

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended February 28, 2021

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 000-22496



SCHNITZER STEEL INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

OREGON

(State or other jurisdiction of incorporation or organization)

93-0341923

(I.R.S. Employer Identification No.)

299 SW Clay Street, Suite 350, Portland, Oregon

(Address of principal executive offices)

97201

(Zip Code)

(503) 224-9900

(Registrant's telephone number, including area code)

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

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Class A Common Stock, \$1.00 par value	SCHN	NASDAQ Global Select Market

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 every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

The registrant had 27,264,633 shares of Class A common stock, par value of \$1.00 per share, and 200,000 shares of Class B common stock, par value of \$1.00 per share, outstanding as of April 5, 2021.

SCHNITZER STEEL INDUSTRIES, INC.
FORM 10-Q
TABLE OF CONTENTS

	<u>PAGE</u>
FORWARD-LOOKING STATEMENTS	3
PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements (Unaudited)	
Unaudited Condensed Consolidated Balance Sheets as of February 28, 2021 and August 31, 2020	4
Unaudited Condensed Consolidated Statements of Operations for the Three and Six Months Ended February 28, 2021 and February 29, 2020	5
Unaudited Condensed Consolidated Statements of Comprehensive Income (Loss) for the Three and Six Months Ended February 28, 2021 and February 29, 2020	6
Unaudited Condensed Consolidated Statements of Equity for the Three and Six Months Ended February 28, 2021 and February 29, 2020	7
Unaudited Condensed Consolidated Statements of Cash Flows for the Six Months Ended February 28, 2021 and February 29, 2020	9
Notes to the Unaudited Condensed Consolidated Financial Statements	11
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations	23
Item 3. Quantitative and Qualitative Disclosures about Market Risk	34
Item 4. Controls and Procedures	35
PART II. OTHER INFORMATION	
Item 1. Legal Proceedings	36
Item 1A. Risk Factors	37
Item 5. Other Information	37
Item 6. Exhibits	38
SIGNATURES	39

FORWARD-LOOKING STATEMENTS

Statements and information included in this Quarterly Report on Form 10-Q by Schnitzer Steel Industries, Inc. that are not purely historical are forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934 and are made pursuant to the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995. Except as noted herein or as the context may otherwise require, all references to “we,” “our,” “us,” “the Company” and “SSI” refer to Schnitzer Steel Industries, Inc. and its consolidated subsidiaries.

Forward-looking statements in this Quarterly Report on Form 10-Q include statements regarding future events or our expectations, intentions, beliefs and strategies regarding the future, which may include statements regarding the impact of pandemics, epidemics or other public health emergencies, such as the coronavirus disease 2019 (“COVID-19”) pandemic; the Company’s outlook, growth initiatives or expected results or objectives, including pricing, margins, sales volumes and profitability; liquidity positions; our ability to generate cash from continuing operations; trends, cyclicalities and changes in the markets we sell into; strategic direction or goals; targets; changes to manufacturing and production processes; the realization of deferred tax assets; planned capital expenditures; the cost of and the status of any agreements or actions related to our compliance with environmental and other laws; expected tax rates, deductions and credits; the impact of sanctions and tariffs, quotas and other trade actions and import restrictions; the potential impact of adopting new accounting pronouncements; obligations under our retirement plans; benefits, savings or additional costs from business realignment, cost containment and productivity improvement programs; and the adequacy of accruals.

Forward-looking statements by their nature address matters that are, to different degrees, uncertain, and often contain words such as “outlook,” “target,” “aim,” “believes,” “expects,” “anticipates,” “intends,” “assumes,” “estimates,” “evaluates,” “may,” “will,” “should,” “could,” “opinions,” “forecasts,” “projects,” “plans,” “future,” “forward,” “potential,” “probable,” and similar expressions. However, the absence of these words or similar expressions does not mean that a statement is not forward-looking.

We may make other forward-looking statements from time to time, including in reports filed with the Securities and Exchange Commission, press releases, presentations and on public conference calls. All forward-looking statements we make are based on information available to us at the time the statements are made, and we assume no obligation to update any forward-looking statements, except as may be required by law. Our business is subject to the effects of changes in domestic and global economic conditions and a number of other risks and uncertainties that could cause actual results to differ materially from those included in, or implied by, such forward-looking statements. Some of these risks and uncertainties are discussed in “Item 1A. Risk Factors” of Part I of our most recent Annual Report on Form 10-K, as supplemented by our subsequently filed Quarterly Reports on Form 10-Q. Examples of these risks include: the impact of pandemics, epidemics or other public health emergencies, such as the COVID-19 pandemic; potential environmental cleanup costs related to the Portland Harbor Superfund site or other locations; the cyclicalities and impact of general economic conditions; changing conditions in global markets including the impact of sanctions and tariffs, quotas and other trade actions and import restrictions; volatile supply and demand conditions affecting prices and volumes in the markets for raw materials and other inputs we purchase; significant decreases in scrap metal prices; imbalances in supply and demand conditions in the global steel industry; reliance on third party shipping companies, including with respect to freight rates and the availability of transportation; inability to obtain or renew business licenses and permits; the impact of goodwill impairment charges; the impact of long-lived asset and equity investment impairment charges; failure to realize or delays in realizing expected benefits from investments in processing and manufacturing technology improvements; inability to achieve or sustain the benefits from productivity, cost savings and restructuring initiatives; inability to renew facility leases; difficulties associated with acquisitions and integration of acquired businesses; customer fulfillment of their contractual obligations; increases in the relative value of the U.S. dollar; the impact of foreign currency fluctuations; potential limitations on our ability to access capital resources and existing credit facilities; restrictions on our business and financial covenants under the agreement governing our bank credit facilities; the impact of consolidation in the steel industry; the impact of equipment upgrades, equipment failures and facility damage on production; product liability claims; the impact of legal proceedings and legal compliance; the adverse impact of climate change; the impact of not realizing deferred tax assets; the impact of tax increases and changes in tax rules; the impact of property tax increases or property tax rate changes; the impact of one or more cybersecurity incidents; environmental compliance costs and potential environmental liabilities; compliance with climate change and greenhouse gas emission laws and regulations; reliance on employees subject to collective bargaining agreements; and the impact of the underfunded status of multiemployer plans in which we participate.

PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

SCHNITZER STEEL INDUSTRIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited, in thousands, except per share amounts)
(Currency - U.S. Dollar)

	February 28, 2021	August 31, 2020
Assets		
Current assets:		
Cash and cash equivalents	\$ 11,326	\$ 17,887
Accounts receivable, net of allowance for credit losses of \$1,633 and \$1,593	210,480	139,147
Inventories	252,268	157,269
Refundable income taxes	6,538	18,253
Prepaid expenses and other current assets	34,621	30,075
Total current assets	515,233	362,631
Property, plant and equipment, net of accumulated depreciation of \$835,799 and \$811,623	502,484	487,004
Operating lease right-of-use assets	136,278	140,584
Investments in joint ventures	10,382	10,057
Goodwill	170,100	169,627
Intangibles, net of accumulated amortization of \$3,543 and \$3,528	4,283	4,585
Deferred income taxes	26,201	27,152
Other assets	40,368	28,287
Total assets	<u>\$ 1,405,329</u>	<u>\$ 1,229,927</u>
Liabilities and Equity		
Current liabilities:		
Short-term borrowings	\$ 2,372	\$ 2,184
Accounts payable	142,717	106,676
Accrued payroll and related liabilities	41,203	41,436
Environmental liabilities	12,975	6,302
Operating lease liabilities	20,279	19,760
Other accrued liabilities	44,936	47,306
Total current liabilities	264,482	223,664
Deferred income taxes	42,175	38,292
Long-term debt, net of current maturities	168,441	102,235
Environmental liabilities, net of current portion	53,965	47,162
Operating lease liabilities, net of current maturities	119,751	125,001
Other long-term liabilities	22,476	13,137
Total liabilities	671,290	549,491
Commitments and contingencies (Note 4)		
Schnitzer Steel Industries, Inc. ("SSI") shareholders' equity:		
Preferred stock – 20,000 shares \$1.00 par value authorized, none issued	—	—
Class A common stock – 75,000 shares \$1.00 par value authorized, 27,263 and 26,899 shares issued and outstanding	27,263	26,899
Class B common stock – 25,000 shares \$1.00 par value authorized, 200 and 200 shares issued and outstanding	200	200
Additional paid-in capital	39,695	36,616
Retained earnings	697,966	649,863
Accumulated other comprehensive loss	(35,282)	(36,871)
Total SSI shareholders' equity	729,842	676,707
Noncontrolling interests	4,197	3,729
Total equity	734,039	680,436
Total liabilities and equity	<u>\$ 1,405,329</u>	<u>\$ 1,229,927</u>

The accompanying Notes to the Unaudited Condensed Consolidated Financial Statements are an integral part of these statements.

SCHNITZER STEEL INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited, in thousands, except per share amounts)
(Currency - U.S. Dollar)

	Three Months Ended		Six Months Ended	
	February 28, 2021	February 29, 2020	February 28, 2021	February 29, 2020
Revenues	\$ 600,111	\$ 439,482	\$ 1,092,218	\$ 845,066
Operating expense:				
Cost of goods sold	487,025	380,520	907,119	745,280
Selling, general and administrative	54,142	46,426	104,048	93,200
(Income) from joint ventures	(454)	(190)	(1,181)	(389)
Asset impairment charges	—	402	—	2,094
Restructuring charges and other exit-related activities	814	4,633	878	5,100
Operating income (loss)	58,584	7,691	81,354	(219)
Interest expense	(1,224)	(1,320)	(3,004)	(2,743)
Other (loss) income, net	(242)	(98)	(407)	108
Income (loss) from continuing operations before income taxes	57,118	6,273	77,943	(2,854)
Income tax (expense) benefit	(11,469)	(1,770)	(17,188)	764
Income (loss) from continuing operations	45,649	4,503	60,755	(2,090)
Income (loss) from discontinued operations, net of tax	30	1	(12)	29
Net income (loss)	45,679	4,504	60,743	(2,061)
Net income attributable to noncontrolling interests	(1,091)	(621)	(2,051)	(1,051)
Net income (loss) attributable to SSI shareholders	<u>\$ 44,588</u>	<u>\$ 3,883</u>	<u>\$ 58,692</u>	<u>\$ (3,112)</u>
Net income (loss) per share attributable to SSI shareholders:				
Basic:				
Income (loss) per share from continuing operations	\$ 1.59	\$ 0.14	\$ 2.10	\$ (0.11)
Net income (loss) per share	\$ 1.59	\$ 0.14	\$ 2.10	\$ (0.11)
Diluted:				
Income (loss) per share from continuing operations	\$ 1.54	\$ 0.14	\$ 2.05	\$ (0.11)
Net income (loss) per share	\$ 1.54	\$ 0.14	\$ 2.05	\$ (0.11)
Weighted average number of common shares:				
Basic	27,991	27,721	27,899	27,618
Diluted	28,862	28,139	28,673	27,618

The accompanying Notes to the Unaudited Condensed Consolidated Financial Statements are an integral part of these statements.

SCHNITZER STEEL INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited, in thousands)
(Currency - U.S. Dollar)

	Three Months Ended		Six Months Ended	
	February 28, 2021	February 29, 2020	February 28, 2021	February 29, 2020
Net income (loss)	\$ 45,679	\$ 4,504	\$ 60,743	\$ (2,061)
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments	1,572	(630)	1,811	(419)
Pension obligations, net	38	115	(222)	142
Total other comprehensive income (loss), net of tax	1,610	(515)	1,589	(277)
Comprehensive income (loss)	47,289	3,989	62,332	(2,338)
Less comprehensive income attributable to noncontrolling interests	(1,091)	(621)	(2,051)	(1,051)
Comprehensive income (loss) attributable to SSI shareholders	<u>\$ 46,198</u>	<u>\$ 3,368</u>	<u>\$ 60,281</u>	<u>\$ (3,389)</u>

The accompanying Notes to the Unaudited Condensed Consolidated Financial Statements are an integral part of these statements.

SCHNITZER STEEL INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(Unaudited, in thousands, except per share amounts)
(Currency - U.S. Dollar)

	Common Stock				Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total SSI Shareholders' Equity	Noncontrolling Interests	Total Equity
	Class A		Class B							
	Shares	Amount	Shares	Amount						
Three Months Ended February 29, 2020										
Balance as of December 1, 2019	26,943	\$ 26,943	200	\$ 200	\$ 29,528	\$ 662,707	\$ (38,525)	\$ 680,853	\$ 4,183	\$ 685,036
Net income	—	—	—	—	—	3,883	—	3,883	621	4,504
Other comprehensive loss, net of tax	—	—	—	—	—	—	(515)	(515)	—	(515)
Distributions to noncontrolling interests	—	—	—	—	—	—	—	—	(507)	(507)
Share repurchases	(53)	(53)	—	—	(861)	—	—	(914)	—	(914)
Issuance of restricted stock	9	9	—	—	(9)	—	—	—	—	—
Share-based compensation cost	—	—	—	—	2,516	—	—	2,516	—	2,516
Dividends (\$0.1875 per common share)	—	—	—	—	—	(5,172)	—	(5,172)	—	(5,172)
Balance as of February 29, 2020	<u>26,899</u>	<u>\$ 26,899</u>	<u>200</u>	<u>\$ 200</u>	<u>\$ 31,174</u>	<u>\$ 661,418</u>	<u>\$ (39,040)</u>	<u>\$ 680,651</u>	<u>\$ 4,297</u>	<u>\$ 684,948</u>

	Common Stock				Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total SSI Shareholders' Equity	Noncontrolling Interests	Total Equity
	Class A		Class B							
	Shares	Amount	Shares	Amount						
Three Months Ended February 28, 2021										
Balance as of December 1, 2020	27,254	\$ 27,254	200	\$ 200	\$ 35,310	\$ 658,710	\$ (36,892)	\$ 684,582	\$ 3,966	\$ 688,548
Net income	—	—	—	—	—	44,588	—	44,588	1,091	45,679
Other comprehensive income, net of tax	—	—	—	—	—	—	1,610	1,610	—	1,610
Distributions to noncontrolling interests	—	—	—	—	—	—	—	—	(860)	(860)
Issuance of restricted stock	10	10	—	—	(10)	—	—	—	—	—
Restricted stock withheld for taxes	(1)	(1)	—	—	—	—	—	(1)	—	(1)
Share-based compensation cost	—	—	—	—	4,395	—	—	4,395	—	4,395
Dividends (\$0.1875 per common share)	—	—	—	—	—	(5,332)	—	(5,332)	—	(5,332)
Balance as of February 28, 2021	<u>27,263</u>	<u>\$ 27,263</u>	<u>200</u>	<u>\$ 200</u>	<u>\$ 39,695</u>	<u>\$ 697,966</u>	<u>\$ (35,282)</u>	<u>\$ 729,842</u>	<u>\$ 4,197</u>	<u>\$ 734,039</u>

The accompanying Notes to the Unaudited Condensed Consolidated Financial Statements are an integral part of these statements.

SCHNITZER STEEL INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF EQUITY
(Unaudited, in thousands, except per share amounts)
(Currency - U.S. Dollar)

	Common Stock				Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total SSI Shareholders' Equity	Noncontrolling Interests	Total Equity
	Class A		Class B							
	Shares	Amount	Shares	Amount						
Six Months Ended February 29, 2020										
Balance as of August 31, 2019	26,464	\$ 26,464	200	\$ 200	\$ 33,700	\$ 675,363	\$ (38,763)	\$ 696,964	\$ 4,332	\$ 701,296
Cumulative effect on adoption of new accounting guidance for leases, net of tax	—	—	—	—	—	(463)	—	(463)	—	(463)
Balance as of September 1, 2019	26,464	26,464	200	200	33,700	674,900	(38,763)	696,501	4,332	700,833
Net (loss) income	—	—	—	—	—	(3,112)	—	(3,112)	1,051	(2,061)
Other comprehensive loss, net of tax	—	—	—	—	—	—	(277)	(277)	—	(277)
Distributions to noncontrolling interests	—	—	—	—	—	—	—	—	(1,086)	(1,086)
Share repurchases	(53)	(53)	—	—	(861)	—	—	(914)	—	(914)
Issuance of restricted stock	762	762	—	—	(762)	—	—	—	—	—
Restricted stock withheld for taxes	(274)	(274)	—	—	(5,571)	—	—	(5,845)	—	(5,845)
Share-based compensation cost	—	—	—	—	4,668	—	—	4,668	—	4,668
Dividends (\$0.375 per common share)	—	—	—	—	—	(10,370)	—	(10,370)	—	(10,370)
Balance as of February 29, 2020	<u>26,899</u>	<u>\$ 26,899</u>	<u>200</u>	<u>\$ 200</u>	<u>\$ 31,174</u>	<u>\$ 661,418</u>	<u>\$ (39,040)</u>	<u>\$ 680,651</u>	<u>\$ 4,297</u>	<u>\$ 684,948</u>

	Common Stock				Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total SSI Shareholders' Equity	Noncontrolling Interests	Total Equity
	Class A		Class B							
	Shares	Amount	Shares	Amount						
Six Months Ended February 28, 2021										
Balance as of September 1, 2020	26,899	\$ 26,899	200	\$ 200	\$ 36,616	\$ 649,863	\$ (36,871)	\$ 676,707	\$ 3,729	\$ 680,436
Net income	—	—	—	—	—	58,692	—	58,692	2,051	60,743
Other comprehensive income, net of tax	—	—	—	—	—	—	1,589	1,589	—	1,589
Distributions to noncontrolling interests	—	—	—	—	—	—	—	—	(1,583)	(1,583)
Issuance of restricted stock	553	553	—	—	(553)	—	—	—	—	—
Restricted stock withheld for taxes	(189)	(189)	—	—	(3,782)	—	—	(3,971)	—	(3,971)
Share-based compensation cost	—	—	—	—	7,414	—	—	7,414	—	7,414
Dividends (\$0.375 per common share)	—	—	—	—	—	(10,589)	—	(10,589)	—	(10,589)
Balance as of February 28, 2021	<u>27,263</u>	<u>\$ 27,263</u>	<u>200</u>	<u>\$ 200</u>	<u>\$ 39,695</u>	<u>\$ 697,966</u>	<u>\$ (35,282)</u>	<u>\$ 729,842</u>	<u>\$ 4,197</u>	<u>\$ 734,039</u>

The accompanying Notes to the Unaudited Condensed Consolidated Financial Statements are an integral part of these statements.

SCHNITZER STEEL INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)
(Currency - U.S. Dollar)

	Six Months Ended	
	February 28, 2021	February 29, 2020
Cash flows from operating activities:		
Net income (loss)	\$ 60,743	\$ (2,061)
Adjustments to reconcile net income (loss) to cash (used in) provided by operating activities:		
Asset impairment charges	—	2,094
Exit-related asset impairments	—	971
Depreciation and amortization	29,295	28,472
Deferred income taxes	5,544	(1,057)
Undistributed equity in earnings of joint ventures	(1,181)	(389)
Share-based compensation expense	7,276	4,639
Gain on the disposal of assets, net	(81)	(274)
Unrealized foreign exchange loss (gain), net	93	(12)
Credit loss, net	66	53
Changes in assets and liabilities, net of acquisitions:		
Accounts receivable	(75,961)	(18,339)
Inventories	(90,151)	9,067
Income taxes	16,097	28
Prepaid expenses and other current assets	1,266	3,056
Other long-term assets	(3,765)	258
Operating lease assets and liabilities	(430)	(144)
Accounts payable	45,050	(8,298)
Accrued payroll and related liabilities	(85)	(6,655)
Other accrued liabilities	(3,618)	4,943
Environmental liabilities	2,488	(740)
Other long-term liabilities	3,494	41
Distributed equity in earnings of joint ventures	1,250	1,000
Net cash (used in) provided by operating activities	(2,610)	16,653
Cash flows from investing activities:		
Capital expenditures	(55,084)	(37,100)
Proceeds from sale of assets	317	608
Deposit on land option	630	630
Net cash used in investing activities	(54,137)	(35,862)
Cash flows from financing activities:		
Borrowings from long-term debt	265,645	244,382
Repayment of long-term debt	(199,229)	(208,614)
Payment of debt issuance costs	(23)	—
Repurchase of Class A common stock	—	(914)
Taxes paid related to net share settlement of share-based payment awards	(3,971)	(5,845)
Distributions to noncontrolling interests	(1,583)	(1,086)
Dividends paid	(10,828)	(10,734)
Net cash provided by financing activities	50,011	17,189
Effect of exchange rate changes on cash	175	(31)
Net decrease in cash and cash equivalents	(6,561)	(2,051)
Cash and cash equivalents as of beginning of period	17,887	12,377
Cash and cash equivalents as of end of period	<u>\$ 11,326</u>	<u>\$ 10,326</u>

The accompanying Notes to the Unaudited Condensed Consolidated Financial Statements are an integral part of these statements.

SCHNITZER STEEL INDUSTRIES, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)
(Currency - U.S. Dollar)

	Six Months Ended	
	February 28, 2021	February 29, 2020
SUPPLEMENTAL DISCLOSURES:		
Cash paid during the period for:		
Interest	\$ 1,827	\$ 1,698
Income taxes (refunded) paid, net	\$ (4,525)	\$ 196
Schedule of noncash investing and financing transactions:		
Purchases of property, plant and equipment included in current liabilities	\$ 11,338	\$ 7,642

The accompanying Notes to the Unaudited Condensed Consolidated Financial Statements are an integral part of these statements.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Summary of Significant Accounting Policies

Basis of Presentation

The accompanying Unaudited Condensed Consolidated Financial Statements of Schnitzer Steel Industries, Inc. and its majority-owned and wholly-owned subsidiaries (the “Company”) have been prepared pursuant to generally accepted accounting principles in the United States of America (“U.S. GAAP”) for interim financial information and the rules and regulations of the United States Securities and Exchange Commission (the “SEC”) for Form 10-Q, including Article 10 of Regulation S-X. The year-end condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by U.S. GAAP. Certain information and note disclosures normally included in annual financial statements have been condensed or omitted pursuant to the rules and regulations of the SEC. In the opinion of management, all normal, recurring adjustments considered necessary for a fair statement have been included. Management suggests that these Unaudited Condensed Consolidated Financial Statements be read in conjunction with the financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended August 31, 2020. The results for the three and six months ended February 28, 2021 and February 29, 2020, are not necessarily indicative of the results of operations for the entire fiscal year.

Segment Reporting

The Company acquires and recycles ferrous and nonferrous scrap metal for sale to foreign and domestic metal producers, processors and brokers, and it procures salvaged vehicles and sells serviceable used auto parts from these vehicles through a network of self-service auto parts stores. Most of these auto parts stores supply the Company’s shredding facilities with auto bodies that are processed into saleable recycled scrap metal. The Company also produces a range of finished steel long products at its steel mini-mill using ferrous recycled scrap metal primarily sourced internally from its recycling and joint venture operations and other raw materials.

The accounting standards for reporting information about operating segments define an operating segment as a component of an enterprise that engages in business activities from which it may earn revenues and incur expenses for which discrete financial information is available that is evaluated regularly by the chief operating decision-maker in deciding how to allocate resources and in assessing performance.

Prior to the first quarter of fiscal 2021, the Company’s internal organizational and reporting structure included two operating and reportable segments: the Auto and Metals Recycling (“AMR”) business and the Cascade Steel and Scrap (“CSS”) business. In the first quarter of fiscal 2021, in accordance with its plan announced in April 2020, the Company completed its transition to a new internal organizational and reporting structure reflecting a functionally-based, integrated model. The Company consolidated its operations, sales, services and other functional capabilities at an enterprise level reflecting enhanced focus by management on optimizing the Company’s vertically integrated value chain. This change resulted in a realignment of how the Chief Executive Officer, who is considered the Company’s chief operating decision-maker, reviews performance and makes decisions on resource allocation, supporting a single segment. The Company began reporting on this new single-segment structure in the first quarter of fiscal 2021 as reflected in its Quarterly Report on Form 10-Q for the quarterly period ended November 30, 2020.

Accounting Changes

As of the beginning of the first quarter of fiscal 2020, the Company adopted an accounting standards update that requires a lessee to recognize a lease liability and a lease right-of-use asset on its balance sheet for all leases greater than 12 months, including those classified as operating leases. The Company adopted the new lease accounting standard using the modified retrospective transition method, whereby it applied the new requirements by recognizing a cumulative-effect adjustment to the opening balance of retained earnings as of September 1, 2019. Such cumulative-effect adjustment for the Company was less than \$1 million, which is presented separately in the Unaudited Condensed Consolidated Statement of Equity for the six months ended February 29, 2020.

Cash and Cash Equivalents

Cash and cash equivalents include short-term securities that are not restricted by third parties and have an original maturity date of 90 days or less. Included in accounts payable are book overdrafts representing outstanding checks in excess of funds on deposit of \$43 million and \$20 million as of February 28, 2021 and August 31, 2020, respectively.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Accounts Receivable, net

Accounts receivable represent amounts primarily due from customers on product and other sales. These accounts receivable, which are reduced by an allowance for credit losses, are recorded at the invoiced amount and do not bear interest. The Company extends credit to customers under contracts containing customary and explicit payment terms, and payment is generally required within 30 to 60 days of shipment. Nonferrous export sales typically require a deposit prior to shipment. Historically, almost all of the Company's ferrous export sales have been made with letters of credit. Ferrous and nonferrous metal sales to domestic customers and finished steel sales are generally made on open account, and a portion of these sales are covered by credit insurance.

The Company evaluates the collectibility of its accounts receivable based on a combination of factors, including whether sales were made pursuant to letters of credit or credit insurance is in place. Management evaluates the aging of customer receivable balances, the financial condition of the Company's customers, historical collection rates and economic trends to estimate the amount of customer receivables that may not be collected in the future and records a provision for expected credit losses. Accounts are written off when all efforts to collect have been exhausted.

Also included in accounts receivable are short-term advances to scrap metal suppliers used as a mechanism to acquire unprocessed scrap metal. The advances are generally repaid with scrap metal, as opposed to cash. Repayments of advances with scrap metal are treated as noncash operating activities in the Unaudited Condensed Consolidated Statements of Cash Flows and totaled \$5 million for each of the six months ended February 28, 2021 and February 29, 2020.

Prepaid Expenses

The Company's prepaid expenses, reported within prepaid expenses and other current assets in the Unaudited Condensed Consolidated Balance Sheets, totaled \$23 million as of each of February 28, 2021 and August 31, 2020, and consisted primarily of deposits on capital projects, prepaid services, prepaid insurance and prepaid property taxes.

Other Assets

The Company's other assets, exclusive of prepaid expenses and assets relating to certain retirement plans, consist primarily of receivables from insurers, cash held in a client trust account relating to a legal settlement, spare parts, capitalized implementation costs for cloud computing arrangements, an equity investment, debt issuance costs, and notes and other contractual receivables. Other assets are reported within either prepaid expenses and other current assets or other assets in the Unaudited Condensed Consolidated Balance Sheets based on their expected use either during or beyond the current operating cycle of one year from the reporting date.

Other assets as of February 28, 2021 and August 31, 2020 included \$12 million and \$5 million, respectively, in receivables from insurers, comprising \$7 million and less than \$1 million, respectively, relating to environmental claims and \$4 million as of each reporting date relating to workers' compensation claims.

Other assets as of February 28, 2021 also included approximately \$7.6 million in cash deposited into a client trust account in the second quarter of fiscal 2021 to fund the remediation of a site a portion of which was previously leased to and operated by an indirect, wholly-owned subsidiary. The cash was deposited into the client trust account by other potentially liable parties in connection with settlement of a lawsuit relating to allocation of the remediation costs, including agreement by the Company's subsidiary to perform certain remedial actions. See "Other Legacy Environmental Loss Contingencies" within "Contingencies – Environmental" in Note 4 – Commitments and Contingencies for further discussion of this matter.

The Company invested \$6 million in the equity of a privately-held waste and recycling entity in fiscal 2017. The equity investment does not have a readily determinable fair value and, therefore, is carried at cost and adjusted for impairments and observable price changes. The investment is reported within other assets in the Unaudited Condensed Consolidated Balance Sheets. The carrying value of the investment was \$6 million as of February 28, 2021 and August 31, 2020. The Company has not recorded any impairments or upward or downward adjustments to the carrying value of the investment since acquisition.

Long-Lived Assets

The Company tests long-lived tangible and intangible assets for impairment at the asset group level, which is determined based on the lowest level for which identifiable cash flows are largely independent of the cash flows of other groups of assets and liabilities. The segment realignment completed in the first quarter of fiscal 2021 described above in this Note under "Segment Reporting" did not significantly impact the composition of the Company's asset groups.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Concentration of Credit Risk

Financial instruments that potentially subject the Company to significant concentration of credit risk consist primarily of cash and cash equivalents, accounts receivable, and notes and other contractual receivables. The majority of cash and cash equivalents is maintained with major financial institutions. Balances with these and certain other institutions exceeded the Federal Deposit Insurance Corporation insured amount of \$250 thousand as of February 28, 2021. Concentration of credit risk with respect to accounts receivable is limited because a large number of geographically diverse customers make up the Company's customer base. The Company controls credit risk through credit approvals, credit limits, credit insurance, letters of credit or other collateral, cash deposits and monitoring procedures.

Recent Accounting Pronouncements

The Company does not expect that its adoption in the future of any recently issued accounting pronouncements will have a material impact on its consolidated financial statements.

Note 2 - Inventories

Inventories consisted of the following (in thousands):

	February 28, 2021	August 31, 2020
Processed and unprocessed scrap metal	\$ 142,342	\$ 63,058
Semi-finished goods	12,411	6,909
Finished goods	53,637	44,476
Supplies	43,878	42,826
Inventories	<u>\$ 252,268</u>	<u>\$ 157,269</u>

Note 3 - Goodwill

The Company evaluates goodwill for impairment annually on July 1 and upon the occurrence of certain triggering events or substantive changes in circumstances that indicate that the fair value of goodwill may be impaired. Impairment of goodwill is tested at the reporting unit level. A reporting unit is an operating segment or one level below an operating segment (referred to as a "component"). A component of an operating segment is required to be identified as a reporting unit if the component is a business for which discrete financial information is available and segment management regularly reviews its operating results. There were no triggering events identified during the first half of fiscal 2021 requiring an interim goodwill impairment test, and the Company did not record a goodwill impairment charge in any of the periods presented.

As of August 31, 2020, the balance of the Company's goodwill was \$170 million, and all but \$1 million of such balance was carried by a single reporting unit within the AMR operating segment that existed at the time. The Company had last performed the quantitative impairment test of goodwill carried by this reporting unit in the fourth quarter of fiscal 2020 using a measurement date of July 1, 2020. The estimated fair value of the reporting unit exceeded its carrying amount by approximately 29% as of July 1, 2020. In the first quarter of fiscal 2021, the Company completed its transition to a new internal organizational and reporting structure reflecting a functionally-based, integrated model, resulting in a single operating segment, replacing the AMR and CSS operating segments. The change in structure led to the identification of components within the single operating segment based on disaggregation of financial information regularly reviewed by segment management. In accordance with the accounting guidance, the Company then reassigned the Company's goodwill to the reporting units affected based on the relative fair values of the elements transferred and the elements remaining within the original reporting units as of the date of the reassessment, September 1, 2020. The Company measured the relative fair values of such elements under the market approach based on earnings multiple data. Beginning on the date of reassessment of September 1, 2020, the Company's goodwill is carried by three reporting units comprising two separate regional groups of metals recycling operations and the Company's retail auto parts stores.

In connection with the segment realignment and redefinition of the Company's reporting units effective as of September 1, 2020, management evaluated if it was more likely than not that the fair value of any of the either legacy or new reporting units with allocated goodwill was below its carrying value as of September 1, 2020, which would indicate a triggering event requiring a goodwill impairment test. Based on management's assessment as of September 1, 2020, it was not more likely than not that the fair value of each reporting unit with allocated goodwill was below its carrying value.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The gross change in the carrying amount of goodwill for the six months ended February 28, 2021 was as follows (in thousands):

	Goodwill
September 1, 2020	\$ 169,627
Foreign currency translation adjustment	473
February 28, 2021	<u>\$ 170,100</u>

Accumulated goodwill impairment charges were \$471 million as of February 28, 2021 and August 31, 2020.

Note 4 - Commitments and Contingencies

Contingencies - Environmental

The Company evaluates the adequacy of its environmental liabilities on a quarterly basis. Adjustments to the liabilities are made when additional information becomes available that affects the estimated costs to study or remediate any environmental issues or expenditures are made for which liabilities were established.

Changes in the Company's environmental liabilities for the six months ended February 28, 2021 were as follows (in thousands):

Balance as of September 1, 2020	Liabilities Established (Released), Net	Payments and Other	Balance as of February 28, 2021	Short-Term	Long-Term
\$ 53,464	\$ 14,974	\$ (1,498)	\$ 66,940	\$ 12,975	\$ 53,965

As of February 28, 2021 and August 31, 2020, the Company had environmental liabilities of \$67 million and \$53 million, respectively, for the potential remediation of locations where it has conducted business or has environmental liabilities from historical or recent activities. The liabilities relate to the investigation and potential future remediation of contaminated sediments and riverbanks, soil contamination, groundwater contamination, storm water runoff issues and other natural resource damages. Except for Portland Harbor and certain liabilities discussed under "Other Legacy Environmental Loss Contingencies" below, such liabilities were not individually material at any site.

Portland Harbor

In December 2000, the Company was notified by the United States Environmental Protection Agency ("EPA") under the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA") that it is one of the potentially responsible parties ("PRPs") that own or operate or formerly owned or operated sites which are part of or adjacent to the Portland Harbor Superfund site (the "Site"). The precise nature and extent of cleanup of any specific areas within the Site, the parties to be involved, the timing of any specific remedial action and the allocation of the costs for any cleanup among responsible parties have not yet been determined. The process of site investigation, remedy selection, identification of additional PRPs and allocation of costs has been underway for a number of years, but significant uncertainties remain. It is unclear to what extent the Company will be liable for environmental costs or natural resource damage claims or third party contribution or damage claims with respect to the Site.

While the Company participated in certain preliminary Site study efforts, it was not party to the consent order entered into by the EPA with certain other PRPs, referred to as the "Lower Willamette Group" ("LWG"), for a remedial investigation/feasibility study ("RI/FS"). During fiscal 2007, the Company and certain other parties agreed to an interim settlement with the LWG under which the Company made a cash contribution to the LWG RI/FS. The LWG has indicated that it had incurred over \$155 million in investigation-related costs over an approximately 18 year period working on the RI/FS. Following submittal of draft RI and FS documents which the EPA largely rejected, the EPA took over the RI/FS process.

The Company has joined with approximately 100 other PRPs, including the LWG members, in a voluntary process to establish an allocation of costs at the Site, including the costs incurred by the LWG in the RI/FS process. The LWG members have also commenced federal court litigation, which has been stayed, seeking to bring additional parties into the allocation process.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In January 2008, the Portland Harbor Natural Resource Trustee Council (“Trustee Council”) invited the Company and other PRPs to participate in funding and implementing the Natural Resource Injury Assessment for the Site. Following meetings among the Trustee Council and the PRPs, funding and participation agreements were negotiated under which the participating PRPs, including the Company, agreed to fund the first phase of the three-phase natural resource damage assessment. Phase 1, which included the development of the Natural Resource Damage Assessment Plan (“AP”) and implementation of several early studies, was substantially completed in 2010. In December 2017, the Company joined with other participating PRPs in agreeing to fund Phase 2 of the natural resource damage assessment, which includes the implementation of the AP to develop information sufficient to facilitate early settlements between the Trustee Council and Phase 2 participants and the identification of restoration projects to be funded by the settlements. In late May 2018, the Trustee Council published notice of its intent to proceed with Phase 3, which will involve the full implementation of the AP and the final injury and damage determination. The Company is proceeding with the process established by the Trustee Council regarding early settlements under Phase 2.

On January 30, 2017, one of the Trustees, the Confederated Tribes and Bands of the Yakama Nation, which withdrew from the council in 2009, filed a suit against approximately 30 parties, including the Company, seeking reimbursement of certain past and future response costs in connection with remedial action at the Site and recovery of assessment costs related to natural resources damages from releases at and from the Site to the Multnomah Channel and the Lower Columbia River. The parties filed various motions to dismiss or stay this suit, and in August 2019, the court issued an order denying the motions to dismiss and staying the action. The Company intends to defend against the claims in this suit and does not have sufficient information to determine the likelihood of a loss in this matter or to estimate the amount of damages being sought or the amount of such damages that could be allocated to the Company.

Estimates of the cost of remedial action for the cleanup of the in-river portion of the Site have varied widely in various drafts of the FS and in the EPA’s final FS issued in June 2016 ranging from approximately \$170 million to over \$2.5 billion (net present value), depending on the remedial alternative and a number of other factors. In comments submitted to the EPA, the Company and certain other stakeholders identified a number of serious concerns regarding the EPA’s risk and remedial alternatives assessments, cost estimates, scheduling assumptions and conclusions regarding the feasibility and effectiveness of remediation technologies.

In January 2017, the EPA issued a Record of Decision (“ROD”) that identified the selected remedy for the Site. The selected remedy is a modified version of one of the alternative remedies evaluated in the EPA’s FS that was expanded to include additional work at a greater cost. The EPA has estimated the total cost of the selected remedy at \$1.7 billion with a net present value cost of \$1.05 billion (at a 7% discount rate) and an estimated construction period of 13 years following completion of the remedial designs. In the ROD, the EPA stated that the cost estimate is an order-of-magnitude engineering estimate that is expected to be within +50% to -30% of the actual project cost and that changes in the cost elements are likely to occur as a result of new information and data collected during the engineering design. The Company has identified a number of concerns regarding the remedy described in the ROD, which is based on data that is more than a decade old, and the EPA’s estimates for the costs and time required to implement the selected remedy. Because of ongoing questions regarding cost effectiveness, technical feasibility, and the use of stale data, it is uncertain whether the ROD will be implemented as issued. In addition, the ROD did not determine or allocate the responsibility for remediation costs among the PRPs.

In the ROD, the EPA acknowledged that much of the data used in preparing the ROD was more than a decade old and would need to be updated with a new round of “baseline” sampling to be conducted prior to the remedial design phase. Accordingly, the ROD provided for additional pre-remedial design investigative work and baseline sampling to be conducted in order to provide a baseline of current conditions and delineate particular remedial actions for specific areas within the Site. This additional sampling was required prior to proceeding with the next phase in the process which is the remedial design. The remedial design phase is an engineering phase during which additional technical information and data are collected, identified and incorporated into technical drawings and specifications developed for the subsequent remedial action. Moreover, the ROD provided only Site-wide cost estimates and did not provide sufficient detail to estimate costs for specific sediment management areas within the Site. Following issuance of the ROD, EPA proposed that the PRPs, or a subgroup of PRPs, perform the additional investigative work identified in the ROD under a new consent order.

In December 2017, the Company and three other PRPs entered into a new Administrative Settlement Agreement and Order on Consent with EPA to perform such pre-remedial design investigation and baseline sampling over a two-year period. The Company estimated that its share of the costs of performing such work would be approximately \$2 million, which it accrued in fiscal 2018. Such costs were fully covered by existing insurance coverage and, thus, the Company also recorded an insurance receivable for \$2 million in fiscal 2018, resulting in no net impact to the Company’s consolidated results of operations.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The pre-remedial design investigation and baseline sampling work has been completed, and the report evaluating the data was submitted to EPA on June 17, 2019. The evaluation report concludes that Site conditions have improved substantially since the data forming the basis of the ROD was collected over a decade ago. The analysis contained in the report has significant implications for remedial design and remedial action at the Site. EPA has reviewed the report, finding with a few limited corrections that the data is of suitable quality and generally acceptable and stating that such data will be used, in addition to existing and forthcoming design-level data, to inform implementation of the ROD. However, EPA did not agree that the data or the analysis warrants a change to the remedy at this time and reaffirmed its commitment to proceed with remedial design. The Company and other PRPs disagree with EPA's position on use of the more recent data and will continue to pursue limited, but critical, changes to the selected remedy for the Site during the remedial design phase.

EPA encouraged PRPs to step forward (individually or in groups) to enter into consent agreements to perform remedial design covering the entire Site and proposed dividing the Site into eight to ten subareas for remedial design. While certain PRPs executed consent agreements for remedial design work, because of EPA's refusal to date to modify the remedy to reflect the most current data on Site conditions and because of concerns with the terms of the consent agreement, the Company elected not to enter into a consent agreement for remedial design with respect to any of the subareas at the Site. On March 26, 2020, EPA issued a unilateral administrative order (UAO) to the Company and MMGL, LLC ("MMGL"), an unaffiliated company, for the remedial design work in the portion of one of the EPA identified subareas within the Site designated as the River Mile 3.5 East Project Area. Following a conference with the Company to discuss the UAO and written comments submitted by the Company, EPA made limited modifications to the UAO and issued an amendment to the UAO on April 27, 2020 with an effective date of May 4, 2020. As required by the UAO, the Company notified EPA of its intent to comply with the UAO on the effective date while reserving all of its sufficient cause defenses. Failure to comply with a UAO, without sufficient cause, could subject the Company to significant penalties or treble damages. Pursuant to the optimized remedial design timeline set forth in the UAO, EPA's expected schedule for completion of the remedial design work is four years. EPA has estimated the cost of the work at approximately \$4 million. The Company has agreed with the other respondent to the UAO, MMGL, that the Company will lead the performance and be responsible for a portion of the costs of the work for remedial design under the UAO and also entered into an agreement with another PRP pursuant to which such other PRP has agreed to fund a portion of the costs of such work. These agreements are not an allocation of liability or claims associated with the Site as between the respondents or with respect to any third party. The Company estimated that its share of the costs of performing such work under the UAO would be approximately \$3 million, which it recorded to environmental liabilities and selling, general and administrative expense in the consolidated financial statements in the third quarter of fiscal 2020. The Company has insurance policies that it believes will provide reimbursement for costs it incurs for remedial design, but not for any penalties. In the second quarter of fiscal 2021, the Company recorded an insurance receivable and a related insurance recovery to selling, general and administrative expense for approximately \$3 million. See "Other Assets" in Note 1 – Summary of Significant Accounting Policies for further discussion of receivables from insurers. The Company also expects to pursue in the future allocation or contribution from other PRPs for a portion of such remedial design costs. In February 2021, EPA announced that 100 percent of the Site's areas requiring active cleanup are in the remedial design phase of the process.

The Company's environmental liabilities as of February 28, 2021 and August 31, 2020 included \$6 million and \$4 million, respectively, relating to the Portland Harbor matters described above.

Except for certain early action projects in which the Company is not involved, remediation activities are not expected to commence for a number of years. Moreover, remediation activities at the Site are expected to be sequenced, and the order and timing of such sequencing has not been determined. In addition, as discussed above, responsibility for implementing and funding the remedy will be determined in a separate allocation process, which is on-going. The Company expects the next major stage of the allocation process to proceed in parallel with the remedial design process.

Because the final remedial actions have not yet been designed and there has not been a determination of the amount of natural resource damages or of the allocation among the PRPs of costs of the investigations, remedial action costs or natural resource damages, the Company believes it is not possible to reasonably estimate the amount or range of costs which it is likely to or which it is reasonably possible that it will incur in connection with the Site, although such costs could be material to the Company's financial position, results of operations, cash flows and liquidity. Among the facts currently being developed are detailed information on the history of ownership of and the nature of the uses of and activities and operations performed on each property within the Site, which are factors that will play a substantial role in determining the allocation of investigation and remedy costs among the PRPs.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The Company has insurance policies that it believes will provide reimbursement for costs it incurs for defense, remedial design, remedial action and mitigation for or settlement of natural resource damages claims in connection with the Site. Most of these policies jointly insure the Company and MMGL, as the successor to a former subsidiary of the Company. The Company and MMGL have negotiated the settlement with certain insurers of claims against them related to the Site, continue to seek settlements with other insurers and formed a Qualified Settlement Fund (“QSF”) which became operative in the fourth quarter of fiscal 2020 to hold such settlement amounts until funds are needed to pay or reimburse costs incurred by the Company and MMGL in connection with the Site. These insurance policies and the funds in the QSF may not cover all of the costs which the Company may incur. The QSF is an unconsolidated variable interest entity (“VIE”) with no primary beneficiary. Two parties unrelated to each other, one appointed by the Company and one appointed by MMGL, share equally the power to direct the activities of the VIE that most significantly impact its economic performance. The Company’s appointee to co-manage the VIE is an executive officer of the Company. Neither MMGL nor its appointee to co-manage the VIE is a related party of the Company for the purpose of the primary beneficiary assessment or otherwise.

The Oregon Department of Environmental Quality is separately providing oversight of investigations and source control activities by the Company at various sites adjacent to Portland Harbor that are focused on controlling any current “uplands” releases of contaminants into the Willamette River. No liabilities have been established in connection with these investigations beyond the costs of investigation and design, which costs have not been material to date, because the extent of contamination, required source control work and the Company’s responsibility for the contamination and source control work, in each case if any, have not yet been determined.

Other Legacy Environmental Loss Contingencies

The Company’s environmental loss contingencies as of February 28, 2021 and August 31, 2020, other than Portland Harbor, include actual or possible investigation and cleanup costs from historical contamination at sites currently or formerly owned or formerly operated by the Company or at other sites where the Company may have responsibility for such costs due to past disposal or other activities (“legacy environmental loss contingencies”). These legacy environmental loss contingencies relate to the potential remediation of waterways and soil and groundwater contamination and may also involve natural resource damages, governmental fines and penalties and claims by third parties for personal injury and property damage. The Company has been notified that it is or may be a potentially responsible party at certain of these sites, and investigation and cleanup activities are ongoing or may be required in the future. The Company recognizes a liability for such matters when the loss is probable and can be reasonably estimated. When investigation and cleanup activities are ongoing or where the Company has not yet been identified as having responsibility or the contamination has not yet been identified, it is reasonably possible that the Company may need to recognize additional liabilities in connection with such sites but the Company cannot currently reasonably estimate the possible loss or range of loss absent additional information or developments. Such additional liabilities, individually or in the aggregate, may have a material adverse effect on the Company’s results of operations, financial condition or cash flows.

During fiscal 2018, the Company accrued \$4 million for the estimated costs related to remediation of shredder residue disposed of in or around the 1970s at third-party sites located near each other. Investigation activities have been conducted under oversight of the applicable state regulatory agency. As of February 28, 2021 and August 31, 2020, the Company had \$4 million accrued for this matter. It is reasonably possible that the Company may recognize additional liabilities in connection with this matter at the time such losses are probable and can be reasonably estimated. The Company previously estimated a range of reasonably possible losses related to this matter in excess of current accruals at between zero and \$28 million based on a range of remedial alternatives and subject to development and approval by regulators of a specific remedy implementation plan. However, subsequent to the development of those remedial alternatives, the Company performed additional investigative activities under new state requirements that have the potential to impact the required remedial actions and associated cost estimates pending further analysis and discussion by the Company and regulators. The Company is investigating whether a portion or all of the current and future losses related to this matter, if incurred, are covered by existing insurance coverage or may be offset by contributions from other responsible parties.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

In addition, the Company's loss contingencies as of February 28, 2021 and August 31, 2020 included \$9 million and \$8 million, respectively, for the estimated costs related to environmental matters in connection with a closed facility owned and previously operated by an indirect, wholly-owned subsidiary, including monitoring and remediation of soil and groundwater conditions. Investigation activities have been conducted under the oversight of the applicable state regulatory agency, and the Company has also been working with local officials with respect to the protection of public water supplies. The increase in the loss contingency accrual in the first six months of fiscal 2021 primarily reflects accrual in the second quarter of \$4 million for incremental estimated remediation costs, partially offset by payment during the first quarter of penalties in the amount of \$2.7 million pursuant to the previously agreed settlement. It is reasonably possible that the Company may recognize additional liabilities in connection with this matter at the time such additional losses are probable and can be reasonably estimated. However, the Company cannot reasonably estimate at this time the possible additional loss or range of possible additional losses associated with this matter pending completion of cost estimates and implementation of the approved remediation plan. As part of its activities relating to the protection of public water supplies, the Company has agreed to reimburse the municipality for certain studies and plans, and it is reasonably possible that it may incur additional liabilities and costs in the future, including for wellhead treatment, which in the case of costs for installation of wellhead treatment, if incurred, could be in the range of \$10 million to \$13 million.

In addition, the Company's loss contingencies as of February 28, 2021 and August 31, 2020 included \$8 million and less than \$1 million, respectively, for the estimated costs related to remediation of a site a portion of which was previously leased to and operated by an indirect, wholly-owned subsidiary. In connection with settlement of a lawsuit relating to allocation of the remediation costs, the Company's subsidiary agreed to perform the remedial action related to metals contamination on the site estimated to cost approximately \$7.9 million, and another potentially liable party agreed to perform the remedial action related to creosote contamination at the site. As part of the settlement, other potentially liable parties agreed to make payments totaling approximately \$7.6 million to fund the remediation of the metals contamination at the site in exchange for a release and indemnity. This amount was fully funded into a client trust account for the Company's subsidiary in December 2020. See "Other Assets" in Note 1 – Summary of Significant Accounting Policies for further discussion of this client trust account. It is reasonably possible that the Company may recognize additional liabilities in connection with this matter at the time such additional losses are probable and can be reasonably estimated. However, the Company cannot reasonably estimate at this time the possible additional loss or range of possible additional losses associated with this matter pending completion, approval and implementation of the remediation action plan.

Summary - Environmental Contingencies

With respect to environmental contingencies other than the Portland Harbor Superfund site and the Other Legacy Environmental Loss Contingencies, which are discussed separately above, management currently believes that adequate provision has been made for the potential impact of its environmental contingencies. Historically, the amounts the Company has ultimately paid for such remediation activities have not been material in any given period, but there can be no assurance that such amounts paid will not be material in the future.

Contingencies - Other

In addition to legal proceedings relating to the contingencies described above, the Company is a party to various legal proceedings arising in the normal course of business. The Company recognizes a liability for such matters when the loss is probable and can be reasonably estimated. The Company does not anticipate that the liabilities arising from such legal proceedings in the normal course of business, after taking into consideration expected insurance recoveries, will have a material adverse effect on its results of operations, financial condition, or cash flows.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 5 - Accumulated Other Comprehensive Loss

Changes in accumulated other comprehensive loss, net of tax, comprise the following (in thousands):

	Three Months Ended February 28, 2021			Three Months Ended February 29, 2020		
	Foreign Currency Translation Adjustments	Pension Obligations, Net	Total	Foreign Currency Translation Adjustments	Pension Obligations, Net	Total
Balances - December 1 (Beginning of period)	\$ (33,945)	\$ (2,947)	\$ (36,892)	\$ (35,478)	\$ (3,047)	\$ (38,525)
Other comprehensive income (loss) before reclassifications	1,572	—	1,572	(630)	—	(630)
Income tax benefit	—	—	—	—	—	—
Other comprehensive income (loss) before reclassifications, net of tax	1,572	—	1,572	(630)	—	(630)
Amounts reclassified from accumulated other comprehensive loss	—	49	49	—	148	148
Income tax (benefit)	—	(11)	(11)	—	(33)	(33)
Amounts reclassified from accumulated other comprehensive loss, net of tax	—	38	38	—	115	115
Net periodic other comprehensive income (loss)	1,572	38	1,610	(630)	115	(515)
Balances - February 28 and 29, respectively (End of period)	<u>\$ (32,373)</u>	<u>\$ (2,909)</u>	<u>\$ (35,282)</u>	<u>\$ (36,108)</u>	<u>\$ (2,932)</u>	<u>\$ (39,040)</u>

	Six Months Ended February 28, 2021			Six Months Ended February 29, 2020		
	Foreign Currency Translation Adjustments	Pension Obligations, Net	Total	Foreign Currency Translation Adjustments	Pension Obligations, Net	Total
Balances - September 1 (Beginning of period)	\$ (34,184)	\$ (2,687)	\$ (36,871)	\$ (35,689)	\$ (3,074)	\$ (38,763)
Other comprehensive income (loss) before reclassifications	1,811	(385)	1,426	(419)	(17)	(436)
Income tax benefit	—	87	87	—	4	4
Other comprehensive income (loss) before reclassifications, net of tax	1,811	(298)	1,513	(419)	(13)	(432)
Amounts reclassified from accumulated other comprehensive loss	—	98	98	—	200	200
Income tax (benefit)	—	(22)	(22)	—	(45)	(45)
Amounts reclassified from accumulated other comprehensive loss, net of tax	—	76	76	—	155	155
Net periodic other comprehensive income (loss)	1,811	(222)	1,589	(419)	142	(277)
Balances - February 28 and 29, respectively (End of period)	<u>\$ (32,373)</u>	<u>\$ (2,909)</u>	<u>\$ (35,282)</u>	<u>\$ (36,108)</u>	<u>\$ (2,932)</u>	<u>\$ (39,040)</u>

Reclassifications from accumulated other comprehensive loss to earnings, both individually and in the aggregate, were not material to the impacted captions in the Unaudited Condensed Consolidated Statements of Operations in all periods presented.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 6 - Revenue

Disaggregation of Revenues

The table below illustrates the Company's revenues disaggregated by major product and sales destination (in thousands):

	Three Months Ended		Six Months Ended	
	February 28, 2021	February 29, 2020	February 28, 2021	February 29, 2020
Major product information:				
Ferrous revenues	\$ 322,679	\$ 232,066	\$ 574,885	\$ 431,964
Nonferrous revenues	147,322	94,522	267,031	192,363
Steel revenues ⁽¹⁾	99,191	85,539	187,605	162,864
Retail and other revenues	30,919	27,355	62,697	57,875
Total revenues	<u>\$ 600,111</u>	<u>\$ 439,482</u>	<u>\$ 1,092,218</u>	<u>\$ 845,066</u>
Revenues based on sales destination:				
Foreign	\$ 332,197	\$ 224,503	\$ 600,596	\$ 442,985
Domestic	267,914	214,979	491,622	402,081
Total revenues	<u>\$ 600,111</u>	<u>\$ 439,482</u>	<u>\$ 1,092,218</u>	<u>\$ 845,066</u>

(1) Steel revenues include primarily sales of finished steel products, semi-finished goods (billets) and manufacturing scrap.

Receivables from Contracts with Customers

The revenue accounting standard defines a receivable as an entity's right to consideration that is unconditional, meaning that only the passage of time is required before payment is due. As of February 28, 2021 and August 31, 2020, receivables from contracts with customers, net of an allowance for credit losses, totaled \$208 million and \$135 million, respectively, representing 99% and 97%, respectively, of total accounts receivable reported on the Unaudited Condensed Consolidated Balance Sheets.

Contract Liabilities

Contract consideration received from a customer prior to revenue recognition is recorded as a contract liability and is recognized as revenue when the Company satisfies the related performance obligation under the terms of the contract. The Company's contract liabilities consist almost entirely of customer deposits for recycled scrap metal sales contracts, which are reported within accounts payable on the Unaudited Condensed Consolidated Balance Sheets and totaled \$8 million as of each of February 28, 2021 and August 31, 2020. Unsatisfied performance obligations reflected in these contract liabilities relate to contracts with original expected durations of one year or less and, therefore, are not disclosed. During the three and six months ended February 28, 2021, the Company reclassified \$1 million and \$6 million, respectively, in customer deposits as of August 31, 2020 to revenues as a result of satisfying performance obligations during the respective periods. During the three and six months ended February 29, 2020, the Company reclassified less than \$1 million and \$2 million, respectively, in customer deposits as of August 31, 2019 to revenues as a result of satisfying performance obligations during the respective periods.

Note 7 - Share-Based Compensation

In the first quarter of fiscal 2021, as part of the annual awards under the Company's Long-Term Incentive Plan, the Compensation Committee of the Company's Board of Directors granted 317,760 restricted stock units ("RSUs") and 316,649 performance share awards to the Company's key employees and officers under the Company's 1993 Amended and Restated Stock Incentive Plan. The RSUs have a five-year term and vest 20% per year commencing October 31, 2021. The aggregate fair value of all of the RSUs granted was based on the market closing price of the underlying Class A common stock on the grant date and totaled \$7 million. The compensation expense associated with the RSUs is recognized over the requisite service period of the awards, net of forfeitures, which for participants who were retirement eligible as of the grant date or who will become retirement eligible during the five-year term of the awards is the longer of two years or the period ending on the date retirement eligibility is achieved.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

The performance share awards comprise two separate and distinct awards with different vesting conditions. Awards vest if the threshold level under the specified metric is met at the end of the approximately three-year performance period. For awards granted in the first quarter of fiscal 2021, the performance metrics were the Company's total shareholder return ("TSR") relative to a designated peer group and the Company's return on capital employed ("ROCE"). Award share payouts depend on the extent to which the performance goals have been achieved. The number of shares that a participant receives is equal to the number of performance shares granted multiplied by a payout factor, which ranges from a threshold of 50% to a maximum of 200%. The TSR award stipulates certain limitations to the payout in the event the value of the payout reaches a defined ceiling level or the Company's TSR is negative.

The Company granted 157,791 performance share awards based on its relative TSR metric over a performance period spanning November 9, 2020 to August 31, 2023. The Company estimates the fair value of TSR awards using a Monte-Carlo simulation model utilizing several key assumptions, including the following for TSR awards granted on November 9, 2020:

	Percentage
Expected share price volatility (SSI)	48.5%
Expected share price volatility (Peer group)	54.9%
Expected correlation to peer group companies	44.5%
Risk-free rate of return	0.23%

The estimated fair value of the TSR awards at the date of grant was \$4 million. The compensation expense for the TSR awards based on the grant-date fair value, net of estimated forfeitures, is recognized over the requisite service period (or to the date a qualifying employment termination event entitles the recipient to a prorated award, if before the end of the service period), regardless of whether the market condition has been or will be satisfied.

The Company granted 158,858 performance share awards based on its ROCE for the three-year performance period consisting of the Company's 2021, 2022 and 2023 fiscal years. The fair value of the awards granted was based on the market closing price of the underlying Class A common stock on the grant date and totaled \$4 million.

The Company accrues compensation cost for ROCE awards based on the probable outcome of achieving specified performance conditions, net of estimated forfeitures, over the requisite service period (or to the date a qualifying employment termination event entitles the recipient to a prorated award, if before the end of the service period). The Company reassesses whether achievement of the performance conditions is probable at each reporting date. If it is probable that the actual performance results will exceed the stated target performance conditions, the Company accrues additional compensation cost for the additional performance shares to be awarded. If, upon reassessment, it is no longer probable that the actual performance results will exceed the stated target performance conditions, or that it is no longer probable that the target performance conditions will be achieved, the Company reverses any recognized compensation cost for shares no longer probable of being issued. If the performance conditions are not achieved at the end of the service period, all related compensation cost previously recognized is reversed.

Performance share awards will be paid in Class A common stock as soon as practicable after the end of the requisite service period and vesting date of October 31, 2023.

In the second quarter of fiscal 2021, the Company granted deferred stock units ("DSUs") to each of its non-employee directors under the Company's SIP. Each DSU gives the director the right to receive one share of Class A common stock at a future date. The grant included an aggregate of 28,042 shares that will vest in full on the day before the Company's 2022 annual meeting of shareholders, subject to continued Board service. The total fair value of these awards at the grant date was \$1 million.

SCHNITZER STEEL INDUSTRIES, INC.
NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 8 - Income Taxes

Effective Tax Rate

The Company's effective tax rate from continuing operations for the second quarter and first six months of fiscal 2021 was an expense on pre-tax income of 20.1% and 22.1%, respectively, compared to an expense on pre-tax income of 28.2% and a benefit on pre-tax loss of 26.8%, respectively, for the comparable prior year periods. The Company's effective tax rate from continuing operations for the second quarter and first six months of fiscal 2021 was lower than that for the comparable prior year periods primarily due to the benefit from the foreign derived intangible income deduction in fiscal 2021 and the effects of higher pre-tax income compared to the prior year periods. The Company's effective tax rate from continuing operations for the second quarter and first six months of fiscal 2020 was higher than the U.S. federal statutory rate of 21% primarily due to the impact of non-deductible officers' compensation and other expenses, as well as the aggregate impact of state taxes, on the projected annual effective tax rate applied to the quarterly results.

Valuation Allowances

The Company assesses the realizability of its deferred tax assets on a quarterly basis through an analysis of potential sources of future taxable income, including prior year taxable income available to absorb a carryback of tax losses, reversals of existing taxable temporary differences, tax planning strategies and forecasts of taxable income. The Company considers all negative and positive evidence, including the weight of the evidence, to determine if valuation allowances against deferred tax assets are required. The Company maintains valuation allowances against certain state, Canadian and all Puerto Rican deferred tax assets.

The Company files federal and state income tax returns in the U.S. and foreign tax returns in Puerto Rico and Canada. For U.S. federal income tax returns, fiscal years 2014 to 2020 remain subject to examination under the statute of limitations.

Note 9 - Net Income (Loss) Per Share

The following table sets forth the information used to compute basic and diluted net income (loss) per share attributable to SSI shareholders (in thousands):

	Three Months Ended		Six Months Ended	
	February 28, 2021	February 29, 2020	February 28, 2021	February 29, 2020
Income (loss) from continuing operations	\$ 45,649	\$ 4,503	\$ 60,755	\$ (2,090)
Net income attributable to noncontrolling interests	(1,091)	(621)	(2,051)	(1,051)
Income (loss) from continuing operations attributable to SSI shareholders	44,558	3,882	58,704	(3,141)
Income (loss) from discontinued operations, net of tax	30	1	(12)	29
Net income (loss) attributable to SSI shareholders	\$ 44,588	\$ 3,883	\$ 58,692	\$ (3,112)
Computation of shares:				
Weighted average common shares outstanding, basic	27,991	27,721	27,899	27,618
Incremental common shares attributable to dilutive performance share awards, restricted stock units and deferred stock units	871	418	774	—
Weighted average common shares outstanding, diluted	28,862	28,139	28,673	27,618

No common stock equivalent shares were considered antidilutive for the three months ended February 28, 2021. Common stock equivalent shares of 103,566 were considered antidilutive and were excluded from the calculation of diluted net income (loss) per share attributable to SSI shareholders for the six months ended February 28, 2021, compared to 531,305 and 687,247 for the three and six months ended February 29, 2020, respectively.

Note 10 - Related Party Transactions

The Company purchases recycled metal from its joint venture operations at prices that approximate fair market value. These purchases totaled \$5 million and \$3 million for the three months ended February 28, 2021 and February 29, 2020, respectively, and \$8 million and \$6 million for the six months ended February 28, 2021 and February 29, 2020, respectively.

SCHNITZER STEEL INDUSTRIES, INC.

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

This section includes a discussion of our operations for the three and six months ended February 28, 2021 and February 29, 2020. The following discussion and analysis provide information which management believes is relevant to an assessment and understanding of our financial condition and results of operations. The discussion should be read in conjunction with our Annual Report on Form 10-K for the year ended August 31, 2020, and the Unaudited Condensed Consolidated Financial Statements and the related Notes thereto included in Part I, Item 1 of this report.

General

Founded in 1906, Schnitzer Steel Industries, Inc. (“SSI”), an Oregon corporation, is one of North America’s largest recyclers of ferrous and nonferrous scrap metal, including end-of-life vehicles, and a manufacturer of finished steel products. As a vertically integrated organization, we offer a range of products and services to meet global demand through our network that includes 50 retail self-service auto parts stores, 44 metals recycling facilities and a steel mini-mill in Oregon.

Prior to the first quarter of fiscal 2021, our internal organizational and reporting structure included two operating and reportable segments: the Auto and Metals Recycling (“AMR”) business and the Cascade Steel and Scrap (“CSS”) business. In the first quarter of fiscal 2021, in accordance with our plan announced in April 2020, we completed the transition to a new internal organizational and reporting structure reflecting a functionally-based, integrated model, supporting a single segment. We consolidated our operations, sales, services and other functional capabilities at an enterprise level reflecting enhanced focus by management on optimizing our vertically integrated value chain. We began reporting on this new single-segment structure in the first quarter of fiscal 2021 as reflected in our Quarterly Report on Form 10-Q for the quarterly period ended November 30, 2020.

We sell ferrous and nonferrous recycled scrap metal in both foreign and domestic markets. We also sell a range of finished steel long products produced at our steel mini-mill. We acquire, process and recycle auto bodies, rail cars, home appliances, industrial machinery, manufacturing scrap and construction and demolition scrap through our recycling facilities. Our retail self-service auto parts stores located across the United States and Western Canada, which operate under the commercial brand-name Pick-n-Pull, procure the significant majority of our salvaged vehicles and sell serviceable used auto parts from these vehicles. Upon acquiring a salvaged vehicle, we remove catalytic converters, aluminum wheels and batteries for separate processing and sale prior to placing the vehicle in our retail lot. After retail customers have removed desired parts from a vehicle, we may remove remaining major component parts containing ferrous and nonferrous metals, which are primarily sold to wholesalers. The remaining auto bodies are crushed and shipped to our metals recycling facilities to be shredded or sold to third parties where geographically more economical. At our metals recycling facilities, we process mixed and large pieces of scrap metal into smaller pieces by crushing, torching, shearing, shredding and sorting, resulting in scrap metal pieces of a size, density and metal content required by customers to meet their production needs. The manufacturing process includes physical separation of ferrous and nonferrous materials through automated and manual processes into various sub-classifications, each of which has a value and metal content used by our customers for their end products. We use a variety of shredding and separation systems to efficiently process and sort recycled scrap metal. Our steel mini-mill produces finished steel products such as rebar, wire rod, coiled rebar, merchant bar and other specialty products using ferrous recycled scrap metal primarily sourced internally from our recycling and joint venture operations and other raw materials.

Our deep water port facilities on both the East and West Coasts of the U.S. (in Everett, Massachusetts; Providence, Rhode Island; Oakland, California; Tacoma, Washington; and Portland, Oregon) and access to public deep water port facilities (in Kapolei, Hawaii and Salinas, Puerto Rico) allow us to efficiently meet the global demand for recycled ferrous metal by enabling us to ship bulk cargoes to steel manufacturers located in Europe, Africa, the Middle East, Asia, North America, Central America and South America. Our exports of nonferrous recycled metal are shipped in containers through various public docks to specialty steelmakers, foundries, aluminum sheet and ingot manufacturers, copper refineries and smelters, brass and bronze ingot manufacturers, wire and cable producers, wholesalers, and other recycled metal processors globally. We also transport both ferrous and nonferrous metals by truck, rail and barge in order to transfer scrap metal between our facilities for further processing, to load shipments at our export facilities, and to meet regional domestic demand.

SCHNITZER STEEL INDUSTRIES, INC.

Our results of operations depend in large part on the demand and prices for recycled metal in foreign and domestic markets and on the supply of raw materials, including end-of-life vehicles, available to be processed at our facilities. We respond to changes in selling prices for processed metal by seeking to adjust purchase prices for unprocessed scrap metal in order to manage the impact on our operating results. We believe we generally benefit from sustained periods of stable or rising recycled scrap metal selling prices, which allow us to better maintain or increase both operating results and unprocessed scrap metal flow into our facilities. When recycled scrap metal selling prices decline, either sharply or for a sustained period, our operating margins typically compress. Our results of operations also depend on the demand and prices for our finished steel products, which are sold to customers located primarily in the Western U.S. and Western Canada.

Our quarterly operating results fluctuate based on a variety of factors including, but not limited to, changes in market conditions for ferrous and nonferrous recycled metal and finished steel products, the supply of scrap metal in our domestic markets, and varying demand for used auto parts from our self-service retail stores. Certain of these factors are influenced, to a degree, by the impact of seasonal changes including severe weather conditions, which can impact the timing of shipments and inhibit construction activity utilizing our products, scrap metal collection at our facilities and production levels in our yards, and retail admissions and parts sales at our auto parts stores. Further, trade actions, including tariffs and any retaliation by affected countries, and licensing and inspection requirements can impact the level of profitability on sales of our products and, in certain cases, impede or restrict our ability to sell to certain export markets or require us to direct our sales to alternative market destinations, which can cause our quarterly operating results to fluctuate.

Coronavirus Disease 2019 (COVID-19)

We continue to monitor the impact of COVID-19 on all aspects of our business. The COVID-19 outbreak, which the World Health Organization characterized as a pandemic in March 2020, has resulted in governments around the world implementing measures with various levels of stringency to help control the spread of the virus. In addition, governments and central banks in several parts of the world have enacted fiscal and monetary stimulus measures to counteract the impacts of COVID-19. We are a company operating in a critical infrastructure industry, as defined by the U.S. Department of Homeland Security. Consistent with federal guidelines and with state and local orders to date, we have continued to operate across our footprint throughout the COVID-19 pandemic. Ensuring the health and welfare of our employees, and all who visit our sites, is our top priority, and we are following all U.S. Centers for Disease Control and Prevention and state and local health department guidelines. Further, we implemented infection control measures at all our sites and put in place travel and in-person meeting restrictions and other physical distancing measures. Following the onset of COVID-19 and its negative effects on our business, most prominently reflected in our third quarter fiscal 2020 results, global economic conditions improved during the first half of our fiscal 2021, resulting in increased demand for our products, which led to our earnings for the second quarter and first six months of our fiscal 2021 exceeding the results for the pre-pandemic comparable prior periods. While the ongoing effects of the COVID-19 pandemic could negatively impact our results of operations, cash flows and financial position, the current level of uncertainty over the economic and operational impacts of COVID-19 means the related financial impact cannot be reasonably estimated at this time.

Use of Non-GAAP Financial Measures

In this management's discussion and analysis, we use supplemental measures of our performance, liquidity and capital structure which are derived from our consolidated financial information but which are not presented in our consolidated financial statements prepared in accordance with GAAP. We believe that providing these non-GAAP financial measures adds a meaningful presentation of our operating and financial performance, liquidity and capital structure. For example, following the modification of our internal organizational and reporting structure completed in the first quarter of fiscal 2021, we use adjusted EBITDA as one of the measures to compare and evaluate financial performance. Adjusted EBITDA is the sum of our net income before results from discontinued operations, interest expense, income taxes, depreciation and amortization, restructuring charges and other exit-related activities, charges for legacy environmental matters (net of recoveries), business development costs, asset impairment charges (net of recoveries) and other items which are not related to underlying business operational performance. See the reconciliations of supplemental financial measures, including adjusted EBITDA, in Non-GAAP Financial Measures at the end of this Item 2.

Our non-GAAP financial measures should be considered in addition to, but not as a substitute for, the most directly comparable U.S. GAAP measures. Although we find these non-GAAP financial measures useful in evaluating the performance of our business, our reliance on these measures is limited because they often materially differ from our consolidated financial statements presented in accordance with GAAP. Therefore, we typically use these adjusted amounts in conjunction with our GAAP results to address these limitations. Our non-GAAP financial measures may not be comparable to similarly titled measures of other companies. Other companies, including companies in our industry, may calculate non-GAAP financial measures differently than we do, limiting the usefulness of those measures for comparative purposes.

SCHNITZER STEEL INDUSTRIES, INC.

Financial Highlights of Results of Operations for the Second Quarter of Fiscal 2021

- Diluted earnings per share from continuing operations attributable to SSI shareholders in the second quarter of fiscal 2021 was \$1.54, compared to \$0.14 in the prior year quarter.
- Adjusted diluted earnings per share from continuing operations attributable to SSI shareholders in the second quarter of fiscal 2021 was \$1.51, compared to \$0.31 in the prior year quarter.
- Net income in the second quarter of fiscal 2021 was \$46 million, compared to \$5 million in the prior year quarter.
- Adjusted EBITDA in the second quarter of fiscal 2021 was \$71 million, compared to \$28 million in the prior year quarter.

Market conditions for recycled metals improved in the second quarter of fiscal 2021, including sharply rising selling prices that reached multi-year highs for certain recycled metal commodities. Average net selling prices for our ferrous and nonferrous products increased significantly compared to the prior year quarter. In the second quarter of fiscal 2021, the average net selling prices for our ferrous and nonferrous products increased by 52% and 51%, respectively, compared to the prior year period. Market conditions for our finished steel products also improved in the second quarter of fiscal 2021, which contributed to higher finished steel average selling prices and sales volumes compared to the prior year period. Our results in the second quarter of fiscal 2021 reflected substantial benefits from the higher price environment for most of our products including a significant expansion in our ferrous metal spreads and a favorable impact from average inventory accounting, as well as increased nonferrous and finished steel sales volumes, compared to the prior year period. We also benefited in the quarter from commercial initiatives and productivity improvements that were supported by the implementation of our One Schnitzer functionally-based organization model completed in the first quarter of fiscal 2021.

The following items further highlight selected liquidity and capital structure metrics:

- For the first six months of fiscal 2021, net cash used in operating activities was \$3 million, compared to net cash provided by operating activities of \$17 million in the prior year comparable period.
- Debt was \$171 million as of February 28, 2021, compared to \$104 million as of August 31, 2020.
- Debt, net of cash, was \$159 million as of February 28, 2021, compared to \$87 million as of August 31, 2020.

See the reconciliations of adjusted diluted earnings per share from continuing operations attributable to SSI shareholders, adjusted EBITDA, and debt, net of cash in Non-GAAP Financial Measures at the end of this Item 2.

SCHNITZER STEEL INDUSTRIES, INC.

Results of Operations

(\$ in thousands, except for prices and per share amounts)	Three Months Ended			Six Months Ended		
	February 28, 2021	February 29, 2020	Change %	February 28, 2021	February 29, 2020	Change %
Ferrous revenues	\$ 322,679	\$ 232,066	39%	\$ 574,885	\$ 431,964	33%
Nonferrous revenues	147,322	94,522	56%	267,031	192,363	39%
Steel revenues ⁽¹⁾	99,191	85,539	16%	187,605	162,864	15%
Retail and other revenues	30,919	27,355	13%	62,697	57,875	8%
Total revenues	600,111	439,482	37%	1,092,218	845,066	29%
Cost of goods sold	487,025	380,520	28%	907,119	745,280	22%
Gross margin (total revenues less cost of goods sold)	\$ 113,086	\$ 58,962	92%	\$ 185,099	\$ 99,786	85%
Gross margin (%)	18.8%	13.4%	40%	16.9%	11.8%	44%
Selling, general and administrative expense	\$ 54,142	\$ 46,426	17%	\$ 104,048	\$ 93,200	12%
Diluted earnings (loss) per share from continuing operations attributable to SSI shareholders:						
Reported	\$ 1.54	\$ 0.14	1,000%	\$ 2.05	\$ (0.11)	NM
Adjusted ⁽²⁾	\$ 1.51	\$ 0.31	387%	\$ 2.09	\$ 0.14	1,393%
Net income (loss)	\$ 45,679	\$ 4,504	914%	\$ 60,743	\$ (2,061)	NM
Adjusted EBITDA ⁽²⁾	\$ 71,411	\$ 28,265	153%	\$ 111,666	\$ 38,100	193%
Average ferrous recycled metal sales prices (\$/LT) ⁽³⁾ :						
Domestic	\$ 349	\$ 244	43%	\$ 297	\$ 222	34%
Foreign	\$ 399	\$ 258	55%	\$ 334	\$ 243	37%
Average	\$ 387	\$ 255	52%	\$ 326	\$ 235	39%
Ferrous volumes (LT, in thousands):						
Domestic ⁽⁴⁾	391	379	3%	779	743	5%
Foreign	586	609	(4)%	1,251	1,221	2%
Total ferrous volumes (LT, in thousands) ⁽⁴⁾	977	988	(1)%	2,030	1,964	3%
Average nonferrous sales price (\$/pound) ⁽³⁾⁽⁵⁾	\$ 0.83	\$ 0.55	51%	\$ 0.74	\$ 0.55	35%
Nonferrous volumes (pounds, in thousands) ⁽⁴⁾⁽⁵⁾	135,899	124,342	9%	274,135	268,518	2%
Finished steel average sales price (\$/ST) ⁽³⁾	\$ 690	\$ 627	10%	\$ 656	\$ 635	3%
Finished steel sales volumes (ST, in thousands)	136	129	6%	270	242	11%
Cars purchased (in thousands) ⁽⁶⁾	80	85	(6)%	158	168	(6)%
Number of auto parts stores at period end	50	51	(2)%	50	51	(2)%
Rolling mill utilization ⁽⁷⁾	88%	72%	22%	93%	79%	18%

NM = Not Meaningful

LT = Long Ton, which is equivalent to 2,240 pounds. ST = Short Ton, which is equivalent to 2,000 pounds.

- (1) Steel revenues include primarily sales of finished steel products, semi-finished goods (billets) and steel manufacturing scrap.
- (2) See the reconciliations of Non-GAAP Financial Measures at the end of this Item 2.
- (3) Price information is shown after netting the cost of freight incurred to deliver the product to the customer.
- (4) Ferrous and nonferrous volumes sold externally and delivered to our steel mill for finished steel production.
- (5) Average sales price and volume information excludes platinum group metals ("PGMs") in catalytic converters.
- (6) Cars purchased by auto parts stores only.
- (7) Rolling mill utilization is based on effective annual production capacity under current conditions of 580 thousand tons of finished steel products.

SCHNITZER STEEL INDUSTRIES, INC.

Revenues

Revenues in the second quarter and first six months of fiscal 2021 increased by 37% and 29%, respectively, compared to the same periods in the prior year primarily due to significantly higher average net selling prices for our ferrous and nonferrous products in both export and domestic markets. These increases were driven by stronger market conditions for recycled metals globally, including periods of sharply rising selling prices that reached multi-year highs for certain recycled metal commodities during the second quarter of fiscal 2021. In the second quarter and first six months of fiscal 2021, the average net selling price for our ferrous products increased by 52% and 39%, respectively, and the average net selling price for our nonferrous products increased by 51% and 35%, respectively, compared to the prior year periods. Nonferrous sales volumes for the second quarter and first six months of fiscal 2021 increased by 9% and 2%, respectively, compared to the prior year periods reflecting stronger demand partially offset by the effects of a shortage of available shipping containers that impacted the timing of shipments. Ferrous sales volumes in the second quarter of fiscal 2021 declined marginally compared to the prior year quarter primarily due to weather-related delays that impacted the timing of shipments. Market conditions for our finished steel products also improved in the second quarter and first six months of fiscal 2021, which contributed to higher finished steel average selling prices and sales volumes compared to the prior year periods, and reflected steady demand in West Coast construction markets and higher rolling mill utilization.

Operating Performance

Net income in the second quarter and first six months of fiscal 2021 was \$46 million and \$61 million, respectively, compared to net income of \$5 million and net loss of \$2 million, respectively, in the prior year periods. Adjusted EBITDA in the second quarter and first six months of fiscal 2021 was \$71 million and \$112 million, respectively, compared to \$28 million and \$38 million, respectively, in the prior year periods. The improvement in our results for the second quarter and first six months of fiscal 2021 reflected substantial benefits from the higher price environment for most of our products including a significant expansion in our ferrous metal spreads and a favorable impact from average inventory accounting, as well as increased nonferrous and finished steel sales volumes, compared to the prior year periods. Ferrous metal spreads in the second quarter and first six months of fiscal 2021 increased by approximately 45% and 25%, respectively, and average net selling prices for our nonferrous joint products that are recovered from the shredding process, comprising primarily zorba, increased by approximately 60% and 45%, respectively, compared to the prior year periods. Our results in the second quarter and first six months of fiscal 2021 also reflected increased contributions from sales of higher priced PGM products compared to the prior year periods and achievement of the full run rate of benefits from productivity initiatives implemented throughout fiscal 2020. In comparison, the lower price environment in the first half of fiscal 2020, which included a sharp decline in commodity prices during most of the first quarter of fiscal 2020 before recovering moderately in the second quarter, adversely impacted ferrous metal margins, the supply of scrap metal including end-of-life vehicles, processed volumes and overall operating results. Selling, general and administrative expense in the second quarter and first six months of fiscal 2021 increased by 17% and 12%, respectively, compared to the prior year periods primarily due to higher incentive compensation accruals aligned with improved business performance. See the reconciliation of adjusted EBITDA in Non-GAAP Financial Measures at the end of this Item 2.

In fiscal 2020, we implemented productivity initiatives aimed at reducing our annual operating expenses, mainly through reductions in non-trade procurement spend, including outside and professional services, lower employee-related expenses and other non-headcount measures. We targeted \$20 million in annual benefits from these initiatives, and we achieved the full run rate of benefits in the second quarter and first half of fiscal 2021. We achieved approximately \$4 million and \$6 million in realized benefits in the second quarter and first six months of fiscal 2020, respectively.

In the first quarter of fiscal 2021, in accordance with our plan announced in April 2020, we completed the transition to a new internal organizational and reporting structure reflecting a functionally-based, integrated model. This change in structure has resulted in a more agile organization and solidified achievement of recent productivity improvements and cost reduction initiatives.

Income Tax

The effective tax rate from continuing operations for the second quarter and first six months of fiscal 2021 was an expense on pre-tax income of 20.1% and 22.1%, respectively, compared to an expense on pre-tax income of 28.2% and a benefit on pre-tax loss of 26.8%, respectively, for the comparable prior year periods. The effective tax rate from continuing operations for the second quarter and first six months of fiscal 2021 was lower than that for the comparable prior year periods primarily due to the benefit from the foreign derived intangible income deduction in fiscal 2021 and the effects of higher pre-tax income compared to the prior year periods. The effective tax rate from continuing operations for the second quarter and first six months of fiscal 2020 was higher than the U.S. federal statutory rate of 21% primarily due to the impact of non-deductible officers' compensation and other expenses, as well as the aggregate impact of state taxes, on the projected annual effective tax rate applied to the quarterly results.

SCHNITZER STEEL INDUSTRIES, INC.

Liquidity and Capital Resources

We rely on cash provided by operating activities as a primary source of liquidity, supplemented by current cash on hand and borrowings under our existing credit facilities.

Sources and Uses of Cash

We had cash balances of \$11 million and \$18 million as of February 28, 2021 and August 31, 2020, respectively. Cash balances are intended to be used primarily for working capital, capital expenditures, dividends, share repurchases, investments and acquisitions. We use excess cash on hand to reduce amounts outstanding under our credit facilities. As of February 28, 2021, debt was \$171 million compared to \$104 million as of August 31, 2020, and debt, net of cash, was \$159 million as of February 28, 2021 compared to \$87 million as of August 31, 2020 (refer to Non-GAAP Financial Measures at the end of this Item 2).

Operating Activities

Net cash used in operating activities in the first six months of fiscal 2021 was \$3 million, compared to net cash provided by operating activities of \$17 million in the first six months of fiscal 2020.

Sources of cash other than from earnings in the first six months of fiscal 2021 included a \$45 million increase in accounts payable primarily due to higher raw material purchase prices and the timing of payments, and a \$16 million increase in income tax accruals. Uses of cash in the first six months of fiscal 2021 included a \$90 million increase in inventories due to higher raw material purchase prices, higher volumes on hand and the timing of purchases and sales, and a \$76 million increase in accounts receivable primarily due to increases in selling prices for recycled metals and finished steel as well as the timing of sales and collections.

Sources of cash in the first six months of fiscal 2020 included a \$9 million decrease in inventories due to lower raw material purchase prices and the timing of purchases and sales. Uses of cash in the first six months of fiscal 2020 included a \$18 million increase in accounts receivable primarily due to the timing of sales and collections, a \$8 million decrease in accounts payable primarily due to lower raw material purchase prices and the timing of payments, and a \$7 million decrease in accrued payroll and related liabilities primarily due to the payment of incentive compensation previously accrued for under our fiscal 2019 plans.

Investing Activities

Net cash used in investing activities was \$54 million in the first six months of fiscal 2021, compared to \$36 million in the first six months of fiscal 2020.

Cash used in investing activities in the first six months of fiscal 2021 included capital expenditures of \$55 million to upgrade our equipment and infrastructure and for investments in advanced metals recovery technology and environmental and safety-related assets, compared to \$37 million in the prior year period.

Financing Activities

Net cash provided by financing activities in the first six months of fiscal 2021 was \$50 million, compared to \$17 million in the first six months of fiscal 2020.

Cash flows from financing activities in the first six months of fiscal 2021 included \$66 million in net borrowings of debt, compared to \$36 million in the prior year period (refer to Non-GAAP Financial Measures at the end of this Item 2). Uses of cash in the first six months of fiscal 2021 and 2020 included \$11 million for the payment of dividends. Cash used in financing activities in the first six months of fiscal 2020 included \$1 million for share repurchases.

SCHNITZER STEEL INDUSTRIES, INC.

Debt

Our senior secured revolving credit facilities, which provide for revolving loans of \$700 million and C\$15 million, mature in August 2023 pursuant to a credit agreement with Bank of America, N.A., as administrative agent, and other lenders party thereto. Interest rates on outstanding indebtedness under the credit agreement are based, at our option, on either the London Interbank Offered Rate (“LIBOR”) (or the Canadian equivalent for C\$ loans), plus a spread of between 1.25% and 3.50%, with the amount of the spread based on a pricing grid tied to our ratio of consolidated funded debt to EBITDA (as defined by the credit agreement), or the greater of (a) the prime rate, (b) the federal funds rate plus 0.50% or (c) the daily rate equal to one-month LIBOR plus 1.75%, in each case, plus a spread of between 0.00% and 2.50% based on a pricing grid tied to our consolidated funded debt to EBITDA ratio. In addition, commitment fees are payable on the unused portion of the credit facilities at rates between 0.20% and 0.50% based on a pricing grid tied to our ratio of consolidated funded debt to EBITDA.

We had borrowings outstanding under our credit facilities of \$157 million as of February 28, 2021 and \$90 million as of August 31, 2020, with the increase relating primarily to funding working capital and capital expenditures. The weighted average interest rate on amounts outstanding under our credit facilities was 2.02% and 4.59% as of February 28, 2021 and August 31, 2020, respectively.

We use the credit facilities to fund working capital, capital expenditures, dividends, share repurchases, investments and acquisitions. Our credit agreement contains various representations and warranties, events of default and financial and other customary covenants which limit (subject to certain exceptions) our ability to, among other things, incur or suffer to exist certain liens, make investments, incur or guaranty additional indebtedness, enter into consolidations, mergers, acquisitions, and sales of assets, make distributions and other restricted payments, change the nature of our business, engage in transactions with affiliates and enter into restrictive agreements, including agreements that restrict the ability of our subsidiaries to make distributions. The financial covenants under the credit agreement include (a) a consolidated fixed charge coverage ratio, defined as the four-quarter rolling sum of consolidated EBITDA less defined maintenance capital expenditures and certain environmental expenditures divided by consolidated fixed charges, (b) a consolidated leverage ratio, defined as consolidated funded indebtedness divided by the sum of consolidated net worth and consolidated funded indebtedness, and (c) a consolidated asset coverage ratio, defined as consolidated asset values divided by consolidated funded indebtedness.

As of February 28, 2021, we were in compliance with the financial covenants under our credit agreement. The consolidated fixed charge coverage ratio was required to be no less than 1.10 to 1.00 and was 4.47 to 1.00 as of February 28, 2021. The consolidated leverage ratio was required to be no more than 0.55 to 1.00 and was 0.20 to 1.00 as of February 28, 2021. The consolidated asset coverage ratio was required to be no less than 1.00 to 1.00 and was 2.39 to 1.00 as of February 28, 2021.

Our obligations under our credit agreement are guaranteed by substantially all of our subsidiaries. The credit facilities and the related guarantees are secured by senior first priority liens on certain of our and our subsidiaries’ assets, including equipment, inventory and accounts receivable.

While we currently expect to remain in compliance with the financial covenants under the credit agreement, we may not be able to do so in the event market conditions, COVID-19 or other negative factors have a significant adverse impact on our results of operations and financial position. If we do not maintain compliance with our financial covenants and are unable to obtain an amendment or waiver from our lenders, a breach of a financial covenant would constitute an event of default and allow the lenders to exercise remedies under the agreements, the most severe of which is the termination of the credit facility under our committed bank credit agreement and acceleration of the amounts owed under the agreement. In such case, we would be required to evaluate available alternatives and take appropriate steps to obtain alternative funds. We cannot assure that any such alternative funds, if sought, could be obtained or, if obtained, would be adequate or on acceptable terms.

Other debt obligations, which totaled \$7 million as of each of February 28, 2021 and August 31, 2020, primarily relate to an equipment purchase, the contract consideration for which includes an obligation to make future monthly payments to the vendor in the form of licensing fees. For accounting purposes, such obligation is treated as a partial financing of the purchase price by the equipment vendor. Monthly payments commence when the equipment is placed in service and continue for a period of four years thereafter.

SCHNITZER STEEL INDUSTRIES, INC.

Capital Expenditures

Capital expenditures totaled \$55 million for the first six months of fiscal 2021, compared to \$37 million for the prior year period. We currently plan to invest up to \$120 million in capital expenditures in fiscal 2021, including approximately \$55 million for investments in growth, including new nonferrous processing technologies, support for volume initiatives and other growth projects, using cash generated from operations and available credit facilities. The COVID-19 pandemic has contributed to some delays in construction activities and equipment deliveries related to our capital projects, and to the time required to obtain permits from government agencies, resulting in the deferral of certain capital expenditures. Given the continually evolving nature of the COVID-19 pandemic and other factors impacting the timing of project completion, the extent to which forecasted capital expenditures could be deferred is uncertain.

Environmental Compliance

Building on our commitment to recycling and operating our business in an environmentally responsible manner, we continue to invest in facilities that improve our environmental presence in the communities in which we operate. As part of our capital expenditures discussed in the prior paragraph, we invested approximately \$7 million in capital expenditures for environmental projects in the first six months of fiscal 2021, and we currently plan to invest up to \$25 million for such projects in fiscal 2021. These projects include investments in storm water systems and equipment to ensure ongoing compliance with air quality and other environmental regulations.

We have been identified by the United States Environmental Protection Agency as one of the potentially responsible parties that own or operate or formerly owned or operated sites which are part of or adjacent to the Portland Harbor Superfund site (the "Site"). See Note 4 - Commitments and Contingencies in the Notes to the Unaudited Condensed Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of this matter, as well as other legacy environmental loss contingencies. We believe it is not possible to reasonably estimate the amount or range of costs which we are likely to or which it is reasonably possible that we will incur in connection with the Site, although such costs could be material to our financial position, results of operations, cash flows and liquidity. We have insurance policies that we believe will provide reimbursement for costs we incur for defense, remediation and mitigation for natural resource damages claims in connection with the Site, although there are no assurances that those policies will cover all of the costs which we may incur. Significant cash outflows in the future related to the Site and other environmental matters could reduce the amounts available for borrowing that could otherwise be used for working capital, capital expenditures, dividends, share repurchases, investments and acquisitions and could result in our failure to maintain compliance with certain covenants in our debt agreements, and could adversely impact our liquidity.

Dividends

On January 7, 2021, our Board of Directors declared a dividend for the second quarter of fiscal 2021 of \$0.1875 per common share, which equates to an annual cash dividend of \$0.75 per common share. The dividend totaling \$5 million was paid on February 1, 2021.

Share Repurchase Program

Pursuant to our share repurchase program as amended in 2001, 2006 and 2008, we were authorized to repurchase up to nine million shares of our Class A common stock. As of February 28, 2021, we had authorization to repurchase up to a remaining 706 thousand shares of our Class A common stock when we deem such repurchases to be appropriate. We may repurchase our common stock for a variety of reasons, such as to optimize our capital structure and to offset dilution related to share-based compensation arrangements. We consider several factors in determining whether to make share repurchases including, among other things, our cash needs, the availability of funding, our future business plans and the market price of our stock. We did not repurchase our common stock during the first half of fiscal 2021.

Assessment of Liquidity and Capital Resources

Historically, our available cash resources, internally generated funds, credit facilities and equity offerings have financed our acquisitions, capital expenditures, working capital and other financing needs.

We generally believe our current cash resources, internally generated funds, existing credit facilities and access to the capital markets will provide adequate short-term and long-term liquidity needs for working capital, capital expenditures, dividends, share repurchases, investments and acquisitions, joint ventures, debt service requirements, environmental obligations and other contingencies. However, in the event of a sustained market deterioration, we may need additional liquidity, which would require us to evaluate available alternatives and take appropriate steps to obtain sufficient additional funds. There can be no assurances that any such supplemental funding, if sought, could be obtained or, if obtained, would be adequate or on acceptable terms.

SCHNITZER STEEL INDUSTRIES, INC.

Off-Balance Sheet Arrangements

None requiring disclosure pursuant to Item 303 of Regulation S-K under the Securities Exchange Act of 1934.

Contractual Obligations

There were no material changes related to contractual obligations and commitments from the information provided in our Annual Report on Form 10-K for the fiscal year ended August 31, 2020.

We maintain stand-by letters of credit to provide support for certain obligations, including workers' compensation and performance bonds. As of February 28, 2021, we had \$8 million outstanding under these arrangements.

Critical Accounting Policies and Estimates

There were no material changes to our critical accounting policies and estimates as described in the "Management's Discussion and Analysis of Financial Condition and Results of Operations" section of our Annual Report on Form 10-K for the year ended August 31, 2020.

Recently Issued Accounting Standards

We have not identified any recent accounting pronouncements that are expected to have a material impact on our financial condition, results of operations or cash flows upon adoption.

Non-GAAP Financial Measures

Debt, net of cash

Debt, net of cash is the difference between (i) the sum of long-term debt and short-term borrowings (i.e., total debt) and (ii) cash and cash equivalents. We believe that presenting debt, net of cash is useful to investors as a measure of our leverage, as cash and cash equivalents can be used, among other things, to repay indebtedness.

The following is a reconciliation of debt, net of cash (in thousands):

	February 28, 2021	August 31, 2020
Short-term borrowings	\$ 2,372	\$ 2,184
Long-term debt, net of current maturities	168,441	102,235
Total debt	170,813	104,419
Less cash and cash equivalents	11,326	17,887
Total debt, net of cash	\$ 159,487	\$ 86,532

Net borrowings (repayments) of debt

Net borrowings (repayments) of debt is the sum of borrowings from long-term debt and repayments of long-term debt. We present this amount as the net change in borrowings (repayments) for the period because we believe it is useful to investors as a meaningful presentation of the change in debt.

The following is a reconciliation of net borrowings (repayments) of debt (in thousands):

	Six Months Ended	
	February 28, 2021	February 29, 2020
Borrowings from long-term debt	\$ 265,645	\$ 244,382
Repayments of long-term debt	(199,229)	(208,614)
Net borrowings (repayments) of debt	\$ 66,416	\$ 35,768

SCHNITZER STEEL INDUSTRIES, INC.

Adjusted EBITDA, adjusted selling, general and administrative expense, adjusted income (loss) from continuing operations attributable to SSI shareholders, and adjusted diluted earnings (loss) per share from continuing operations attributable to SSI shareholders

Management believes that providing these non-GAAP financial measures adds a meaningful presentation of our results from business operations excluding adjustments for restructuring charges and other exit-related activities, legacy environmental matters (net of recoveries), business development costs not related to ongoing operations, asset impairment charges, and the income tax expense (benefit) allocated to these adjustments, items which are not related to underlying business operational performance, and improves the period-to-period comparability of our results from business operations.

Following are reconciliations of net income (loss) to adjusted EBITDA, and adjusted selling, general and administrative expense (in thousands):

	Three Months Ended		Six Months Ended	
	February 28, 2021	February 29, 2020	February 28, 2021	February 29, 2020
Reconciliation of adjusted EBITDA:				
Net income (loss)	\$ 45,679	\$ 4,504	\$ 60,743	\$ (2,061)
(Income) loss from discontinued operations, net of tax	(30)	(1)	12	(29)
Interest expense	1,224	1,320	3,004	2,743
Income tax expense (benefit)	11,469	1,770	17,188	(764)
Depreciation and amortization	14,469	14,385	29,295	28,472
Restructuring charges and other exit-related activities	814	4,633	878	5,100
(Recoveries) charges for legacy environmental matters, net ⁽¹⁾	(2,214)	451	546	1,744
Business development costs	—	801	—	801
Asset impairment charges	—	402	—	2,094
Adjusted EBITDA	\$ 71,411	\$ 28,265	\$ 111,666	\$ 38,100
Selling, general and administrative expense:				
As reported	\$ 54,142	\$ 46,426	\$ 104,048	\$ 93,200
Recoveries (charges) for legacy environmental matters, net ⁽¹⁾	2,214	(451)	(546)	(1,744)
Business development costs	—	(801)	—	(801)
Adjusted	\$ 56,356	\$ 45,174	\$ 103,502	\$ 90,655

(1) Legal and environmental charges, net of recoveries, for legacy environmental matters including those related to the Portland Harbor Superfund site and to other legacy environmental loss contingencies. See Note 4 - Commitments and Contingencies, "Portland Harbor" and "Other Legacy Environmental Loss Contingencies" in the Notes to the Unaudited Condensed Consolidated Financial Statements in Part I, Item 1 of this report.

SCHNITZER STEEL INDUSTRIES, INC.

Following are reconciliations of adjusted income (loss) from continuing operations attributable to SSI shareholders and adjusted diluted earnings (loss) per share from continuing operations attributable to SSI shareholders (in thousands, except per share data):

	Three Months Ended		Six Months Ended	
	February 28, 2021	February 29, 2020	February 28, 2021	February 29, 2020
Income (loss) from continuing operations attributable to SSI shareholders:				
As reported	\$ 44,558	\$ 3,882	\$ 58,704	\$ (3,141)
Restructuring charges and other exit-related activities	814	4,633	878	5,100
(Recoveries) charges for legacy environmental matters, net ⁽¹⁾	(2,214)	451	546	1,744
Business development costs	—	801	—	801
Asset impairment charges	—	402	—	2,094
Income tax expense (benefit) allocated to adjustments ⁽²⁾	334	(1,464)	(315)	(2,615)
Adjusted	<u>\$ 43,492</u>	<u>\$ 8,705</u>	<u>\$ 59,813</u>	<u>\$ 3,983</u>
Diluted earnings (loss) per share from continuing operations attributable to SSI shareholders:				
As reported	\$ 1.54	\$ 0.14	\$ 2.05	\$ (0.11)
Restructuring charges and other exit-related activities, per share	0.03	0.16	0.03	0.18
(Recoveries) charges for legacy environmental matters, net, per share ⁽¹⁾	(0.08)	0.02	0.02	0.06
Business development costs, per share	—	0.03	—	0.03
Asset impairment charges, per share	—	0.01	—	0.08
Income tax expense (benefit) allocated to adjustments, per share ⁽²⁾	0.01	(0.05)	(0.01)	(0.09)
Adjusted ⁽³⁾	<u>\$ 1.51</u>	<u>\$ 0.31</u>	<u>\$ 2.09</u>	<u>\$ 0.14</u>

- (1) Legal and environmental charges, net of recoveries, for legacy environmental matters including those related to the Portland Harbor Superfund site and to other legacy environmental loss contingencies. See Note 4 - Commitments and Contingencies, "Portland Harbor" and "Other Legacy Environmental Loss Contingencies" in the Notes to the Unaudited Condensed Consolidated Financial Statements in Part I, Item 1 of this report.
- (2) Income tax allocated to the aggregate adjustments reconciling reported and adjusted income (loss) from continuing operations attributable to SSI shareholders and diluted earnings (loss) per share from continuing operations attributable to SSI shareholders is determined based on a tax provision calculated with and without the adjustments.
- (3) May not foot due to rounding.

SCHNITZER STEEL INDUSTRIES, INC.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Commodity Price Risk

We are exposed to commodity price risk, mainly associated with variations in the market price for ferrous and nonferrous metals, including scrap metal, finished steel products, auto bodies and other commodities. The timing and magnitude of industry cycles are difficult to predict and are impacted by general economic conditions. We respond to increases and decreases in forward selling prices by adjusting purchase prices. We actively manage our exposure to commodity price risk and monitor the actual and expected spread between forward selling prices and purchase costs and processing and shipping expense. Sales contracts are based on prices negotiated with our customers, and generally orders are placed 30 to 60 days ahead of the shipment date. However, financial results may be negatively impacted when forward selling prices fall more quickly than we can adjust purchase prices or when customers fail to meet their contractual obligations. We assess the net realizable value of inventory (“NRV”) each quarter based upon contracted sales orders and estimated future selling prices. Based on contracted sales and estimates of future selling prices, a 10% decrease in the selling price of inventory would not have had a material NRV impact as of February 28, 2021.

Interest Rate Risk

There have been no material changes to our disclosure regarding interest rate risk set forth in Item 7A. Quantitative and Qualitative Disclosures About Market Risk included in our Annual Report on Form 10-K for the year ended August 31, 2020.

Credit Risk

Credit risk relates to the risk of loss that might occur as a result of non-performance by counterparties of their contractual obligations to take delivery of scrap metal and finished steel products and to make financial settlements of these obligations, or to provide sufficient quantities of scrap metal or payment to settle advances, loans and other contractual receivables in connection with demolition and scrap extraction projects. We manage our exposure to credit risk through a variety of methods, including shipping ferrous scrap metal exports under letters of credit, collection of deposits prior to shipment for certain nonferrous export customers, establishment of credit limits for certain sales on open terms, credit insurance and designation of collateral and financial guarantees securing advances, loans and other contractual receivables. Due in part to the effects of COVID-19, we have experienced reductions in the availability of credit insurance that we have historically used to cover a portion of our recycled metal and finished steel sales to domestic customers, which reduced availability may increase our exposure to customer credit risk.

Historically, we have shipped almost all of our large shipments of ferrous scrap metal to foreign customers under contracts supported by letters of credit issued or confirmed by banks deemed creditworthy. The letters of credit ensure payment by the customer. As we generally sell export recycled ferrous metal under contracts or orders that generally provide for shipment within 30 to 60 days after the price is agreed, our customers typically do not have difficulty obtaining letters of credit from their banks in periods of rising ferrous prices, as the value of the letters of credit are collateralized by the value of the inventory on the ship. However, in periods of significantly declining prices, our customers may not be able to obtain letters of credit for the full sales value of the inventory to be shipped.

As of each of February 28, 2021 and August 31, 2020, 40% of our accounts receivable balance was covered by letters of credit. Of the remaining balance, 98% was less than 60 days past due as of each of February 28, 2021 and August 31, 2020.

Foreign Currency Exchange Rate Risk

We are exposed to foreign currency exchange rate risk, mainly associated with sales transactions and related accounts receivable denominated in the U.S. Dollar by our Canadian subsidiary with a functional currency of the Canadian Dollar. In certain instances, we may use derivatives to manage some portion of this risk. As of February 28, 2021 and August 31, 2020, we did not have any derivative contracts.

SCHNITZER STEEL INDUSTRIES, INC.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities and Exchange Act of 1934, as amended (the “Exchange Act”)) that are designed to ensure that information we are required to disclose in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission’s rules and forms and that such information is accumulated and communicated to management, including the Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures. Any controls and procedures, no matter how well designed and operated, can only provide reasonable assurance of achieving the desired control objectives. Our management, with the participation of the Chief Executive Officer and Chief Financial Officer, has completed an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of February 28, 2021, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control Over Financial Reporting

There was no change in our internal control over financial reporting (as that term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ended February 28, 2021, that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

SCHNITZER STEEL INDUSTRIES, INC.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

Information regarding reportable legal proceedings is contained in Part I, “Item 3. Legal Proceedings” in our Annual Report on Form 10-K for the fiscal year ended August 31, 2020; in Part II, “Item 1. Legal Proceedings” in our Quarterly Report on Form 10-Q for the quarterly period ended November 30, 2020; and below in this Part II, “Item 1. Legal Proceedings” of this Quarterly Report on Form 10-Q. Also see Note 4 - Commitments and Contingencies in the Notes to the Unaudited Condensed Consolidated Financial Statements in Part I, Item I, incorporated by reference herein.

As previously reported, we had reached agreement with the Alameda County District Attorney and the California Office of the Attorney General (COAG), the latter on behalf of certain state agencies, to settle certain alleged violations of environmental requirements at one of our operations in California stemming from investigations initiated in 2013 and inspections conducted in 2015. The settlement provided for \$2.05 million for civil penalties and reimbursement of the agencies’ enforcement costs and \$2.05 million to fund Supplemental Environmental Projects in the local community to promote public health and the environment. On February 3, 2021, a stipulation and consent order was filed in and approved by the Alameda County Superior Court of the State of California. The monetary payments pursuant to the settlement were made in March 2021. On February 23, 2021, the California State Department of Toxic Substance Control (DTSC), one of the state agencies involved in the investigations and settlement, issued a corrective action enforcement order that would require us to submit a current conditions report, to undertake a facilities investigation, risk assessment and corrective measures study, and to implement corrective measures selected by the DTSC based on those assessments and studies. We dispute DTSC’s alleged jurisdictional basis for the order, as well as the scope of work required by the order, which we believe is unwarranted and duplicative of ongoing assessments being conducted under the oversight of another state agency. We have filed a notice of defense that by law stays the effectiveness of the order and are challenging the order through the DTSC administrative process.

In addition, the DTSC issued a similar corrective action enforcement order on March 18, 2021 with respect to our metal recycling facility in Fresno, California based on inspections conducted by the DTSC in 2013. That 2013 inspection is the basis for the previously reported enforcement matter brought by the COAG, on behalf of DTSC, that was filed in the Superior Court of the State of California, County of Fresno in June 2020. We dispute DTSC’s alleged jurisdictional basis for the recent order, as well as the scope of work required by that order. We have also filed a notice of defense in this matter that by law stays the effectiveness of the order and are challenging the order through the DTSC administrative process.

In addition, as previously reported, we have been in discussions with the District Attorneys for six counties in California in connection with a joint investigation into alleged violations of environmental requirements at various Pick-n-Pull locations within California. We have implemented additional compliance measures at all operating Pick-n-Pull locations in the state and expect to negotiate a state-wide settlement of this matter that will address the concerns raised in this joint investigation. Based on the settlement discussions to date and the program improvements we have implemented, we do not believe that the outcome of this matter will be material to our financial position, results of operations, cash flows or liquidity.

On March 23, 2021, the California Superior Court for the County of Alameda issued an order in a case filed on August 5, 2020 by The Athletics Investment Group LLC against the DTSC as Respondent and the Company as Real Party in Interest seeking a writ of mandate commanding the DTSC to rescind the “f letter” issued to the Company’s metal shredding facility in California. Pursuant to determinations under section 66260.200(f) of the state hazardous waste regulations issued in 1988 and 1989 (the “f letters”), the DTSC determined that treated shredder waste from the Company’s facility does not pose a significant hazard to human health, safety or the environment and therefore classified the waste as a “nonhazardous waste” which among other things permits its use as alternative daily cover at municipal landfills. The court in its order concluded that, under a law enacted by the legislature in 2014, the DTSC had a mandatory duty to rescind the “f letters” and granted the petition for writ of mandate. The court reached this decision despite a determination by DTSC in 2018 pursuant to the 2014 statute that treated shredder residue does not need to be managed as a hazardous waste in order to protect human health, safety or the environment. Separate orders implementing the court’s ruling have not yet been issued, and the timing and procedures for rescission of the “f letters,” as well as whether the DTSC will establish a workable alternative that will allow treated residue to continue to qualify as non-hazardous waste, remain uncertain. DTSC and the Company have 60 days from issuance of the order to provide a notice of appeal, which notice would result in an automatic stay of the order.

SCHNITZER STEEL INDUSTRIES, INC.

ITEM 1A. RISK FACTORS

There have been no material changes to our risk factors reported or new risk factors identified since the filing of our Annual Report on Form 10-K for the year ended August 31, 2020, except as follows:

Risk Factors Relating to Our Business

Reliance on third party shipping companies may restrict our ability to ship our products

We significantly rely on third parties to handle and transport raw materials to our production facilities and products to customers. Despite our practice of utilizing a diversified group of suppliers of transportation, factors beyond our control, including changes in fuel prices, political events, governmental regulation of transportation, changes in market rates, carrier availability, carrier bankruptcy, labor shortages, shipping industry consolidation and disruptions in transportation routes and infrastructure, may adversely impact our ability to ship our products and our operating margins. These impacts could include delays or other disruptions in shipments in transit, including as a result of congested seaports and travel routes, or third party shipping companies increasing their charges for transportation services or otherwise reducing or eliminating the availability of their containers, vehicles, rail cars, barges or ships. For example, during the second quarter of fiscal 2021, worldwide demand for logistical services increased sharply, which led to a global shortage of available shipping containers, congested seaports and higher freight rates, impacting the timing of certain shipments and resulting in reductions in sales volumes of certain products. The delays in container shipping for U.S. exports have been exacerbated by the backlog of containerized imports at U.S. seaports and the recent disruption in transit through the Suez Canal. While we aim to pass on the majority of shipping and related charges to our customers, there can be no assurance that we will be able to do so into the future. As a result, we may not be able to transport our products in a timely and cost-effective manner, which could have a material adverse effect on our financial condition and results of operations and may harm our reputation.

Risk Factors Relating to the Regulatory Environment

Governmental agencies may refuse to grant or renew our licenses and permits, thus restricting our ability to operate

We conduct certain of our operations subject to licenses, permits and approvals from state and local governments. Governmental agencies often resist the establishment of certain types of facilities in their communities, including metal recycling and auto parts facilities. Changes in zoning and increased residential and mixed-use development near our facilities are reducing the buffer zones and creating land use conflicts with heavy industrial uses such as ours. This could result in increased complaints, increased inspections and enforcement including fines and penalties, operating restrictions, the need for additional capital expenditures and increased opposition to maintaining or renewing required approvals, licenses and permits. In addition, waste products from our operations are subject to classification and regulation that, among other things, determine how such materials may be handled, stored, transported and disposed. Failure to obtain or maintain regulatory permits, approvals or exemptions for such waste could materially increase our costs or limit our operations.

In March 2021, for example, a state court in California determined that the state regulatory agency had a mandatory duty under a 2014 law to rescind the regulatory determinations pursuant to which treated metal shredder residue from our and other metal recycling facilities in the state has been classified as non-hazardous and safely used as alternative daily cover at landfills for over 30 years. See Part II, “Item 1. Legal Proceedings” in this Quarterly Report on Form 10-Q for further discussion of this matter. While implementation of the court’s decision is unclear at this point, failure to put in place a workable alternative that will allow such material to continue to qualify as non-hazardous waste or to identify other cost-effective disposal options or to overturn this decision on appeal could limit our operations in the state and could have a material adverse effect on our results of operations and on the metal shredding industry in California in general.

Furthermore, from time to time, both the U.S. and foreign governments impose regulations and restrictions on trade in the markets in which we operate. In some countries, governments require us to apply for certificates or registration before allowing shipment of recycled metal to customers in those countries. There can be no assurance that future approvals, licenses and permits will be granted or that we will be able to maintain and renew the approvals, licenses and permits we currently hold. Failure to obtain these approvals could cause us to limit or discontinue operations in these locations or prevent us from developing or acquiring new facilities, which could have a material adverse effect on our financial condition and results of operations.

ITEM 5. OTHER INFORMATION

None.

SCHNITZER STEEL INDUSTRIES, INC.

ITEM 6. EXHIBITS

<u>Exhibit Number</u>	<u>Exhibit Description</u>
10.1*	Summary Sheet of 2021 Non-Employee Director Compensation
10.2*	Separation and Release Agreement by and between the Registrant and Jeff Dyck, dated February 17, 2021
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	Inline XBRL Instance Document – the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document.
101.SCH	Inline XBRL Taxonomy Extension Schema Document
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibit 101)

*Management contract or compensatory plan or arrangement.

SCHNITZER STEEL INDUSTRIES, INC.

SIGNATURES

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

SCHNITZER STEEL INDUSTRIES, INC.
(Registrant)

Date: April 7, 2021

By: /s/ Tamara L. Lundgren

Tamara L. Lundgren
Chairman, President and Chief Executive Officer

Date: April 7, 2021

By: /s/ Richard D. Peach

Richard D. Peach
Executive Vice President, Chief Financial Officer and Chief Strategy Officer