FERRO CORP
Form 10-Q
November 05, 2008

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

(**Mark One)**

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

For the quarterly period ended September 30, 2008

or

o **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 1-584

FERRO CORPORATION

(Exact name of registrant as specified in its charter)

Ohio	**34-0217820**
(State of Corporation)	(IRS Employer Identification No.)
1000 Lakeside Avenue **Cleveland, OH**	**44114**
(Address of Principal executive offices)	(Zip Code)

216-641-8580

(Telephone Number)

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 þ NO o

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

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

At October 31, 2008, there were 43,743,117 shares of Ferro Common Stock, par value $1.00, outstanding.

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PART I FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)
Ferro Corporation and Consolidated Subsidiaries
Condensed Consolidated Statements of Income

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007
	(Dollars in thousands, except per share amounts)			
Net sales	$ 608,588	$ 550,701	$ 1,866,240	$ 1,634,064
Cost of sales	494,577	450,553	1,515,526	1,319,609
Gross profit	114,011	100,148	350,714	314,455
Selling, general and administrative expenses	78,274	71,069	238,122	234,212
Restructuring charges	9,042	5,826	22,280	7,689
Other expense (income):				
Interest expense	12,497	14,488	39,740	46,220
Interest earned	(213)	(271)	(484)	(1,425)
Loss on extinguishment of debt	5,531		5,531	
Foreign currency losses (gains), net	1,660	(10)	769	924
Miscellaneous expense (income), net	727	(13)	4,659	(399)
Income before taxes	6,493	9,059	40,097	27,234
Income tax expense	1,605	3,472	16,688	10,814
Income from continuing operations	4,888	5,587	23,409	16,420
Loss from discontinued operations, net of tax	57	2	73	216
Net income	4,831	5,585	23,336	16,204
Dividends on preferred stock	225	252	675	797
Net income available to common shareholders	$ 4,606	$ 5,333	$ 22,661	$ 15,407
Per common share data				
Basic earnings:				
From continuing operations	$ 0.11	$ 0.12	$ 0.53	$ 0.36
From discontinued operations	0.00	0.00	0.00	0.00
	$ 0.11	$ 0.12	$ 0.53	$ 0.36
Diluted earnings:				
From continuing operations	$ 0.11	$ 0.12	$ 0.52	$ 0.36
From discontinued operations	0.00	0.00	0.00	0.00
	$ 0.11	$ 0.12	$ 0.52	$ 0.36
Cash dividends declared	$ 0.145	$ 0.145	$ 0.435	$ 0.435

See accompanying notes to condensed consolidated financial statements.

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Ferro Corporation and Consolidated Subsidiaries
Condensed Consolidated Balance Sheets

	September 30, 2008	December 31, 2007
	(Dollars in thousands)	
ASSETS		
Current assets		
Cash and cash equivalents	$ 14,524	$ 12,025
Accounts and trade notes receivable, net	253,183	245,369
Note receivable from Ferro Finance Corporation	29,708	29,577
Inventories	306,254	262,799
Deferred income taxes	23,549	15,764
Other receivables	52,500	33,419
Other current assets	7,412	8,239
Total current assets	687,130	607,192
Other assets		
Property, plant and equipment, net	506,382	519,959
Goodwill	290,088	291,070
Amortizable intangible assets, net	11,899	9,071
Deferred income taxes	99,210	100,935
Other non-current assets	112,581	110,033
Total assets	$ 1,707,290	$ 1,638,260
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities		
Loans payable and current portion of long-term debt	$ 7,372	$ 5,444
Accounts payable	263,189	269,591
Income taxes	23,926	
Accrued payrolls	33,286	26,415
Accrued expenses and other current liabilities	90,235	108,882
Total current liabilities	418,008	410,332
Other liabilities		
Long-term debt, less current portion	601,997	520,645
Postretirement and pension liabilities	130,151	140,988
Deferred income taxes	9,416	9,848
Other non-current liabilities	53,068	56,644
Total liabilities	1,212,640	1,138,457
Minority interests	10,318	9,896
Series A convertible preferred stock (approximates redemption value)	12,517	13,623
Shareholders equity		
Common stock	52,323	52,323
Paid-in capital	167,105	166,391

Retained earnings	471,463	468,190
Accumulated other comprehensive loss	(18,827)	(7,765)
Common shares in treasury, at cost	(200,249)	(202,855)
Total shareholders equity	471,815	476,284
Total liabilities and shareholders equity	$ 1,707,290	$ 1,638,260

See accompanying notes to condensed consolidated financial statements.

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Ferro Corporation and Consolidated Subsidiaries
Condensed Consolidated Statement of Shareholders Equity and Comprehensive Income

	Common Shares in Treasury Shares	Common Shares in Treasury Amount	Common Stock	Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Share-holders Equity
				(In thousands)			
Balances at December 31, 2007	8,753	$ (202,855)	$ 52,323	$ 166,391	$ 468,190	$ (7,765)	$ 476,284
Net income					23,336		23,336
Other comprehensive income (loss), net of tax:							
Foreign currency translation adjustments						(15,014)	(15,014)
Postretirement benefit liability adjustments						2,676	2,676
Raw material commodity swap adjustments						454	454
Interest rate swap adjustments						456	456
Total comprehensive income							11,908
Cash dividends:							
Common					(18,883)		(18,883)
Preferred					(675)		(675)
Income tax benefits				32			32
Stock-based compensation transactions	(173)	2,606		682			3,288
Adjustment to initially apply FAS No. 158 as of January 1, 2008					(505)	366	(139)
Balances at September 30, 2008	8,580	$ (200,249)	$ 52,323	$ 167,105	$ 471,463	$ (18,827)	$ 471,815

See accompanying notes to condensed consolidated financial statements.

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Ferro Corporation and Consolidated Subsidiaries
Condensed Consolidated Statements of Cash Flows

	Nine months ended September 30, 2008	Nine months ended September 30, 2007
	(Dollars in thousands)	
Cash flows from operating activities		
Net income	$ 23,336	$ 16,204
Depreciation and amortization	57,770	63,825
Precious metals deposits		70,073
Accounts and trade notes receivable, inventories, and accounts payable	(66,426)	13,696
Note receivable from Ferro Finance Corporation	(131)	(6,804)
Other changes in current assets and liabilities, net	(3,106)	(27,964)
Other adjustments, net	(9,532)	(7,701)
Net cash provided by continuing operations	1,911	121,329
Net cash used for discontinued operations	(73)	(48)
Net cash provided by operating activities	1,838	121,281
Cash flows from investing activities		
Capital expenditures for property, plant and equipment	(51,805)	(43,247)
Expenditures for other assets	(3,400)	
Proceeds from sale of assets and businesses	586	2,704
Dividends received from affiliates	336	551
Net cash used for investing activities	(54,283)	(39,992)
Cash flows from financing activities		
Net borrowings (repayments) under short-term facilities	2,102	(740)
Proceeds from convertible notes	172,500	
Proceeds from revolving credit facility	756,440	592,167
Proceeds from term loan facility		55,000
Extinguishment of 9 1/8% notes	(205,269)	
Principal payments on revolving credit facility	(638,227)	(700,864)
Principal payments on term loan facility	(8,689)	(2,287)
Debt issue costs paid	(5,462)	(1,783)
Proceeds from exercise of stock options	58	9,217
Cash dividends paid	(19,558)	(19,570)
Other financing activities	1,464	(4,442)
Net cash provided by (used for) financing activities	55,359	(73,302)
Effect of exchange rate changes on cash and cash equivalents	(415)	849
Increase in cash and cash equivalents	2,499	8,836
Cash and cash equivalents at beginning of period	12,025	16,985
Cash and cash equivalents at end of period	$ 14,524	$ 25,821

Cash paid during the period for:		
Interest	$ 46,247	$ 46,925
Income taxes	$ 8,379	$ 11,387

See accompanying notes to condensed consolidated financial statements.

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Ferro Corporation and Consolidated Subsidiaries
Notes to Condensed Consolidated Financial Statements
1. Basis of Presentation

Ferro Corporation (Ferro, we, us or the Company) prepared these unaudited condensed consolidated financial statements of Ferro Corporation and its consolidated subsidiaries in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by U.S. GAAP for complete financial statements and, therefore, should be read in conjunction with the consolidated financial statements and related notes included in our Annual Report on Form 10-K for the year ended December 31, 2007. The preparation of financial statements in conformity with U.S. GAAP requires us to make estimates and assumptions that affect the timing and amount of assets, liabilities, equity, revenues and expenses reported and disclosed. Actual amounts could differ from our estimates, resulting in changes in revenues or costs that could have a material impact on the Company s results of operations, financial position, or cash flows. In our opinion, we made all adjustments that are necessary for a fair presentation, and those adjustments are of a normal recurring nature unless otherwise noted. Due to differing business conditions, our various initiatives, and some seasonality, the results for the three and nine months ended September 30, 2008, are not necessarily indicative of the results expected in subsequent quarters or for the full year.

2. Accounting Standards Adopted in the Nine Months Ended September 30, 2008

On January 1, 2008, we adopted FASB Statement No. 157, *Fair Value Measurements*, (FAS No. 157), FASB Staff Position No. FAS 157-1, *Application of FASB Statement No. 157 to FASB Statement No. 13 and Other Accounting Pronouncements That Address Fair Value Measurements for Purposes of Lease Classification or Measurement Under Statement 13*, (FSP No. FAS 157-1), and FASB Staff Position No. FAS 157-2, *Effective Date of FASB Statement No. 157*, (FSP No. FAS 157-2). Effective July 1, 2008, we also adopted FASB Staff Position No. FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset is not Active*, (FSP No. FAS 157-3). FAS No. 157 defines fair value, establishes a framework and gives guidance regarding the methods used for measuring fair value, and expands disclosures about fair value measurements, but does not require any new fair value measurements. FSP No. FAS 157-1 excludes FASB Statement No. 13, *Accounting for Leases*, (FAS No. 13) as well as other accounting pronouncements that address fair value measurement on lease classification or measurement under FAS No. 13 from the scope of FAS No. 157. FSP No. FAS 157-2 delays the effective date of FAS No. 157 for all nonrecurring fair value measurements of nonfinancial assets and nonfinancial liabilities until fiscal years beginning after November 15, 2008. FSP No. FAS 157-3 amends FAS No. 157 to give an example of how to determine the fair value of a financial asset in an inactive market, but does not change the fair value measurement principles of FAS No. 157. The portions of these pronouncements that were not delayed were adopted prospectively, and their adoption reduced the disclosed fair value of our borrowings under the revolving credit and term loan facilities and reduced the carrying value of our interest rate swaps. We are currently evaluating the impact on our consolidated financial statements of adopting the deferred portions of these pronouncements on January 1, 2009.

On January 1, 2008, we adopted the measurement provisions of FASB Statement No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R)*, (FAS No. 158). The measurement provisions require companies to measure defined benefit plan assets and obligations as of the annual balance sheet date. Previously, we used September 30 as the measurement date for U.S. pension and other postretirement benefits. We have elected to use the September 30, 2007, measurement of assets and benefit obligations to calculate the fiscal year 2008 expense. Expense for the gap period from September 30 to December 31 is recognized as of January 1, 2008, as a charge of $0.5 million, net of tax, to retained earnings and a credit of $0.4 million, net of tax, to accumulated other comprehensive income.

On January 1, 2008, we adopted FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*, (FAS No. 159). This statement permits us to choose, at specified election dates, to measure eligible items at fair value (the fair value option). For items for which the fair value option has been elected, we would report unrealized gains and losses in earnings at each subsequent reporting date and recognize up-front costs and fees in earnings as incurred. We have not elected to measure any eligible items at fair value, and we do not have any current plans to do so. Therefore, adoption of FAS No. 159 did not have an effect on our consolidated financial statements.

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On January 1, 2008, we adopted Emerging Issues Task Force Issue No. 06-11, *Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards*, (EITF No. 06-11). EITF No. 06-11 requires that the income tax benefit from dividends that are charged to retained earnings and paid to employees for nonvested equity shares be recognized as an increase to paid-in capital. Previously, we recognized this income tax benefit as an increase to retained earnings. Beginning in 2008, we report this income tax benefit as an increase to paid-in capital.

3. Newly Issued Accounting Pronouncements

In December 2007, the FASB issued Statement No. 141(R), *Business Combinations*, (FAS No. 141(R)) and Statement No. 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51*, (FAS No. 160). These statements change the way that companies account for business combinations and noncontrolling interests (e.g., minority interests). Both standards are to be applied prospectively for fiscal years beginning after December 15, 2008. However, FAS No. 160 requires entities to apply the presentation and disclosure requirements retrospectively to comparative financial statements. In 2009, we will retrospectively reclassify the amount of minority interests in consolidated subsidiaries to equity and separately report the amount of net income or loss attributable to minority interests.

In March 2008, the FASB issued Statement No. 161, *Disclosures about Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133*, (FAS No. 161). This Statement requires enhanced disclosures about an entity s derivative and hedging activities. This Statement is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008, with early application encouraged. This Statement encourages, but does not require, comparative disclosures for earlier periods at initial adoption. We do not expect the adoption of FAS No. 161 to have a material impact on our consolidated financial statements.

In April 2008, the FASB issued Staff Position No. FAS 142-3, *Determination of the Useful Life of Intangible Assets*, (FSP No. FAS 142-3). This pronouncement amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under FASB Statement No. 142, *Goodwill and Other Intangible Assets*. FSP No. FAS 142-3 is to be applied prospectively and is effective for financial statements issued for fiscal years beginning after December 15, 2008, with early adoption prohibited. We are currently evaluating its effect on our financial statements.

In May 2008, the FASB issued Staff Position No. APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash upon Conversion (Including Partial Cash Settlement)*, (FSP No. APB 14-1). This pronouncement specifies that issuers of such instruments should separately account for the liability and equity components in a manner that will reflect the entity s nonconvertible debt borrowing rate when interest cost is recognized in subsequent periods. FSP No. APB 14-1 is to be applied retrospectively and is effective for financial statements issued for fiscal years and interim periods beginning after December 15, 2008. If this pronouncement had been applied at September 30, 2008, the carrying value of the liability component of the 6.50% Convertible Senior Notes would have been approximately $152.7 million, including $0.4 million of imputed interest, and the carrying value of the equity component would have been approximately $19.6 million, net of $0.6 million of allocated third-party transaction costs.

4. Inventories

Inventories consisted of the following:

	September 30, 2008	December 31, 2007
	(Dollars in thousands)	
Raw materials	$ 94,975	$ 74,659
Work in process	50,639	41,640
Finished goods	160,640	146,500
Total	$ 306,254	$ 262,799

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In the production of some of our products, we use precious metals, some of which we obtain from financial institutions under consignment agreements with terms of one year or less. The financial institutions retain ownership of the precious metals and charge us fees based on the amounts we consign. These fees were $1.1 million and $0.8 million for the three months ended September 30, 2008 and 2007, respectively, and $3.4 million and $2.8 million for the nine months ended September 30, 2008 and 2007, respectively, and were charged to cost of sales. We had on hand $125.8 million at September 30, 2008, and $148.3 million at December 31, 2007, of precious metals owned by financial institutions, measured at fair value based on market prices for identical assets.

5. Property, Plant and Equipment

Property, plant and equipment is reported net of accumulated depreciation of $668.0 million at September 30, 2008, and $713.5 million at December 31, 2007.

6. Financing and Long-term Debt

Loans payable and current portion of long-term debt consisted of the following:

	September 30, 2008	December 31, 2007
	(Dollars in thousands)	
Loans payable to banks	$ 3,128	$ 954
Current portion of long-term debt	4,244	4,490
Total	$ 7,372	$ 5,444

Long-term debt consisted of the following:

	September 30, 2008	December 31, 2007
	(Dollars in thousands)	
$172.5 million 6.50% Convertible Senior Notes	$ 172,500	$
$200 million 9 1/8% Senior Notes, net of unamortized discounts		199,636
Revolving credit facility	132,070	13,857
Term loan facility	293,261	301,950
Capitalized lease obligations	7,863	8,924
Other notes	547	768
	606,241	525,135
Less current portion	(4,244)	(4,490)
Total	$ 601,997	$ 520,645

Credit Rating

At September 30, 2008, the Company s corporate credit rating was B1, with a positive outlook, by Moody s Investor Services, Inc. and B+, with a stable outlook, by Standard & Poor s Rating Group.

6.50% Convertible Senior Notes

In August 2008, Ferro issued $172.5 million of 6.50% Convertible Senior Notes due 2013 (the Convertible Notes). The proceeds from the offering, along with available cash, including borrowings under Ferro s revolving credit facility, were used to purchase all of Ferro s outstanding 9 1/8% Senior Notes. The Convertible Notes bear interest at a rate of 6.5% per year, payable semi-annually in arrears on February 15 and August 15 of each year, beginning on February 15, 2009. The Convertible Notes mature on August 15, 2013.

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The Convertible Notes are convertible, under certain circumstances, using a net share settlement process, into a combination of cash and shares of Ferro s common stock. The initial base conversion price of the Convertible Notes is approximately $32.34, based on the initial base conversion rate of 30.9253 shares of common stock per $1,000 principal amount of Convertible Notes. Upon conversion of a Convertible Note, the holder will receive cash equal to the principal amount of the Convertible Note and shares of common stock to the extent the Convertible Note s conversion value exceeds the principal amount. In addition, upon certain circumstances, Ferro will increase the applicable conversion rate for a holder who elects to convert its Convertible Notes. The number of additional shares of common stock is determined pursuant to a specified formula, which is dependent on the Company s stock price at the time of conversion. Ferro may be required to repurchase the Convertible Notes if Ferro is involved in certain types of corporate transactions or other events constituting a fundamental change.

9 1/8% Senior Notes

In June 2008, Ferro commenced a cash tender offer to purchase any and all of its outstanding $200 million aggregate principal amount of 9 1/8% Senior Notes due 2009 (the 9 1/8% Notes). In August and September, we purchased all of the 9 1/8% Notes for $205.3 million, including call premiums and tender costs, and recorded a loss of $5.5 million, including unamortized discounts and fees. We financed the purchase of the 9 1/8% Notes and related costs from the issuance of the Convertible Notes, along with available cash, including borrowings under Ferro s revolving credit facility.

Revolving Credit and Term Loan Facilities

In 2006, we entered into an agreement with a group of lenders for a $700 million credit facility, consisting of a multi-currency senior revolving credit facility and a senior term loan facility. In 2007, we cancelled the unused portion of the term loan facility and amended the credit facility (the Amended Credit Facility). At September 30, 2008, the Amended Credit Facility consisted of a $300 million revolving credit facility, which matures in 2011, and a $305 million term loan facility, which matures in 2012. As part of the agreement, we can request an increase of $50 million in the revolving credit facility. We had $159.3 million at September 30, 2008, and $277.5 million at December 31, 2007, available under the revolving credit facility, after reductions for standby letters of credit secured by this facility.

In 2007, we began making periodic principal payments on the term loans. We are required to make minimum quarterly principal payments of $0.8 million from July 2008 to July 2011. During the last year of the loan s life, we are required to repay the remaining balance of the term loans in four quarterly installments. Currently, those last four payments will be $71.0 million each. In addition to the minimum quarterly payments, each April we may be required to make an additional principal payment. The amount of this additional payment is dependent on the Company s leverage and certain cash flow metrics. Any additional payment that is required reduces, on a dollar-for-dollar basis, the amount due in the last four quarterly payments. In April 2008, we made an additional principal payment of $6.4 million.

The interest rates under the Amended Credit Facility are equal to the sum of (A) either (1) LIBOR or (2) the higher of the Federal Funds Rate plus 0.5% or the Prime Rate and (B) for the revolving credit facility, a variable margin based on the Company s leverage, or for the term loan facility, a fixed margin. As part of the 2007 amendments, $175 million of borrowings under the term loan facility were restricted to using three-month LIBOR in determining their interest rates. This change was made in connection with interest rate swap agreements executed in 2007. These swap agreements effectively fixed the interest rate through June 2011 on $150 million of borrowings under the term loan facility. The average interest rate for revolving credit borrowings was 4.4% at September 30, 2008, and 6.5% at December 31, 2007, and the effective interest rate for term loan borrowings after adjusting for the interest rate swaps was 6.2% at September 30, 2008, and 7.2% at December 31, 2007.

Receivable Sales Programs

We have several programs to sell, on an ongoing basis, pools of our trade accounts receivable. These programs accelerate cash collections at favorable financing costs and help us manage the Company s liquidity requirements. The costs associated with these programs are reported as interest expense and were $5.1 million and $5.3 million for the nine months ended September 30, 2008 and 2007, respectively.

In our largest program, we sell substantially all of Ferro s U.S. trade accounts receivable to Ferro Finance Corporation (FFC), a wholly-owned unconsolidated qualified special purpose entity (QSPE). FFC finances its acquisition of trade receivable assets by issuing beneficial interests in (securitizing) the receivables to multi-seller receivables securitization companies (the Conduits). In June 2008, we amended the program to reduce the maximum proceeds and the conduits commitment levels from $100 million to $75 million. Ferro had received net proceeds of $75.0 million at September 30, 2008, and $54.6 million at December 31, 2007, for outstanding receivables. FFC and the Conduits have no recourse to Ferro s other assets for failure of debtors to pay when due, as the assets transferred are legally isolated in accordance with the U.S. bankruptcy laws. Ferro, on behalf of FFC and the Conduits, provides normal collection and administration services for the trade accounts receivable sold.

Activity from this program for the nine months ended September 30 is detailed below:

	2008	2007
	(Dollars in thousands)	
Trade accounts receivable sold to FFC	$ 840,151	$ 739,005
Cash proceeds from FFC	840,405	731,454
Trade accounts receivable collected and remitted to FFC and the conduits	820,027	726,553

In addition, we maintain several international programs to sell trade accounts receivable, primarily without recourse. The commitments supporting these programs can be withdrawn at any time and totaled $78.0 million at September 30, 2008, and $80.8 million at December 31, 2007. Ferro had received net proceeds under the international programs of $28.8 million at September 30, 2008, and $42.1 million at December 31, 2007, for outstanding receivables. Ferro provides normal collection and administration services for the trade accounts receivable sold to certain financial institutions.

Activity from these programs for the nine months ended September 30 is detailed below:

	2008	2007
	(Dollars in thousands)	
Trade accounts receivable sold to financial institutions	$ 186,054	$ 128,788
Cash proceeds from financial institutions	184,628	125,024
Trade accounts receivable collected and remitted to financial institutions for programs where we provide collection and administrative services	60,863	65,060

7. Financial Instruments

The following financial instruments are measured at fair value for disclosure purposes. The carrying values of these instruments may or may not be their fair values.

6.50% Convertible Senior Notes. The carrying amount of the Convertible Notes was $172.5 million and their fair value was $159.7 million at September 30, 2008. The fair value of these notes is based on a third party s estimated bid price.

9 1/8% Senior Notes. The carrying amount of the 9 1/8% Notes was $199.6 million and their fair value was $205.0 million at December 31, 2007. The fair value of these notes is based on a third party s estimated bid price.

Revolving credit facility. The carrying amount of the revolving credit facility was $132.1 million at September 30, 2008, and $13.9 million at December 31, 2007. The fair value of the revolving credit facility was $122.9 million at September 30, 2008, and $13.9 million at December 31, 2007. The fair value of the revolving credit facility is based on the present value of expected future cash flows and assumptions about current interest rates. Beginning in 2008 in connection with the adoption of FAS No. 157, the fair value also reflects assumptions about the creditworthiness of the Company that market participants would use in pricing the debt.

Term loan facility. The carrying amount of the term loan facility was $293.3 million at September 30, 2008, and $302.0 million at December 31, 2007. The fair value of the term loan facility was $272.9 million at September 30, 2008, and $302.0 million at December 31, 2007. The fair value of the term loan facility is based on the present value of expected future cash flows and assumptions about current interest rates. Beginning in 2008 in connection with the adoption of FAS No. 157, the fair value also reflects assumptions about the creditworthiness of the Company that market participants would use in pricing the debt.

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The following financial instruments are measured and recorded at fair value on a recurring basis. The inputs to the valuation techniques used to measure fair value are classified into the following categories:

Level 1:	Quoted market prices in active markets for identical assets or liabilities.
Level 2:	Observable market-based inputs or unobservable inputs that are corroborated by market data.
Level 3:	Unobservable inputs that are not corroborated by market data.

The carrying amount, fair value, and classification within the fair value hierarchy of these financial instruments were as follows:

	September 30, 2008	Fair Value Measurements at September 30, 2008 Level 1	Level 2	Level 3	December 31, 2007
	(Dollars in thousands)				
Assets					
Foreign currency forward contracts	$ 1,374	$	$ 1,374	$	$ 16
Precious metals forward contracts					755
Total fair value	$ 1,374	$	$ 1,374	$	$ 771
Liabilities					
Interest rate swaps	$ (7,401)	$	$ (7,401)	$	$ (8,109)
Foreign currency forward contracts	(73)		(73)		(284)
Raw material commodity swaps	(938)		(938)		(1,499)
Precious metals forward contracts	(6)		(6)		
Total fair value	$ (8,418)	$	$ (8,418)	$	$ (9,892)

Interest rate swaps. To reduce our exposure to interest rate changes on variable-rate debt, we entered into interest rate swap agreements in 2007. These swaps effectively converted $150 million of our variable-rate term loan facility to a fixed rate. We mark these agreements to fair value and recognize the resulting gains or losses as other comprehensive income or loss. In 2007, the fair value of the interest rate swaps was based on settlement prices provided by the counterparties. Beginning in 2008 in connection with the adoption of FAS No. 157, the fair value of the swaps is based on the present value of expected future cash flows, which reflects assumptions about current interest rates and the creditworthiness of the Company that market participants would use in pricing the swaps.

Foreign currency forward contracts. We manage foreign currency risks principally by entering into forward contracts to mitigate the impact of currency fluctuations on transactions. We mark these contracts to fair value based on market prices for comparable contracts and recognize the resulting gains or losses in net foreign currency gains or losses.

Raw material commodity swaps. We hedge a portion of our exposure to changes in the pricing of certain raw material commodities principally using swap arrangements that allow us to fix the price of the commodities for future purchases. We mark these contracts to fair value based on market prices for comparable contracts and recognize the resulting gains or losses as other comprehensive income or loss. After the contracts mature and the materials are sold, the gains and losses are recognized as part of cost of sales.

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Precious metals forward contracts. We enter into forward purchase arrangements with precious metals suppliers to completely cover the value of fixed price sales contracts for products with precious metal content. Some of these agreements, with purchase commitments totaling $13.0 million at September 30, 2008, are designated as normal purchase contracts and are not marked to fair value. We mark the remaining precious metal contracts to fair value based on market prices for comparable contracts and recognize the resulting gains or losses as miscellaneous income or expense.

8. Income Taxes

Income tax expense for the first nine months of 2008 was $16.7 million, or 41.6% of pre-tax income. Income tax expense for the first nine months of 2007 was $10.8 million, or 39.7% of pre-tax income. The reasons for the increase in the effective tax rate were a change in the mix of income by country and a decrease in the U.S. tax cost on foreign dividends. The effective tax rate was also impacted by an unfavorable tax court decision in Brazil, an increase in the valuation allowance, and favorable adjustments to prior-year accruals which, in aggregate, totaled $2.4 million.

During the first nine months of 2008, we allocated income tax expense directly to shareholders equity for the following items: $0.7 million for postretirement benefit liability adjustments, $0.2 million for raw material commodity swap adjustments, $0.2 million for interest rate swap adjustments, and $0.2 million for the adjustments to initially apply FAS No. 158. During the first nine months of 2007, we allocated income tax expense (benefit) directly to shareholders equity for the following items: $0.5 million for postretirement benefit liability adjustments, $(1.2) million for raw material commodity swap adjustments, and $(1.8) million for interest rate swap adjustments.

The Company conducts business globally, and, as a result, the U.S. parent company and its subsidiaries file income tax returns in the U.S. federal jurisdiction and various state and foreign jurisdictions. In the normal course of business, the U.S. parent company and its subsidiaries are subject to examination by taxing authorities throughout the world, including Spain, France, Germany, Netherlands, Italy, Japan, China, Portugal, and the United Kingdom. With few exceptions, we are not subject to federal, state, local or non-U.S. income tax examinations for years before 2000.

9. Contingent Liabilities

As previously disclosed, in February 2003, we produced documents in connection with an investigation by the United States Department of Justice into possible antitrust violations in the heat stabilizer industry. In April 2006, we were notified by the Department of Justice that the Government had closed its investigation. Before closing its investigation, the Department of Justice took no action against the Company or any of its current or former employees. In 2003, the Company was named as a defendant in several lawsuits alleging civil damages and requesting injunctive relief relating to the conduct the Government was investigating, and, in June 2008, the Company was named in four more indirect purchaser lawsuits related to an existing lawsuit in the Eastern District of Pennsylvania. In July 2007, we entered into a definitive written settlement agreement in the class action lawsuit involving direct purchasers. The settlement agreement was approved by the United States District Court for the Eastern District of Pennsylvania in December 2007. Although the Company decided to bring this matter to a close through settlement, the Company did not admit to any of the alleged violations and continues to deny any wrongdoing. The Company is vigorously defending the remaining six civil actions alleging antitrust violations in the heat stabilizer industry. These actions are in their early stages; therefore, we cannot determine the outcomes of these lawsuits at this time. In December 2006, we filed a lawsuit against the former owner of our heat stabilizer business seeking indemnification for the defense of these lawsuits and any resulting payments by the Company. In April 2008, the United States District Court for the Northern District of Ohio dismissed our lawsuit, and we have appealed the court s decision to the United States Court of Appeals for the Sixth Circuit.

There are various other lawsuits and claims pending against the Company and its consolidated subsidiaries. In our opinion, the ultimate liabilities, if any, and expenses resulting from such lawsuits and claims will not materially affect the consolidated financial position, results of operations, or cash flows of the Company.

The Company had bank guarantees and standby letters of credit issued by financial institutions, which totaled $14.4 million at September 30, 2008, and $17.7 million at December 31, 2007. These agreements primarily relate to Ferro s insurance programs, potential environmental remediation liabilities, and foreign tax payments. If the Company fails to perform its obligations, the guarantees and letters of credit may be drawn down by their holders, and we would be liable to the financial institutions for the amounts drawn.

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10. Retirement Benefits

Information concerning net periodic benefit costs of our U.S. pension plans (including our unfunded nonqualified plans), non-U.S. pension plans, and postretirement health care and life insurance benefit plans for the three months ended September 30 is as follows:

	U.S. Pension Plans		Non-U.S. Pension Plans		Other Benefit Plans	
	2008	2007	2008	2007	2008	2007
			(Dollars in thousands)			
Components of net periodic cost:						
Service cost	$ 50	$ 317	$ 1,308	$ 1,663	$ 16	$ 124
Interest cost	5,177	5,026	2,955	2,359	731	836
Expected return on plan assets	(5,663)	(5,140)	(2,148)	(1,871)		
Amortization of prior service cost	25	39	29	27	(411)	(349)
Net amortization and deferral	624	1,456	53	148		
Curtailment and settlement effects			(133)			(814)
Special termination benefits				2,189		
Net periodic benefit cost	$ 213	$ 1,698	$ 2,064	$ 4,515	$ 336	$ (203)

Information concerning net periodic benefit costs of our U.S. pension plans (including our unfunded nonqualified plans), non-U.S. pension plans, and postretirement health care and life insurance benefit plans for the nine months ended September 30 is as follows:

	U.S. Pension Plans		Non-U.S. Pension Plans		Other Benefit Plans	
	2008	2007	2008	2007	2008	2007
			(Dollars in thousands)			
Components of net periodic cost:						
Service cost	$ 150	$ 948	$ 4,366	$ 4,888	$ 48	$ 428
Interest cost	15,531	15,083	8,934	6,937	2,193	2,554
Expected return on plan assets	(16,989)	(15,392)	(6,484)	(5,499)		
Amortization of prior service cost	75	118	78	82	(1,233)	(935)
Net amortization and deferral	1,872	4,405	165	434		
Curtailment and settlement effects		250	(133)			(814)
Special termination benefits				2,189		
Net periodic benefit cost	$ 639	$ 5,412	$ 6,926	$ 9,031	$ 1,008	$ 1,233

The change in net periodic cost is due primarily to restructuring activities related to closing the Company s Rotterdam, Netherlands, and Niagara Falls, New York, manufacturing facilities, the freezing of pension benefits at several U.S. plants, and the limiting of eligibility for retiree medical and life insurance coverage for nonunion employees. We recorded curtailment gains of $0.1 million in the third quarter of 2008 and special termination benefits of $2.2 million in the third quarter of 2007 for pension benefits related to the Rotterdam, Netherlands, closing. We recorded curtailment gains of $0.7 million in the third quarter of 2007 for other benefits and curtailment losses of $0.3 million in the first quarter of 2007 for pension benefits related to the Niagara Falls, New York, closing.

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11. Stock-Based Compensation

The following table contains the total stock-based compensation expense recorded in selling, general and administrative expense for the nine months ended September 30:

	2008	2007
	(Dollars in thousands)	
Stock options	$ 1,753	$ 2,333
Performance shares	187	794
Deferred stock units	411	505
Restricted shares	307	
Total	$ 2,658	$ 3,632

The following table contains information regarding the stock-based compensation as of and for the nine-month period ended September 30, 2008:

	Number of Shares or Units Granted	Weighted-Average Fair Value per Share or Unit	Aggregate Grant Date Fair Value of Shares or Units Granted (Dollars in thousands)	Remaining Service or Performance Period (In years)
Stock options	513,100	$ 4.27	$ 2,191	3.4
Performance shares	77,825	17.26	1,343	2.4
Deferred stock units	34,200	16.69	571	0.4
Restricted shares	99,600	17.51	1,744	2.4

The stock-based compensation transaction in shareholders equity consisted of the following for the nine months ended September 30, 2008:

	Common Shares in Treasury		Paid-in Capital
	Shares	Amount	
	(In thousands)		
Stock options	(3)	$ 367	$ 2,236
Performance shares, net		25	(654)
Deferred stock units	(33)	143	
Directors deferred compensation		(558)	558
Preferred stock conversions	(38)	689	
Restricted shares	(99)	1,940	(1,458)
Total	(173)	$ 2,606	$ 682

Restricted Share Awards

Under the 2006 Long-Term Incentive Plan, the Company may award restricted shares of Ferro common stock. The restricted shares vest in three years from the date of the award and are forfeited if the recipient s employment terminates, except in the case of death or disability. During the vesting period, the recipient is not entitled to exercise rights pertaining to the restricted shares, including the right to vote such shares, and dividends on the restricted shares are deferred without interest. Following the vesting period, the recipient may not dispose of the shares for two years, without Ferro s prior written consent. The first restricted shares were awarded in 2008.

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12. Restructuring and Cost Reduction Programs

During 2008, we continued several restructuring programs across a number of our business segments with the objectives of leveraging our global scale, realigning and lowering our cost structure and optimizing capacity utilization. The programs are primarily associated with North America and Europe. Management continues to evaluate our business, and therefore, there may be supplemental provisions for new plan initiatives as well as changes in estimates to amounts previously recorded, as payments are made or actions are completed.

In July 2006, we announced that we were restructuring our European operations, including a portion of our Performance Coatings and Color and Glass Performance Materials segments. This program affected operations in Spain, Italy, Portugal, France, Netherlands, and Germany. We expect these actions to significantly reduce the cost structure of our manufacturing operations.

The initial phase of this European restructuring resulted in a workforce reduction of 127 employees in these two segments and we are evaluating further workforce reductions. A decision to proceed with actions related to any additional charges will be made after the Company has completed required consultations with employee representatives at the affected sites. Revised total anticipated charges through 2009 amount to $11.5 million. Charges incurred through 2007 amounted to $9.0 million. Restructuring charges for the nine months ended September 30, 2008, include $1.1 million for employee severance costs, other costs of $0.7 million, and $0.3 million of accrual reversals.

In May 2007, we began the next phase of our European restructuring by initiating discussions with representatives of workers at our Rotterdam, Netherlands, porcelain enamel manufacturing site. In September 2007, we reached an agreement with the Rotterdam Works Council. As a result, the Company discontinued porcelain enamel manufacturing at its Rotterdam facility in the third quarter of 2008 and consolidated production at other European facilities. This consolidation resulted in the reduction of 84 employees. Restructuring charges are expected to total $26.5 million. During 2007, we recorded $11.8 million in restructuring charges and an additional $0.5 million for inventory write downs included in cost of sales. During the first nine months of 2008, we recorded $8.9 million for employee severance costs, $3.8 million for future minimum lease obligations, and $0.9 million in other costs, partly offset by a pension curtailment credit of $0.1 million.

In addition to the European restructuring efforts, we initiated worldwide restructuring plans for our Performance Coatings, Color and Glass Performance Materials, Polymer Additives, and Specialty Plastics segments in November 2007, March 2008, and April 2008. These restructuring plans resulted in the reduction of 109 employees. Total estimated employee termination charges through 2008 are $5.4 million. During 2007, we recorded total charges of $1.4 million. In the first nine months of 2008, we recorded $4.0 million of additional restructuring charges.

In February 2008, we announced the closing of a Plastics facility in Aldridge, United Kingdom. This closure resulted in the reduction of 10 employees and total costs of $0.6 million. During the first nine months of 2008, we recorded $0.4 million in severance costs and $0.2 million in lease termination costs.

In June 2008, we announced the partial closing of a Performance Coatings facility in Americana, Brazil. This closure resulted in the reduction of 66 employees and total costs of $1.5 million. During the first nine months of 2008, we recorded $1.1 million in severance costs and $0.4 million of asset impairment costs.

In September 2008, we closed the Polymer Additives facility in Castanheira, Portugal, which resulted in the elimination of 10 employees with a total cost of $1.2 million. During September 2008, we recorded $0.2 million in severance costs, $0.5 million in contract termination costs, and $0.5 million in asset impairment costs.

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We have summarized the activities and accrual balances related to our restructuring and cost reduction programs below:

	Employee Termination Benefits	Other Costs	Asset Impairment	Total
	(Dollars in thousands)			
Balance, December 31, 2007	$ 8,381	$ 1,560	$	$ 9,941
Restructuring charges	15,346	6,025	909	22,280
Cash payments	(21,570)	(1,723)		(23,293)
Currency translation adjustment	(193)	(363)		(556)
Non-cash items	(76)	(178)	(909)	(1,163)
Balance, September 30, 2008	$ 1,888	$ 5,321	$	$ 7,209

We expect to make cash payments to settle the remaining liability for employee termination benefits and other costs primarily within the next 12 months, except where legal or contractual restrictions prevent us from doing so.

13. Discontinued Operations

Discontinued operations relate to the Powder Coatings, Petroleum Additives and Specialty Ceramics businesses that we sold in 2002 and 2003. There were no sales or cash flows from investing or financing activities from discontinued operations in the nine months ended September 30, 2008 or 2007. The loss from discontinued operations includes ongoing legal costs and reserve adjustments directly related to discontinued operations. Discontinued operations resulted in the following pre-tax losses and related income tax benefits:

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
	(Dollars in thousands)			
Pre-tax losses	$ 94	$ 4	$ 120	$ 355
Tax benefits	37	2	47	139
Net of tax losses	$ 57	$ 2	$ 73	$ 216

We have continuing environmental remediation obligations that are related to these divestitures, and we had accrued $3.3 million at September 30, 2008, and $3.3 million at December 31, 2007, for these matters.

14. Earnings per Share

Details of the calculation of basic and diluted earnings per share are shown below:

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007
	(In thousands, except per share amounts)			
Basic earnings per share computation:				
Net income available to common shareholders	$ 4,606	$ 5,333	$ 22,661	$ 15,407
Add: Loss from discontinued operations	57	2	73	216
	$ 4,663	$ 5,335	$ 22,734	$ 15,623
Weighted-average common shares outstanding	43,266	43,030	43,226	42,881
Basic earnings per share from continuing operations	$ 0.11	$ 0.12	$ 0.53	$ 0.36
Diluted earnings per share computation:				
Net income available to common shareholders	$ 4,606	$ 5,333	$ 22,661	$ 15,407
Add: Loss from discontinued operations	57	2	73	216
Plus: Convertible preferred stock				
	$ 4,663	$ 5,335	$ 22,734	$ 15,623
Weighted-average common shares outstanding	43,266	43,030	43,226	42,881
Assumed conversion of convertible senior notes				
Assumed conversion of convertible preferred stock				
Assumed satisfaction of performance share conditions	76	59	72	54
Assumed satisfaction of deferred stock unit conditions	20	24	11	14
Assumed exercise of stock options	161			
Weighted-average diluted shares outstanding	43,523	43,113	43,309	42,949
Diluted earnings per share from continuing operations	$ 0.11	$ 0.12	$ 0.52	$ 0.36

15. Comprehensive Income

The components of comprehensive income were as follows:

	Three months ended September 30, 2008	Three months ended September 30, 2007	Nine months ended September 30, 2008	Nine months ended September 30, 2007

	(Dollars in thousands)			
Net income	$ 4,831	$ 5,585	$ 23,336	$ 16,204
Other comprehensive income, net of tax:				
Foreign currency translation adjustments	(36,261)	15,441	(15,014)	28,183
Postretirement benefit liability adjustments	3,090	(137)	2,676	(140)
Raw material commodity swap adjustments	(1)	(391)	454	(1,903)
Interest rate swap adjustments	(150)	(2,089)	456	(2,840)
Comprehensive income	$ (28,491)	$ 18,409	$ 11,908	$ 39,504

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16. Reporting for Segments

The Company has six reportable segments: Performance Coatings, Electronic Materials, Color and Glass Performance Materials, Polymer Additives, Specialty Plastics and Other Businesses. We have combined our Tile Coating Systems and Porcelain Enamel business units into one reportable segment, Performance Coatings, based on their similar economic and operating characteristics. We have also combined two of our segments, Pharmaceuticals and Fine Chemicals, into one reportable segment, Other Businesses, because they do not meet the quantitative thresholds for separate disclosure.

The accounting policies of our segments are consistent with those described for our consolidated financial statements in the summary of significant accounting policies contained in our Annual Report on Form 10-K for the year ended December 31, 2007. We measure segment income for internal reporting purposes as income from continuing operations before unallocated corporate expenses, restructuring charges, other expense (income) items, such as interest expense, and income tax expense. Unallocated corporate expenses primarily consist of corporate employment costs and professional services.

Net sales to external customers by segment are presented in the table below. Sales between segments were not material.

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
	(Dollars in thousands)			
Performance Coatings	$ 162,523	$ 153,742	$ 501,819	$ 451,058
Electronic Materials	155,122	116,645	452,317	338,412
Color and Glass Performance Materials	115,013	113,575	374,083	329,195
Polymer Additives	93,081	85,230	284,107	252,903
Specialty Plastics	58,097	62,236	183,499	198,994
Other Businesses	24,752	19,273	70,415	63,502
Total net sales	$ 608,588	$ 550,701	$ 1,866,240	$ 1,634,064

Below are each segment s income and reconciliations to income before taxes from continuing operations:

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
	(Dollars in thousands)			
Performance Coatings	$ 12,135	$ 8,449	$ 34,400	$ 29,947
Electronic Materials	17,095	8,522	43,527	19,534
Color and Glass Performance Materials	9,712	11,727	40,695	39,462
Polymer Additives	4,385	3,417	11,703	10,576
Specialty Plastics	2,796	3,586	7,520	10,961
Other Businesses	2,645	593	7,405	7,982
Total segment income	48,768	36,294	145,250	118,462
Unallocated corporate expenses	13,031	7,215	32,658	38,219
Restructuring charges	9,042	5,826	22,280	7,689
Other expense, net	20,202	14,194	50,215	45,320
Income before taxes from continuing operations	$ 6,493	$ 9,059	$ 40,097	$ 27,234

We sell our products throughout the world, and we attribute sales to countries based on the country where we generate the customer invoice. We have detailed net sales by geographic region in the table below:

	Three months ended September 30,		Nine months ended September 30,	
	2008	2007	2008	2007
	(Dollars in thousands)			
United States	$ 281,502	$ 232,405	$ 811,678	$ 710,423
International	327,086	318,296	1,054,562	923,641
Total net sales	$ 608,588	$ 550,701	$ 1,866,240	$ 1,634,064

17. Subsequent Event

On September 29, 2008, we entered into an agreement for the sale of our fine chemicals business to Novolyte Technologies LP, an affiliate of Arsenal Capital Management LP. On October 31, 2008, we amended the agreement, primarily to reduce the selling price from $66.0 million to $60.0 million, and closed the sale of the U.S. portion of the business for $52.0 million. The remaining $8.0 million of purchase price will be held in escrow until the completion of an equity transfer of Ferro (Suzhou) Energy Storage Materials Co. Ltd. (Ferro Suzhou), a wholly-owned subsidiary of Ferro, which owns the fine chemicals business manufacturing facilities in Suzhou, China. The equity transfer of Ferro Suzhou is subject to certain conditions, including government approval of the equity transfer in China and the receipt of certain permits or licenses. The equity transfer is expected to be completed by the end of 2008.

At September 30, 2008, the fine chemicals business had approximately $25 million of property, plant and equipment, $12 million of accounts receivable, $9 million of inventory, and $7 million of accounts payable and other liabilities.

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

Overview

Net income for the three months ended September 30, 2008, declined to $4.8 million from $5.6 million in the third quarter of 2007. Income declined primarily as a result of higher selling, general and administrative expenses, a loss on the extinguishment of debt resulting from bond refinancing activities and higher restructuring charges. Partially offsetting these higher costs were increased gross profit, resulting from higher sales, and lower interest expense.

Net sales increased by 10.5% primarily as a result of higher sales in our Electronic Materials, Performance Coatings, and Polymer Additives segments. Sales declined in the Specialty Plastics segment, compared with the third quarter of 2007. The primary drivers for the increased sales were improved product pricing and product mix, as well as changes in foreign currency exchange rates. Higher product pricing included increased pass-through of higher precious metal costs.

Raw material costs continued to be volatile in the quarter. While prices of a number of commodities fell during the quarter, these prices did not immediately translate to lower costs within the supply chain. Petrochemical-based input costs declined during the quarter, for instance, but temporary shutdowns of refining capacity in the U.S. Gulf Coast resulting from late-summer hurricanes delayed the downstream effects of lower crude oil prices. In aggregate, raw material prices were higher than in the prior-year period.

Gross profit increased during the third quarter, both in dollar terms and as a percent of sales, compared with the third quarter of 2007. Gross profit percentage continues to be negatively impacted by higher precious metal costs, which we generally pass through to customers with minimal gross profit contribution.

Selling, general and administrative (SG&A) expense increased in the 2008 third quarter compared to the prior year. The principal drivers for the increase were changes in foreign currency exchange rates, and higher incentive compensation and benefit expenses. As a percentage of net sales, our 2008 third quarter SG&A expense was 12.9%, unchanged from the third quarter of 2007.

Interest expense declined in the three months ended September 30, 2008, compared with the prior-year period. The decline was due to lower interest rates on our debt, partially offset by higher average borrowing levels. During the third quarter, we issued new convertible bonds. The proceeds from the new bonds, along with additional borrowings under our revolving credit facility, were used to repay our 9 1/8% coupon senior notes, due January 2009. The repayment of the senior notes resulted in a loss on extinguishment of debt of $5.5 million during the quarter.

Outlook

Economic conditions weakened during the quarter, resulting in reduced demand from customers in a number of regions around the world. Contributing to the weakness was a reduction in the availability of credit in many worldwide markets, which is expected to have a continuing negative effect on future consumer and business spending. Markets in the United States that are related to residential housing, automobiles and automotive parts, and appliances are expected to remain weak until there is a general increase in economic activity and consumer demand. Markets outside the United States have been stronger in recent quarters, but international markets, particularly in continental Europe, weakened during the third quarter and are expected to exhibit weak customer demand in the coming quarter, although some of this reduced demand is expected to be offset by higher sales in North Africa, the Middle East and Eastern Europe. Demand for our electronic materials used in solar cells is strong and is expected to continue to show year-over-year growth, although rapid expansion of capacity among solar cell manufacturers could lead to some increased demand volatility due to short-term supply chain imbalances in the future.

We expect to continue to record charges associated with our current and future restructuring programs, particularly related to our rationalization of our manufacturing operations in Europe.

Factors that could adversely affect our future financial performance are described under the heading Risk Factors in Item 1A of Part II of this Quarterly Report on Form 10-Q for the quarter ended September 30, 2008.

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Results of Operations

Comparison of the three months ended September 30, 2008 and 2007

	Three months ended September 30, 2008	Three months ended September 30, 2007	$ Change	% Change
	(Dollars in thousands, except per share amounts)			
Net sales	$ 608,588	$ 550,701	$ 57,887	10.5%
Cost of sales	494,577	450,553	44,024	9.8%
Gross profit	114,011	100,148	13,863	13.8%
Gross profit percentage	18.7%	18.2%		
Selling, general and administrative expenses	78,274	71,069	7,205	10.1%
Restructuring charges	9,042	5,826	3,216	55.2%
Other expense (income):				
Interest expense	12,497	14,488	(1,991)	(13.7%)
Interest earned	(213)	(271)	58	(21.4%)
Loss on extinguishment of debt	5,531		5,531	
Foreign currency losses (gains), net	1,660	(10)	1,670	(16,700.0%)
Miscellaneous expense (income), net	727	(13)	740	(5,692.3%)
Income before taxes	6,493	9,059	(2,566)	(28.3%)
Income tax expense	1,605	3,472	(1,867)	(53.8%)
Income from continuing operations	4,888	5,587	(699)	(12.5%)
Loss from discontinued operations, net of tax	57	2	55	2,750.0%
Net income	$ 4,831	$ 5,585	$ (754)	(13.5%)
Diluted earnings per share	$ 0.11	$ 0.12	$ (0.01)	(8.3%)

Sales for the quarter ended September 30, 2008, increased by 10.5%, driven by increased product prices, including pass-throughs for higher precious metal costs, improved product mix, and favorable changes in foreign currency exchange rates. Aggregated sales volume had a slightly negative effect on sales for the quarter, as a result of lower volume in Specialty Plastics, Polymer Additives and Color and Glass Performance Materials, partially offset by increased sales volume in Electronic Materials.

Gross profit increased in the 2008 third quarter primarily as a result of increased product pricing and lower manufacturing costs, partially offset by higher raw material costs. Gross profit was reduced by $1.5 million in the quarter as a result of costs related to manufacturing rationalization activities and asset write-offs. Charges for manufacturing rationalization activities were $0.5 million in the third quarter of 2007. Gross profit as a percent of sales was negatively impacted by higher raw materials costs, including precious metal costs. Precious metal costs are generally passed through to customers with minimal gross profit contributions.

Selling, general and administrative (SG&A) expenses were 12.9% of net sales in the 2008 third quarter, unchanged from the third quarter of 2007. SG&A spending in the third quarter increased, in dollar terms, primarily due to changes in foreign currency exchange rates, increased benefit expenses and higher incentive compensation accruals. The 2008 third-quarter SG&A expense also included charges of $1.9 million primarily related to corporate development activities, partially offset by a favorable insurance settlement.

Restructuring charges were $9.0 million in the 2008 third quarter, an increase from $5.8 million in the third quarter of 2007. The 2008 third quarter charges were primarily related to our manufacturing rationalization activities in Europe related to our Performance Coatings and Color and Glass Performance Materials segments.

Interest expense declined in the 2008 third quarter as a result of lower average interest rates, partially offset by higher borrowing levels.

During the 2008 third quarter, we refinanced our 9 1/8% coupon senior notes using the proceeds of a new convertible bond issue and additional borrowing from our revolving credit facility. In connection with the repayment of the previous senior notes, we recorded a loss on extinguishment of debt of $5.5 million during the quarter. This loss consists of costs that would have been reported as interest expense during the remaining life of the previous senior notes had we not extinguished the debt early.

Income tax expense for the three months ending September 30, 2008, was $1.6 million, or 24.7% of pre-tax income, compared to $3.5 million, or 38.5% of pre-tax income, in the third quarter of 2007. The reasons for the decrease in the effective tax rate were a change in the mix of income by country and a decrease in the U.S. tax cost on foreign dividends.

There were no new businesses included in discontinued operations in the third quarter of 2008.

	Three months ended September 30, 2008	2007	$ Change	% Change
	(Dollars in thousands)			
Segment Sales				
Performance Coatings	$ 162,523	$ 153,742	$ 8,781	5.7%
Electronic Materials	155,122	116,645	38,477	33.0%
Color & Glass Performance Materials	115,013	113,575	1,438	1.3%
Polymer Additives	93,081	85,230	7,851	9.2%
Specialty Plastics	58,097	62,236	(4,139)	(6.7%)
Other Businesses	24,752	19,273	5,479	28.4%
Total segment sales	$ 608,588	$ 550,701	$ 57,887	10.5%
Segment Operating Income				
Performance Coatings	$ 12,135	$ 8,449	$ 3,686	43.6%
Electronic Materials	17,095	8,522	8,573	100.6%
Color & Glass Performance Materials	9,712	11,727	(2,015)	(17.2%)
Polymer Additives	4,385	3,417	968	28.3%
Specialty Plastics	2,796	3,586	(790)	(22.0%)
Other Businesses	2,645	593	2,052	346.0%
Total segment operating income	$ 48,768	$ 36,294	$ 12,474	34.4%

Performance Coatings Segment Results. Sales increased in Performance Coatings primarily due to higher sales of tile coatings. The sales increase was driven by favorable changes in foreign exchange rates and higher sales volume of tile coatings, partially offset by lower sales volume of porcelain enamel products. Sales increased in Europe, Asia and Latin America, and declined in the United States. Operating income increased as a result of a combination of improved product pricing, manufacturing cost improvements, lower SG&A expense and increased sales volume, partially offset by higher raw material costs.

Electronic Materials Segment Results. Sales increased in Electronic Materials, driven by continued strong demand for metal pastes and powders, particularly those products used to manufacture solar cells. The higher sales were driven by higher product pricing, including increased precious metal costs which generally are passed through to our customers with minimal gross profit contribution. Sales grew as a result of sharply higher shipments from our manufacturing facilities in the United States, although much of this product volume is used by customers in other regions. Operating income increased as a result of the positive effects of increased sales of higher-margin products, and benefits from manufacturing productivity improvements, partially offset by higher SG&A expense.

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Color and Glass Performance Materials Segment Results. Sales increased in Color and Glass Performance Materials as the effects of favorable foreign currency exchange rates and improved product pricing more than offset lower sales volume. Demand from customers in Europe declined during the quarter, although sales for the full quarter were slightly higher compared to the third quarter of 2007. Operating income declined as a result of lower sales volume, higher manufacturing costs, an increased bad debt reserve, and higher raw material costs, partially offset by lower SG&A expense.

Polymer Additives Segment Results. Sales increased in Polymer Additives as a result of improved product pricing and product mix, as well as favorable changes in foreign currency exchange rates. Sales increased in Europe and the United States, the segment s two primary sales regions. Operating income increased primarily as a result of higher product pricing and improved product mix, partially offset increased raw material costs.

Specialty Plastics Segment Results. Sales declined in Specialty Plastics as a result of continued weak customer demand in the United States and Europe. The weak demand resulted in lower sales volume, which was partially offset by higher product pricing. Operating income declined from the prior-year period as a result of lower manufacturing volume and higher raw material costs, partially offset by increased product pricing. Lower manufacturing costs and SG&A expenses, achieved through reduction in employee positions, also contributed positively to operating income.

Other Businesses Segment Results. Sales increased in Other Businesses as a result of higher sales volume of fine chemical and pharmaceutical products. Operating income increased as a result of the higher sales volume and improved product mix.

	Three months ended September 30, 2008	Three months ended September 30, 2007	$ Change	% Change
	(Dollars in thousands)			
Geographic Revenues				
United States	$ 281,502	$ 232,405	$ 49,097	21.1%
International	327,086	318,296	8,790	2.8%
Total	$ 608,588	$ 550,701	$ 57,887	10.5%

Sales increased in the United States, Europe and Latin America during the three months ended September 30, 2008, compared with the prior-year period. Sales in Asia were little changed from the third quarter of 2007. In the United States, the sales increase was driven by Electronic Materials products, with additional contributions from increased sales in Polymer Additives. U.S. sales declined in Specialty Plastics. International sales increased primarily as a result of higher European sales of Polymer Additives and increased Performance Coatings products sales in all international regions.

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Comparison of the nine months ended September 30, 2008 and 2007

	Nine months ended September 30, 2008	2007	$ Change	% Change
	(Dollars in thousands, except per share amounts)			
Net sales	$ 1,866,240	$ 1,634,064	$ 232,176	14.2%
Cost of sales	1,515,526	1,319,609	195,917	14.8%
Gross profit	350,714	314,455	36,259	11.5%
Gross profit percentage	18.8%	19.2%		
Selling, general and administrative expenses	238,122	234,212	3,910	1.7%
Restructuring charges	22,280	7,689	14,591	189.8%
Other expense (income):				
Interest expense	39,740	46,220	(6,480)	(14.0%)
Interest earned	(484)	(1,425)	941	(66.0%)
Loss on extinguishment of debt	5,531		5,531	
Foreign currency losses, net	769	924	(155)	(16.8%)
Miscellaneous expense (income), net	4,659	(399)	5,058	(1,267.7%)
Income before taxes	40,097	27,234	12,863	47.2%
Income tax expense	16,688	10,814	5,874	54.3%
Income from continuing operations	23,409	16,420	6,989	42.6%
Loss from discontinued operations, net of tax	73	216	(143)	(66.2%)
Net income	$ 23,336	$ 16,204	$ 7,132	44.0%
Diluted earnings per share	$ 0.52	$ 0.36	$ 0.16	44.4%

Net sales increased by 14.2% in the nine months ended September 30, 2008, compared with the same period in 2007. The sales increase was driven by higher sales in the Electronic Materials, Performance Coatings, Color and Glass Performance Materials, Polymer Additives and Other Businesses segments. Sales in our Specialty Plastics segment declined. The sales growth primarily was the result of higher product prices, including pass-through of higher precious metal costs, improved product mix, and favorable changes in foreign currency exchange rates. Sales increased in all regions, compared with the first nine months of 2007.

Gross profit increased in the first three quarters of 2008 compared with the first three quarters of 2007, primarily as a result of increased product prices and higher sales, partially offset by higher raw material costs. Gross profit during the first nine months of 2008 was negatively impacted by $3.0 million in charges related to asset write-offs and manufacturing rationalization activities. Gross profit was also reduced by costs of approximately $3.3 million to clean up an accidental discharge of product into the wastewater treatment facility at our Bridgeport, New Jersey, manufacturing location. Gross profit, as a percentage of net sales, was negatively impacted by higher raw material costs, including costs of precious metals. Precious metal costs generally are passed through to customers with minimal gross profit contribution. Gross profit was reduced by $4.7 million in the first nine months of 2007, primarily as a result of accelerated depreciation charges related to our manufacturing rationalization activities. Also, gross profit in the first three quarters of 2007 was reduced by the costs of a temporary interruption of production at our manufacturing site in South Plainfield, New Jersey, and costs that were required to address quality issues at our

Evansville, Indiana, manufacturing facility.

Selling, general and administrative (SG&A) expenses declined to 12.8% of net sales in the first nine months of 2008 compared with 14.3% of sales in the prior-year period. SG&A expenses for the first nine months of 2008 included charges of $3.8 million primarily related to corporate development activities, asset write-offs and employee severance expenses, partially offset by benefits from litigation settlements and insurance proceeds. SG&A expense in the first nine months of 2007 included charges of $8.4 million, primarily related to reserves for litigation settlements and corporate development activities.

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Restructuring charges increased to $22.3 million in the first nine months of 2008 compared with $7.7 million in the first nine months of 2007. The 2008 restructuring charges are primarily related to manufacturing rationalization activities in our Performance Coatings and Color and Glass Performance Materials manufacturing operations in Europe and Brazil, and additional restructuring activities in our Performance Coatings, Color and Glass Performance Materials, Polymer Additives, and Specialty Plastics segments that were initiated in 2007 and the first nine months of 2008.

Interest expense declined during the first nine months of 2008 compared with the prior-year period. In the first nine months of 2007, we recorded a non-recurring $2.0 million write-off of unamortized fees associated with an unused portion of our term loan arrangements. In the first nine months of 2008, our interest expense also declined because our average interest rates on borrowings were lower than in the same period during 2007. The benefit was partially offset by higher borrowing levels.

During the 2008 third quarter, we refinanced our 9 1/8% coupon senior notes using the proceeds of a new convertible bond issue and additional borrowing from our revolving credit facility. In connection with the repayment of the previous senior notes, we recorded a loss on extinguishment of debt of $5.5 million during the quarter. This loss consists of costs that would have been reported as interest expense during the remaining life of the previous senior notes had we not extinguished the debt early.

Miscellaneous expense was $4.7 million in the first nine months of 2008 compared with miscellaneous income of $0.4 million in the first nine months of 2007. The primary drivers of the change were an increased provision for an environmental contingency in Latin America related to a previously closed manufacturing site, a loss on forward contracts in the current period compared to a gain in the prior-year period, and lower gains on the disposal of assets.

Income tax expense for the first nine months of 2008 was $16.7 million, or 41.6% of pre-tax income. Income tax expense for the first nine months of 2007 was $10.8 million, or 39.7% of pre-tax income. The reasons for the increase in the effective tax rate were a change in the mix of income by country and a decrease in the U.S. tax cost on foreign dividends. The effective tax rate was also impacted by an unfavorable tax court decision in Brazil, an increase in the valuation allowance, and favorable adjustments to prior-year accruals which, in aggregate, totaled $2.4 million.

There were no new businesses included in discontinued operations in the first nine months of 2008.

	Nine months ended September 30, 2008	2007	$ Change	% Change
	(Dollars in thousands)			
Segment Sales				
Performance Coatings	$ 501,819	$ 451,058	$ 50,761	11.3%
Electronic Materials	452,317	338,412	113,905	33.7%
Color & Glass Performance Materials	374,083	329,195	44,888	13.6%
Polymer Additives	284,107	252,903	31,204	12.3%
Specialty Plastics	183,499	198,994	(15,495)	(7.8%)
Other Businesses	70,415	63,502	6,913	10.9%
Total segment sales	$ 1,866,240	$ 1,634,064	$ 232,176	14.2%
Segment Operating Income				
Performance Coatings	$ 34,400	$ 29,947	$ 4,453	14.9%
Electronic Materials	43,527	19,534	23,993	122.8%
Color & Glass Performance Materials	40,695	39,462	1,233	3.1%
Polymer Additives	11,703	10,576	1,127	10.7%
Specialty Plastics	7,520	10,961	(3,441)	(31.4%)
Other Businesses	7,405	7,982	(577)	(7.2%)
Total segment operating income	$ 145,250	$ 118,462	$ 26,788	22.6%

Performance Coatings Segment Results. Sales increased in Performance Coatings primarily as a result of increased sales of tile coating products. Sales increased in Europe, Asia and Latin America while sales in the United States declined. The primary drivers of the sales growth were favorable changes in foreign currency exchange rates and increased sales volume of tile coatings products. Operating income increased in the first nine months of 2008 due to higher product prices, volume increases and SG&A reductions, partially offset by raw material cost increases.

Electronic Materials Segment Results. Sales increased in Electronic Materials as a result of increased sales of metal pastes and powders, particularly sales to manufacturers of solar cells. Sales grew as a result of increased product pricing, including higher product prices resulting from the pass-through to customers of higher precious metal costs. Sales also increased as a result of increased sales volume and favorable changes in foreign currency exchange rates. Sales increased from U.S.-based manufacturing operations. Products from our U.S. facilities often are used by our customers in other regions, particularly in Asia. Operating income increased as a result of the positive effects of increased sales of higher-margin products, lower manufacturing costs and benefits from prior-period restructuring activities. Also, during the first nine months of 2007, operating income was reduced by costs associated with a temporary interruption of manufacturing activities at our manufacturing site in South Plainfield, New Jersey.

Color and Glass Performance Materials Segment Results. Sales increased in Color and Glass Performance Materials as a result of growth in sales of glass coatings and performance pigment materials. The higher sales were primarily the result of favorable changes in foreign currency exchange rates and higher product prices. Sales increased in all regions, led by growth in Europe. Operating income improved primarily as a result of improved product pricing and favorable changes in foreign currency exchange rates, partially offset by higher raw material costs.

Polymer Additives Segment Results. Sales increased in Polymer Additives as a result of higher product pricing and favorable changes in foreign exchange rates, partially offset by the effects of lower sales volume. Sales increased in Europe and the United States. During the first nine months of 2008 operating income increased slightly, driven by improved product pricing that was largely offset by higher raw material costs and the negative effects of lower sales volume. Also during the first nine months of 2008 operating income was negatively impacted by $3.3 million in additional manufacturing costs resulting from the clean-up of an accidental discharge of product into the wastewater treatment facility at our Bridgeport, New Jersey, manufacturing location.

Specialty Plastics Segment Results. Sales declined in Specialty Plastics primarily due to continuing weak demand from U.S.-based customers, particularly in the automotive parts and appliance industries. As a result of the weak demand, sales volume declined, more than offsetting the positive effects of increased product pricing and favorable changes in foreign currency exchange rates. Operating income declined as a result of higher raw material costs and lower manufacturing volumes, partially offset by increased product pricing. Cost reduction activities in manufacturing and SG&A expense helped to moderate the decline in operating income.
Other Businesses Segment Results. Sales increased in Other Businesses as a result of increased sales of fine chemical products. Sales of pharmaceutical products in the first nine months of 2008 were lower than the prior-year period. Sales volume of certain of our pharmaceutical products can vary significantly from period to period as a result of our customers intermittent production of some low-volume products which use our materials. Operating income declined as a result of a less favorable product mix.

	Nine months ended September 30, 2008	2007	$ Change	% Change
	(Dollars in thousands)			
Geographic Revenues				
United States	$ 811,678	$ 710,423	$ 101,255	14.3%
International	1,054,562	923,641	130,921	14.2%
Total	$ 1,866,240	$ 1,634,064	$ 232,176	14.2%

Sales increased in all regions during the first nine months of 2008 compared with the prior-year period. In the United States, sales growth was led by increased sales in Electronic Materials, with additional contributions from Polymer Additives and Color and Glass Performance Materials. U.S. sales declined in Specialty Plastics and Performance Coatings. Sales increased in Europe, Asia and Latin America. The international sales growth was led by increased sales of Performance Coatings, Color and Glass Performance Materials, Electronic Materials and Polymer Additives.
Summary of Cash Flows for the nine months ended September 30, 2008 and 2007

	Nine months ended September 30, 2008	2007	$ Change	% Change
	(Dollars in thousands)			
Net cash provided by operating activities	$ 1,838	$ 121,281	$ (119,443)	(98.5%)
Net cash used for investing activities	(54,283)	(39,992)	(14,291)	35.7%
Net cash provided by (used for) financing activities	55,359	(73,302)	128,661	(175.5%)
Effect of exchange rate changes on cash and cash equivalents	(415)	849	(1,264)	(148.9%)
Increase in cash and cash equivalents	$ 2,499	$ 8,836	$ (6,337)	(71.7%)

Cash flows from operating activities decreased by $119.4 million in the first nine months of 2008 compared with the same period of 2007. In the first nine months of 2007, we received $70.1 million of deposits held by financial institutions under our precious metals consignment program. Deposit requirements were eliminated during 2007. Cash used for inventories and accounts and trade notes receivable, net of accounts payable, increased $80.1 million, primarily due to increases in raw material prices which are largely passed through to our customers.
Cash used for investing activities increased by $14.3 million, primarily due to higher capital expenditures of $8.6 million, expenditures for other, primarily intangible, assets of $3.4 million to expand a product line, and lower

proceeds from sales of assets and businesses of $2.1 million.

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Cash flows from financing activities increased by $128.7 million. Changes in borrowing activity resulted in an increase of $140.8 million. In the first nine months of 2008, we borrowed $84.1 million, while in the same period of 2007, we used cash to reduce our debt by $56.7 million. The first nine months of 2007 also included $9.2 million in proceeds to the Company from the exercise of stock options.

Capital Resources and Liquidity

Credit Rating

At September 30, 2008, the Company s corporate credit rating was B1, with a positive outlook, by Moody s Investor Services, Inc. and B+, with a stable outlook, by Standard & Poor s Rating Group.

6.50% Convertible Senior Notes

In August 2008, Ferro issued $172.5 million of 6.50% Convertible Senior Notes due 2013 (the Convertible Notes). The proceeds from the offering, along with available cash, including borrowings under Ferro s revolving credit facility, were used to purchase all of Ferro s outstanding 9 1/8% Senior Notes. The Convertible Notes bear interest at a rate of 6.5% per year, payable semi-annually in arrears on February 15 and August 15 of each year, beginning on February 15, 2009. The Convertible Notes mature on August 15, 2013. At September 30, 2008, we were in compliance with the covenants under the Convertible Notes indentures.

9 1/8% Senior Notes

In June 2008, Ferro commenced a cash tender offer to purchase any and all of its outstanding $200 million aggregate principal amount of 9 1/8% Senior Notes due 2009 (the 9 1/8% Notes). In August and September, we purchased all of the 9 1/8% Notes for $205.3 million, including call premiums and tender costs, and recorded a loss of $5.5 million, including unamortized discounts and fees. We financed the purchase of the 9 1/8% Notes and related costs from the issuance of the Convertible Notes, along with available cash, including borrowings under Ferro s revolving credit facility.

Revolving Credit and Term Loan Facility

In 2006, we e