ 60,142

See notes to consolidated financial statements.

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements

Years ended September 30, 2012 and 2011

(Amounts in thousands, except per share data)

1. Summary of Significant Accounting Policies

1. Summary of Significant Accounting Policies

A. DESCRIPTION OF BUSINESS

SIFCO Industries, Inc. and Subsidiaries (the Company) are engaged in the production and sale of a variety of metalworking processes, services and products produced primarily to the specific design requirements of its customers. The processes and services include forging, heat-treating, coating, welding, machining, and selective plating. The products include forged components (both conventional and precision), machined forged parts and other machined metal parts, remanufactured components for turbine engines, and selective plating solutions and equipment. The Company's operations are conducted in three business segments: (i) Forged Components Group, (ii) Turbine Component Services and Repair Group and (iii) Applied Surface Concepts Group.

B. PRINCIPLES OF CONSOLIDATION

The accompanying consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated. The U.S. dollar is the functional currency for all the Company's U.S. operations and its Irish subsidiary. For these operations, all gains and losses from completed currency transactions are included in income currently. The functional currency for the Company's other non-U.S. subsidiaries is the local currency. Assets and liabilities are translated into U.S. dollars at the rates of exchange at the end of the period, and revenues and expenses are translated using average rates of exchange. Foreign currency translation adjustments are reported as a component of accumulated other comprehensive loss in the consolidated statements of shareholders equity.

C. CASH EQUIVALENTS

The Company considers all highly liquid short-term investments with original maturities of three months or less to be cash equivalents. A substantial majority of the Company's cash and cash equivalent bank balances exceed federally insured limits at September 30, 2012.

D. SHORT-TERM INVESTMENTS

In general, short-term investments have a maturity of three months to one year at the date of purchase. Short-term investments classified as held-to-maturity are recorded at cost, which approximates fair value.

E. CONCENTRATIONS OF CREDIT RISK

Receivables are presented net of allowance for doubtful accounts of \$614 and \$664 at September 30, 2012 and 2011, respectively. Accounts receivable outstanding longer than the contractual payment terms are considered past due. The Company writes off accounts receivable when they become uncollectible. During fiscal 2012 and 2011, \$322 and \$133 of accounts receivable were written off against the allowance for doubtful accounts, respectively. Bad debt expense totaled \$164 and \$196 in fiscal 2012 and 2011, respectively.

Most of the Company's receivables represent trade receivables due from manufacturers of turbine engines and aircraft components as well as turbine engine overhaul companies located throughout the world, including a significant concentration of U.S. based companies. In fiscal 2012, approximately 44% of the Company's net sales were to four (4) of its largest customers and approximately 66% of the Company's net sales were to a combination of five (5) of its largest customers and their direct subcontractors. No other single customer or group represents greater than 5% of total net sales in fiscal 2012. At September 30, 2012, approximately 39% of the Company's outstanding net accounts receivable were due from four (4) of its largest customers and approximately 61% of the Company's outstanding net accounts receivable were due from a combination of five (5) of its largest customers and their direct subcontractors. The Company performs ongoing credit evaluations of its customers' financial conditions. The Company believes its allowance for doubtful accounts is sufficient based on the credit exposures outstanding at September 30,

2012.

F. INVENTORY VALUATION

Inventories are stated at the lower of cost or market. For a portion of the Forge Group's inventory, cost is determined using the last-in, first-out (LIFO) method. For approximately 42% and 54% of the Company's inventories at September 30, 2012 and 2011, respectively, the LIFO method is used to value the Company's inventories. The first-in, first-out (FIFO) method is used to value the remainder of the Company's inventories.

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

The Company maintains allowances for obsolete and excess inventory. The Company evaluates its allowances for obsolete and excess inventory each quarter. Each business segment maintains policies, which require at a minimum that reserves be established based on an analysis of the age of the inventory. In addition, if the Company identifies specific obsolescence, other than that identified by the aging criteria, an additional reserve will be recognized. Specific obsolescence and excess reserve requirements may arise due to technological or market changes, or based on cancellation of an order. The Company's reserves for obsolete and excess inventory were \$1,718 and \$1,398 at September 30, 2012 and 2011, respectively.

G. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment are stated at cost. Depreciation is generally computed using the straight-line and the double declining balance methods. Depreciation is provided in amounts sufficient to amortize the cost of the assets over their estimated useful lives. Depreciation provisions are based on estimated useful lives: (i) buildings, including building improvements - 5 to 50 years; (ii) machinery and equipment, including office and computer equipment - 3 to 30 years, (iii) software - 1 to 10 years and (iv) leasehold improvements - 3 to 6 years.

The Company reviews the carrying value of its long-lived assets, including property, plant and equipment, at least annually or when events and circumstances warrant such a review. This review is performed using estimates of future undiscounted cash flows, which include proceeds from disposal of assets. If the carrying value of a long-lived asset is greater than the estimated undiscounted future cash flows, then the long-lived asset is considered impaired and an impairment charge is recorded for the amount by which the carrying value of the long-lived asset exceeds its fair value. Asset impairment charges of \$219 were recorded in fiscal 2011 related to certain machinery and equipment of the Company's Repair Group. The impairment is recorded in loss (gain) on disposal or impairment of operating assets in the accompanying statements of operations. The machinery and equipment was determined to be impaired and, therefore, the carrying value of such assets was reduced to its net realizable value.

The Company's Irish subsidiary sold its operating business and retained ownership of its Cork, Ireland facility after the business was sold. This property is subject to a lease arrangement with the acquirer of the business. At September 30, 2012, the carrying value of the property is \$1,790 and is included in corporate identifiable assets (see Note 11). Rental income of \$433 and \$443 was recognized in fiscal 2012 and 2011, and is recorded in other income on the consolidated statements of operations.

H. GOODWILL AND INTANGIBLE ASSETS

Goodwill represents the excess of the purchase price paid over the fair value of the net assets of an acquired business. Goodwill is subject to annual impairment testing and the Company has selected July 31 as the annual impairment testing date. The Company first assesses qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value, including goodwill. If so, then a two-step impairment test is used to identify potential goodwill impairment. The first step of the goodwill impairment test compares the fair value of a reporting unit (as defined) with its carrying amount, including goodwill. If the fair value of the reporting unit exceeds its carrying amount, goodwill is not considered impaired, and the second step of the goodwill impairment test is not required. The second step measures the amount of impairment, if any, by comparing the carrying value of the goodwill associated with a reporting unit to the implied fair value of the goodwill derived from the estimated overall fair value of the reporting unit and the individual fair values of the other assets and liabilities of the reporting unit.

Intangible assets consist of identifiable intangibles acquired or recognized in the accounting for the acquisition of a business and include such items as a trade name, a non-compete agreement, below market lease, customer relationships and order backlog. Intangible assets are amortized over their useful lives ranging from less than one year to ten years.

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

I. NET INCOME PER SHARE

The Company's net income per basic share has been computed based on the weighted-average number of common shares outstanding. Net income per diluted share reflects the effect of the Company's outstanding stock options, restricted shares and performance shares under the treasury stock method. The dilutive effect of the Company's stock options, restricted shares and performance shares were as follows:

	September 30,	
	2012	2011
Net income	\$ 6,548	\$ 7,449
Weighted-average common shares outstanding (basic)	5,317	5,271
Effect of dilutive securities:		
Stock options	15	38
Restricted shares	6	8
Performance shares	42	7
Weighted-average common shares outstanding (diluted)	5,380	5,324
Net income per share - basic	\$ 1.23	\$ 1.41
Net income per share - diluted	\$ 1.22	\$ 1.40

Outstanding share awards relating to approximately 144 and 123 weighted average shares were excluded from the calculation of diluted earnings per share for the twelve months ended September 30, 2012 and 2011, respectively, as the impact of including such share awards in the calculation of diluted earnings per share would have had an anti-dilutive effect.

J. REVENUE RECOGNITION

The Company recognizes revenue in accordance with the relevant portions of the guidance provided by the United States Securities and Exchange Commission (SEC) related to revenue recognition in financial statements. Revenue is generally recognized when products are shipped or services are provided to customers.

K. IMPACT OF RECENTLY ADOPTED ACCOUNTING STANDARDS

In July 2012, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update (ASU) 2012-2, *Intangibles - Goodwill and Other*, which allows an entity to first assess qualitative factors to determine whether it is more likely than not that an indefinite-lived asset is impaired for determining whether it is necessary to perform the quantitative impairment test. The ASU is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. Early adoption is permitted. The adoption of this ASU did not have a material impact on the Company's consolidated financial statements.

In September 2011, the FASB issued ASU 2011-09, *Disclosures about an Employer's Participation in a Multiemployer Plan* which requires the Company to provide additional quantitative and qualitative disclosures for multiemployer pension plans and multiemployer other postretirement benefit plans in which the Company participates. The ASU is effective for fiscal years ending after December 15, 2011, with early adoption permitted. The adoption of this guidance did not have a material impact on the Company's consolidated financial statements.

L. IMPACT OF NEWLY ISSUED ACCOUNTING STANDARDS

In December 2011, the FASB issued ASU 2011-12, *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in ASU 2011-05*, and as a result entities are required to continue to report reclassifications out of accumulated other comprehensive income consistent with the presentation requirements in effect before ASU 2011-05. This update is effective for public companies with fiscal years beginning after December 15, 2011. The Company does not expect the adoption of this guidance to have a material impact on its consolidated financial statements.

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

M. USE OF ESTIMATES

Accounting principles generally accepted in the U.S. (GAAP) require management to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent liabilities, at the date of the consolidated financial statements, and the reported amounts of revenues and expenses during the period in preparing these financial statements. Actual results could differ from those estimates.

N. DERIVATIVE FINANCIAL INSTRUMENTS

The Company uses an interest rate swap agreement to reduce risk related to variable-rate debt, which is subject to changes in market rates of interest. The interest rate swap is designated as a cash flow hedge. At September 30, 2012, the Company held an interest rate swap agreement with a notional amount of \$8,000. Cash flows related to the interest rate swap agreement are included in interest expense. The Company's interest rate swap agreement and its variable-rate term debt are based upon LIBOR. During fiscal year 2012, the Company's interest rate swap agreement qualified as a fully effective cash flow hedge against the Company's variable-rate term note interest risk. The following table reports the effects of the mark-to-market valuation of the Company's interest rate swap agreement at September 30, 2012:

Interest rate swap agreement market value adjustment	\$ (93)
Tax effect of interest rate swap agreement market value adjustment	35
Net interest rate swap agreement market value adjustment	\$ (58)

Historically, the Company has been able to mitigate the impact of foreign currency risk, to the extent it existed, by means of hedging such risk through the use of foreign currency exchange contracts, which typically expired within one year. However, such risk was mitigated only for the periods for which the Company had foreign currency exchange contracts in effect, and only to the extent of the U.S. dollar amounts of such contracts. At September 30, 2012 and 2011, the Company had no foreign currency exchange contracts outstanding.

O. RESEARCH AND DEVELOPMENT

Research and development costs are expensed as incurred. Research and development expense was approximately \$1,046 and \$946 in fiscal 2012 and 2011, respectively.

P. ACCUMULATED OTHER COMPREHENSIVE LOSS

Comprehensive income is included on the consolidated statements of shareholders' equity. The components of accumulated other comprehensive loss as shown on the consolidated balance sheets at September 30 are as follows:

	2012	2011
Foreign currency translation adjustment, net of income tax benefit of \$200 and \$410, respectively	\$ (5,566)	\$ (5,770)
Net retirement plan liability adjustment, net of income tax benefit of \$4,090 and \$4,157, respectively	(6,720)	(6,932)
Interest rate swap agreement, net of income tax benefit of \$35 in 2012	(58)	0
Total accumulated other comprehensive loss	\$ (12,344)	\$ (12,702)

Q. INCOME TAXES

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The Company files a consolidated U.S. federal income tax return and tax returns in various state and local jurisdictions. The Company's non-U.S. subsidiaries also file tax returns in various jurisdictions, including Ireland, the United Kingdom, France and Sweden. The Company has provided U.S. deferred income taxes on all cumulative earnings of non-U.S. subsidiaries.

The Company provides deferred income taxes for the temporary difference between the financial reporting basis and tax basis of the Company's assets and liabilities. Such taxes are measured using the enacted tax rates that are assumed to be in effect when the differences reverse. Deferred tax assets result principally from recording certain expenses in the financial statements in excess of amounts currently deductible for tax purposes. Deferred tax liabilities result principally from tax depreciation in excess of book depreciation and unremitted foreign earnings.

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

The Company maintains a valuation allowance against its deferred tax assets when management believes it is more likely than not that all or a portion of a deferred tax asset may not be realized. Changes in valuation allowances are included in the income tax provision in the period of change. In determining whether a valuation allowance is warranted, the Company evaluates factors such as prior earnings history, expected future earnings, carry-back and carry-forward periods and tax strategies that could potentially enhance the likelihood of the realization of a deferred tax asset.

R. RECLASSIFICATIONS

Certain amounts in prior years may have been reclassified to conform to the 2012 consolidated financial statement presentation.

2. Inventories**2. Inventories**

Inventories at September 30 consist of:

	2012	2011
Raw materials and supplies	\$ 4,551	\$ 4,216
Work-in-process	9,162	3,194
Finished goods	4,979	2,829
Total inventories	\$ 18,692	\$ 10,239

If the FIFO method had been used for the entire Company, inventories would have been \$9,537 and \$7,974 higher than reported at September 30, 2012 and 2011, respectively.

3. Goodwill and Intangible Assets**3. Goodwill and Intangible Assets**

The Company's intangible assets by major asset class subject to amortization as of:

September 30, 2012	Estimated Useful Life	Original Cost	Accumulated Amortization	Net Book Value
Intangible assets:				
Trade name	10 years	\$ 1,900	\$ 254	\$ 1,646
Non-compete agreement	5 years	1,500	364	1,136
Below market lease	5 years	900	325	575
Customer relationships	10 years	13,000	1,796	11,204
Order backlog	1 year	2,100	2,034	66
Transition services agreement	< 1 year	23	23	0
Total intangible assets		\$ 19,423	\$ 4,796	\$ 14,627

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September 30, 2011

Intangible assets:				
Trade name	10 years	\$ 900	\$ 73	\$ 827
Non-compete agreement	5 years	500	81	419
Below market lease	5 years	900	145	755
Customer relationships	10 years	6,800	548	6,252
Order backlog	1 year	1,300	1,047	253
Transition services agreement	< 1 year	23	23	0
Total intangible assets		\$ 10,423	\$ 1,917	\$ 8,506

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

Included in the intangible assets at September 30, 2012 are assets acquired in connection with the purchase of the forging business and substantially all related operating assets from GEL Industries, Inc. (DBA Quality Aluminum Forge, Inc.) on October 28, 2011, as discussed more fully in Note 12. These acquired intangible assets consist of:

	Estimated Useful Life	Original Cost
Intangible assets:		
Trade name	10 years	\$ 1,000
Non-compete agreement	5 years	1,000
Customer relationships	10 years	6,200
Order backlog	1 year	800
Total intangible assets		\$ 9,000

The amortization expense on identifiable intangible assets for fiscal 2012 and 2011 was \$2,879 and \$1,917 respectively. Amortization expense associated with the identified intangible assets, all of which relates to the Forged Components Group, is expected to be as follows:

	Amortization Expense
Fiscal year 2013	\$ 2,037
Fiscal year 2014	1,970
Fiscal year 2015	1,970
Fiscal year 2016	1,744
Fiscal year 2017	1,507

Goodwill, all of which relates to the Forged Components Group, is not amortized, but is subject to an annual impairment test. The Company tests its goodwill for impairment in the fourth fiscal quarter, and in interim periods if certain events occur indicating that the carrying amount of goodwill may be impaired. During fiscal 2012, the Company performed a quantitative assessment of goodwill for impairment. The impairment test consisted of a comparison between the fair value of the indefinite lived intangible assets, as determined by projected undiscounted cash flows from future operations, and the carrying values. The Company concluded that no impairment exists as of September 30, 2012. All of the goodwill is expected to be deductible for tax purposes. Changes in the net carrying amount of goodwill were as follows:

Balance at September 30, 2011	\$ 3,493
Goodwill acquired during the year	3,522
Balance at September 30, 2012	\$ 7,015

4. Accrued Liabilities

4. Accrued Liabilities

Accrued liabilities at September 30 consist of:

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	2012	2011
Accrued employee compensation and benefits	\$ 1,574	\$ 1,792
Accrued workers compensation	668	674
Accrued dividends	1,073	1,060
Other accrued liabilities	1,638	1,100
Total accrued liabilities	\$ 4,953	\$ 4,626

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

5. Government Grants

5. Government Grants

In previous periods the Company received grants from certain government entities as an incentive to invest in facilities, research and employees. Capital grants are amortized into income over the estimated useful lives of the related assets. Employment grants are amortized into income over five years. The unamortized portion of deferred grant revenue is recorded in other long-term liabilities at September 30, 2012 and 2011, which amounted to \$336 and \$375, respectively. The majority of the Company's grants are denominated in Euros. The Company adjusts its deferred grant revenue balance in response to currency exchange rate fluctuations for as long as such grants are treated as obligations.

6. Long-Term Debt

6. Long-Term Debt

Long-term debt at September 30 consists of:

	2012	2011
Revolving credit agreement	\$ 11,338	\$ 1,184
Term loan	8,000	0
Promissory Note	2,345	0
Other	2	32
	21,685	1,216
Less current maturities	2,002	30
Total long-term debt	\$ 19,683	\$ 1,186

In October 2011, the Company entered into an amendment to its existing credit agreement (the Credit Agreement Amendment) with its bank to increase the maximum borrowing amount from \$30.0 million to \$40.0 million, of which \$10.0 million is a five (5) year term loan and \$30.0 million is a five (5) year revolving loan, secured by substantially all the assets of the Company and its U.S. subsidiaries and a pledge of 65% of the stock of its non-U.S. subsidiaries. The term loan is repayable in quarterly installments of \$0.5 million starting December 1, 2011.

The term loan has a Libor-based variable interest rate that was 2.2% at September 30, 2012 and which becomes an effective fixed rate of 2.9% after giving effect to an interest rate swap agreement. Borrowing under the revolving loan bears interest at a rate equal to Libor plus 0.75% to 1.75%, which percentage fluctuates based on the Company's leverage ratio of outstanding indebtedness to EBITDA. At September 30, 2012 the interest rate was 1.25%. The loans are subject to certain customary financial covenants including, without limitation, covenants that require the Company to not exceed a maximum leverage ratio and to maintain a minimum fixed charge coverage ratio. There is also a commitment fee ranging from 0.10% to 0.25% to be incurred on the unused balance. The Company was in compliance with all applicable loan covenants as of September 30, 2012.

In connection with the acquisition of the Quality Aluminum Forge business (QAF), as discussed more fully in Note 12, the Company issued a \$2.4 million non-interest bearing promissory note to the seller, which note is payable by the Company in November, 2013. The imputed interest rate used to discount the note was 2% per annum.

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

7. Income Taxes

7. Income Taxes

The components of income before income tax provision are as follows:

	Years Ended September 30,	
	2012	2011
U.S.	\$ 8,419	\$ 10,388
Non-U.S.	981	850
Income before income tax provision	\$ 9,400	\$ 11,238

The income tax provision consists of the following:

	Years Ended September 30,	
	2012	2011
Current income tax provision:		
U.S. federal	\$ 2,530	\$ 2,486
U.S. state and local	465	463
Non-U.S.	229	162
Total current tax provision	3,224	3,111
Deferred income tax provision (benefit):		
U.S. federal	(396)	627
U.S. state and local	(40)	(62)
Non-U.S.	64	113
Total deferred tax provision (benefit)	(372)	678
Income tax provision	\$ 2,852	\$ 3,789

The income tax provision differs from amounts currently payable or refundable due to certain items reported for financial statement purposes in periods that differ from those in which they are reported for tax purposes. The income tax provision in the accompanying consolidated statements of operations differs from amounts determined by using the statutory rate as follows:

	Years Ended September 30,	
	2012	2011
Income before income tax provision	\$ 9,400	\$ 11,238
Less-U.S. state and local income tax provision	465	401
Income before U.S. and non-U.S. federal income tax provision	\$ 8,935	\$ 10,837

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Income tax provision at U.S. federal statutory rates	\$ 3,038	\$ 3,693
Tax effect of:		
Domestic production activities deduction	(278)	(275)
Undistributed earnings of non-U.S. subsidiaries	(91)	132
State and local income taxes	425	401
Federal tax credits	(330)	(289)
Other	88	127
Income tax provision	\$ 2,852	\$ 3,789

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

Deferred tax assets and liabilities at September 30 consist of the following:

	2012	2011
Deferred tax assets:		
Net non-U.S. operating loss carryforwards	\$ 592	\$ 592
Employee benefits	3,282	2,910
Inventory reserves	664	641
Asset impairment reserve	398	435
Allowance for doubtful accounts	154	190
Foreign tax credits	3,021	3,221
Other	43	149
Total deferred tax assets	8,154	8,138
Deferred tax liabilities:		
Depreciation	(2,954)	(3,336)
Unremitted foreign earnings	(4,454)	(5,083)
Other	(248)	0
Total deferred tax liabilities	(7,656)	(8,419)
Net deferred tax assets (liabilities)	498	(281)
Valuation allowance	(579)	(452)
Net deferred tax liabilities	\$ (81)	\$ (733)

At September 30, 2012, the Company has a non-U.S. tax loss carryforward of approximately \$5,458, which relates to the Company's Irish subsidiary that ceased operations in 2007. A valuation allowance has been recorded against the deferred tax asset related to this non-U.S. tax loss carryforward because it is unlikely that such operating loss can be utilized unless the Irish subsidiary resumed operations. The non-U.S. tax loss carryforward does not expire.

The Company recognized a \$127 increase in the valuation allowance against its net deferred tax assets in fiscal years 2012 and a \$12 reduction in the valuation allowance against its net deferred tax assets in fiscal 2011.

The Company reported liabilities for uncertain tax positions, which includes any related interest and penalties, in fiscal 2012 and 2011 of \$120 and \$96, respectively. During fiscal 2012, the Company recognized a nominal amount for interest and no amount for penalties. Based on the statute of limitations for specific jurisdictions, the related unrecognized tax benefit for positions previously taken may change in the next 12 months by approximately \$3, which would be recorded through income tax expense. The Company classifies interest and penalties on uncertain tax positions as income tax expense. A summary of activity related to the Company's uncertain tax position is as follows:

	2012	2011
Balance at beginning of year	\$ 96	\$ 63
Increase due to tax positions taken in current year	55	46
Increase due to tax positions taken in prior years	1	14
Lapse of statute of limitations	(32)	(27)
Balance at end of year	\$ 120	\$ 96

SIFCO Industries, Inc. and Subsidiaries

Notes to Consolidated Financial Statements (Continued)

The Company is subject to income taxes in the U.S. federal jurisdiction, and various states, local and non-U.S. jurisdictions. The Company is no longer subject to U.S. federal, state and local or non-U.S. income tax examinations for the years prior to fiscal year 2006.

8. Retirement Benefit Plans

8. Retirement Benefit Plans

Defined Benefit Plans

The Company and certain of its subsidiaries sponsor defined benefit pension plans covering most of its employees. The Company's funding policy for its defined benefit pension plans is based on an actuarially determined cost method allowable under Internal Revenue Service regulations. One of the Company's defined benefit pension plans, which covers substantially all non-union employees of the Company's U.S. operations who were hired prior to March 1, 2003, was frozen in 2003. Consequently, although the plan otherwise continues, the plan ceased the accrual of additional pension benefits for service subsequent to March 1, 2003.

The Company uses a September 30 measurement date for its U.S. defined benefit pension plans. Net pension expense, benefit obligations and plan assets for the Company-sponsored defined benefit pension plans consists of the following:

	Years Ended September 30,	
	2012	2011
Service cost	\$ 266	\$ 273
Interest cost	988	1,059
Expected return on plan assets	(1,413)	(1,454)
Amortization of prior service cost	47	117
Amortization of net loss	861	682
Early retirement expense	0	61
Settlement cost	513	0
Net pension expense for defined benefit plan	\$ 1,262	\$ 738

The status of all defined benefit pension plans at September 30 is as follows:

2012	2011
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