

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

FORM 10-K

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

FOR THE FISCAL YEAR ENDED OCTOBER 31, 1999

OR

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

COMMISSION FILE NUMBER 1-5725

QUANEX CORPORATION  
(Exact name of registrant as specified in its charter)

DELAWARE  
(State or other jurisdiction of  
incorporation or organization)

38-1872178  
(I.R.S. Employer  
Identification No.)

1900 WEST LOOP SOUTH, SUITE 1500  
HOUSTON, TEXAS  
(Address of principal executive offices)

77027  
(Zip Code)

Registrant's telephone number, including area code (713) 961-4600

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

TITLE OF EACH CLASS -----	NAME OF EACH EXCHANGE ON WHICH REGISTERED -----
Common Stock, \$.50 par value	New York Stock Exchange, Inc.
Rights to Purchase Series A Junior Participating Preferred Stock	New York Stock Exchange, Inc.
6.88% Convertible Subordinated Debentures	New York Stock Exchange, Inc.

Securities registered pursuant to Section 12(g) of the Act: NONE

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

The aggregate market value of the registrant's voting stock held by  
non-affiliates as of December 31, 1999, computed by reference to the closing  
price for the Common Stock on the New York Stock Exchange, Inc. on that date,  
was \$358,765,289. Such calculation assumes only the registrant's officers and  
directors were affiliates of the registrant.

At December 31, 1999, there were outstanding 14,351,225 shares of the  
registrant's Common Stock, \$.50 par value.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's definitive Proxy Statement, to be filed with  
the Commission within 120 days of October 31, 1999, for its Annual Meeting of  
Stockholders to be held on February 23, 2000, are incorporated herein by  
reference in Items 10, 11, 12, and 13 of Part III of this Annual Report.

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## PART I

## ITEM 1. BUSINESS

## GENERAL

Quanex was organized in 1927 as a Michigan corporation under the name Michigan Seamless Tube Company. The Company reincorporated in Delaware in 1968 under the same name and then changed its name to Quanex Corporation in 1977. The Company's executive offices are located at 1900 West Loop South, Suite 1500, Houston, Texas 77027. References made to the "Company" or "Quanex" include Quanex Corporation and its subsidiaries unless the context indicates otherwise.

Quanex is a technological leader in the production of value-added engineered carbon and alloy steel bars, aluminum flat-rolled products, and precision-formed metal products. The Company uses state-of-the-art manufacturing technologies, low-cost production processes, and engineering and metallurgical expertise to provide customers with specialized products for specific applications. These capabilities also provide Quanex with unique competitive advantages.

The Company seeks to reduce the impact of cyclical economic downturns on its operations by serving diverse markets. These markets include the transportation industry, the industrial machinery and capital equipment industries, the homebuilding and remodeling industries, defense industries, and other commercial markets.

The Company's future growth strategy is focused on the continued penetration of higher margin markets, continued expansion of its aluminum and steel manufacturing operations, expansion of precision-formed, value-added metal products, and niche acquisitions.

In October 1998, Quanex completed the purchase of Decatur Aluminum Corporation, an aluminum sheet manufacturer in Decatur, Alabama, for approximately \$19 million. The newly acquired company, renamed Nichols Aluminum-Alabama, Inc. (Nichols Aluminum Alabama), includes cold rolling and finishing operations and a wide-width paint line that allows it to produce painted or coated aluminum sheet, a premium value-added product. This acquisition significantly expanded the aluminum mill sheet products segment's overall cold-rolling capacity, effectively utilizing most of the 400-million pounds of current casting capacity.

On December 15, 1999, the Company announced that it had signed a contract to acquire the assets of Alcoa's Fort Lupton, Colorado-based aluminum sheet production facility for \$8 million plus working capital value which is estimated at \$17 million. Consummation of the sale is subject to government approval.

The acquisition of the Fort Lupton mill will increase the casting, cold-finishing and value-added painting capacities of Nichols Aluminum, Quanex's aluminum sheet business. The Fort Lupton mill can produce more than 40-million pounds annually of high-grade aluminum sheet for a variety of applications, including beverage cans and other food packaging, home furnishing, and other consumer durable products.

The Company also has invested significantly in technologically advanced continuous manufacturing processes to meet demanding quality specifications and to achieve additional cost efficiencies. In its MACSTEEL operations, rotary centrifugal continuous casters are used with an in-line manufacturing process to produce bearing grade and aircraft quality, seam-free, engineered carbon and alloy steel bars that enable Quanex to participate in higher margin markets. Since 1992, the Company has invested more than \$169 million to enhance its steel manufacturing and refining processes, to improve rolling and finishing capability, and to expand manufacturing capacity at its MACSTEEL operations to approximately 620,000 tons per year. Phases I through IV of the MACSTEEL expansions have been completed. In Phase IV of these expansions, finished during 1999, the Company installed an additional cold finishing line at each of the MACSTEEL plants in Jackson, Michigan, and at Ft. Smith, Arkansas. This project doubled the shipping capacity of MACPLUS cold finished bars, a premium value-added product, to more than 180,000 tons annually. In October 1998, the Company announced its Phase V program, which will increase engineered steel bar shipping capacity by approximately 13% to 700,000 tons annually. Phase V also includes smaller projects at MACSTEEL Heat Treating, based in Huntington, Indiana, where a third processing line is being built, and at Kenosha, Wisconsin-based MACSTEEL NitroSteel, where efficiency enhancing equipment has been installed. Phase V is expected to be complete by year-end 2000.

In November 1998 the Aluminum Mill Sheet Products segment completed construction of two rotary furnaces and upgraded the gross processing equipment at its casting plant. The \$12 million expansion now allows the Company's Nichols Aluminum Division to use less costly scrap, resulting in lower raw material costs, improved yields of scrap to molten metal, and improved efficiency through more flexible operations.

The Company's businesses are managed on a decentralized basis. Each operating group has administrative, operating and marketing functions. Financial reporting systems measure each group's return on investment, and the Company seeks to reward superior performance with incentive compensation, which is a significant portion of total employee compensation. Intercompany sales are conducted on an arms-length basis. Operational activities and policies are managed by both corporate officers and key division executives. Also, a small corporate staff provides corporate accounting, financial and treasury management, tax, and human resource services to the operating divisions.

#### MANUFACTURING PROCESSES, MARKETS, AND PRODUCT SALES BY BUSINESS SEGMENT

The Company's operations are grouped into three business segments: (i) engineered steel bars, (ii) aluminum mill sheet products, and (iii) engineered products. General corporate expenses are classified as other operations.

Information with respect to major markets for the Company's products, expressed as a percentage of consolidated net sales, is shown under the heading "Sales by Major Markets" as set forth below. For financial information regarding each of Quanex's business segments, see "Management's Discussion and Analysis of Financial Condition and Results of Operations" herein and Note 13 to the Consolidated Financial Statements. Although Quanex has attempted to estimate its sales by product and market categories, many products have multiple end uses for several industries and sales are not recorded on the basis of product or market categories. A portion of sales is made to distributors who sell to different industries. Net sales by principal market are based upon the total dollar volume of customer invoices. For the year ended October 31, 1999, one customer, Autoliv Inc., accounted for 12% of Company sales.

Quanex operates 13 manufacturing facilities in eight states in the United States and one plant in Zwolle, The Netherlands. These facilities feature efficient plant design and flexible manufacturing processes, enabling the Company to produce a wide variety of products for various industries and applications. The Company is generally able to maintain minimal levels of finished goods inventories at most locations because it typically manufactures products to customer specifications upon order.

## SALES BY MAJOR MARKETS

MARKETS	MARKET DESCRIPTION	QUANEX PRODUCTS	SALES (\$ MILLIONS)				
			FISCAL YEAR ENDED OCTOBER 31,				
			1999	1998	1997	1996	1995
TRANSPORTATION	Auto/Truck	Steel bars, impact-extruded components, aluminum sheet	\$384.1 47.4%	\$352.9 44.2%	\$322.3 43.2%	\$207.2 33.4%	\$170.9 28.3%
	Other Transportation (including ship/railroad, recreational vehicles and military transportation)	Steel bars, treated tubes and bars, aluminum sheet	\$ 30.1 3.7%	\$ 31.8 4.0%	\$ 32.8 4.4%	\$ 22.0 3.6%	\$ 23.1 3.8%
	TOTAL TRANSPORTATION		\$414.2 51.1%	\$384.7 48.2%	\$355.1 47.6%	\$229.2 37.0%	\$194.0 32.1%
ALUMINUM BUILDING PRODUCTS	Residential and Commercial Building Materials, Other	Aluminum sheet, fabricated aluminum products, aluminum coil, coated aluminum coil	\$293.9 36.3%	\$334.8 42.0%	\$327.5 43.9%	\$313.1 50.5%	\$331.6 54.9%
INDUSTRIAL MACHINERY AND CAPITAL EQUIPMENT	General Industrial Machinery (including mining, agriculture and construction) Capital Equipment	Specialized forgings, impact-extruded products, steel bars	\$ 37.8 4.7%	\$ 29.9 3.8%	\$ 24.9 3.3%	\$ 47.4 7.6%	\$ 59.9 9.9%
	(including material handling, machine tools, and office/household)	Steel bars, treated bars and tubes, partition products, impact-extruded products	\$ 12.3 1.5%	\$ 10.4 1.3%	\$ 17.5 2.4%	\$ 22.0 3.6%	\$ 13.1 2.2%
	TOTAL INDUSTRIAL MACHINERY AND CAPITAL EQUIPMENT		\$ 50.1 6.2%	\$ 40.3 5.1%	\$ 42.4 5.7%	\$ 69.4 11.2%	\$ 73.0 12.1%
OTHER			\$ 51.9 6.4%	\$ 37.7 4.7%	\$ 21.1 2.8%	\$ 8.4 1.3%	\$ 5.4 .9%
	TOTAL SALES		\$810.1 100.0%	\$797.5 100.0%	\$746.1 100.0%	\$620.1 100.0%	\$604.0 100.0%

## Engineered Steel Bars

The Company's Engineered Steel Bars segment comprises engineered steel bar operations, steel bar and tube heat treating services, and steel bar and tube corrosion and wear resistant finishing services.

The Company's engineered steel bar operations are conducted through its MACSTEEL division, consisting of two plants located in Ft. Smith, Arkansas, and Jackson, Michigan. These plants manufacture hot finished, precision engineered, carbon and alloy steel bars. The Company believes that MACSTEEL has the only two plants in North America using continuous rotary centrifugal casting technology. This casting process produces seam-free bars, without surface defects or inclusions, thereby reducing the need for subsequent surface conditioning. The continuous casting and automated in-line manufacturing operations at the MACSTEEL plants substantially reduce labor and energy costs by eliminating the intermittent steps that characterize manufacturing operations at most larger, and particularly integrated steel mills. The Company typically sells only complete heat lots, or batches, which are made to specific customer requirements. Heat lots average 45 tons at the Jackson plant and 50 tons at the Ft. Smith plant.

MACSTEEL produces various grades of customized engineered steel bars by melting steel scrap and casting it in a rotary centrifugal continuous caster. MACSTEEL's molten steel is further processed through secondary refining processes that includes argon stirring, ladle injection, and vacuum arc degassing prior to casting. These processes enable MACSTEEL to produce higher quality, "cleaner" steels.

As a result of its state-of-the-art continuous manufacturing technology, which reduces labor, energy and process yield loss, the Company believes that MACSTEEL is one of the lowest cost producers of precision engineered carbon and alloy steel bars. The Company believes that energy costs at MACSTEEL are significantly lower than those of its competitors because its bars are moved directly from the caster to the rolling mill before cooling, eliminating the need for costly reheating. MACSTEEL's low unit labor costs are achieved with its highly automated manufacturing process, enabling it to produce finished steel bars using less than two man-hours of labor per ton compared with an estimated average of four to five man-hours per ton for U.S. integrated steel producers.

MACSTEEL products are custom manufactured for customers in the passenger car, light truck, sport utility vehicle (SUVs), heavy truck, anti-friction bearing, off-road and farm equipment, defense, capital equipment, and seamless tubular industries. These industries use engineered steel bars in critical applications such as camshafts, crankshafts, transmission gears, wheel spindles and hubs, bearing cages and rollers, steering components, hydraulic mechanisms and seamless tube production. Also, MACSTEEL engineered steel bars are used for the manufacture of components for safety critical steel air bag inflators at the Company's plant in New Albany, Mississippi.

Also included in the Engineered Steel Bars segment is a heat treating plant in Huntington, Indiana ("Heat Treat"), and a plant in Kenosha, Wisconsin, that improves the wear and corrosion resistance properties of steel bars and tubes ("NitroSteel").

The Heat Treat facility uses custom designed, in-line equipment to provide tube and bar heat treating and related services, such as quench and temper, stress relieving, normalizing, "cut-to-length", and metallurgical testing. This plant serves customers in the energy, automotive, ordnance and mining markets.

The NitroSteel plant processes steel bars and tubes using the patented Nitrotec treatment to improve corrosion and wear resistance while providing an environmentally friendly, non-toxic alternative to chrome plating. NitroSteel's products are made for specific customer applications and sold into fluid power markets.

## Aluminum Mill Sheet Products

The Company's Aluminum Mill Sheet Products segment comprises aluminum sheet continuous casting operations and cold rolling, annealing, painting, and other finishing operations through its Nichols Aluminum Division (Nichols).

Nichols manufactures mill finished and coated aluminum sheet for the home improvement, residential and light commercial construction, transportation, appliance, and service center markets. The division comprises four plants: a thin-slab casting and hot rolling mill (NAC) located in Davenport, Iowa, and three cold rolling and finishing plants located in Davenport, Iowa (NAD), Lincolnshire, Illinois (NAL), and Decatur, Alabama (NAA).

NAC's mini-mill uses a single, in-line casting process that can produce 400 million pounds of reroll (hot-rolled aluminum sheet) annually. The mini-mill converts aluminum scrap to sheet through melting, continuous casting, and in-line hot rolling processes. NAC has shredding and blending capabilities, including two rotary barrel furnaces, that broaden its sources of raw material and allow it to melt lower grades of scrap. Delacquering equipment improves the quality of the raw material before it reaches the melting furnaces by burning off combustibles in the scrap. Scrap is blended using computerized processes to most economically achieve the desired molten aluminum alloy composition. The molten metal flows into a Hazelett thin-slab caster, which casts an aluminum slab up to 52 inches wide and .75 inches thick. The slab is fed directly to a hot mill where three in-line rolling stands reduce the slab to gauges as thin as .045 inches. This hot rolling process substantially reduces subsequent cold rolling requirements. NAC also has an efficient, in-house dross recovery system to improve raw material yields.

The Company believes the combination of capacity increases and technological enhancements directed at producing higher quality reroll results in a significant manufacturing advantage with savings derived from reduced raw material costs, optimized scrap utilization, reduced unit energy cost, reduced cold rolling requirements and lower labor costs.

Further processing of the reroll occurs at the NAD, NAL or NAA plants, where customers' specific product requirements can be met through cold rolling to various gauges, annealing for additional mechanical and formability properties, tension leveling to improve the flatness of the sheet, and slitting to specific widths. Products at the NAD and NAA plants can also be custom painted, an important value-added feature for the applications of certain customers in building products, transportation, and appliance markets.

#### Engineered Products

The Company's Engineered Products segment consists of impact extrusion operations for primarily aluminum and steel products, which are produced at Piper Impact facilities, and aluminum and steel fabrication operations conducted at the Fabricated Products Division.

The Piper Impact division comprises Piper Impact, which includes two impact-extrusion facilities in New Albany, Mississippi, dedicated to steel and aluminum products, and Piper Impact Europe, with an aluminum impact-extrusion facility in Zwolle, The Netherlands. Fabricated Products comprises the AMSCO plant in Rice Lake, Wisconsin, and two Homeshield Fabricated Products ("HFP") plants in Chatsworth, Illinois, that manufacture precision-formed metal products.

Piper Impact and Piper Impact Europe are technological leaders in the manufacture of custom designed, impact extruded aluminum and steel parts for transportation, electronics, defense, and other commercial applications. Piper Impact's operations use impact extrusion technology to produce highly engineered, near-net shaped components from aluminum and steel bar slugs. The pressure resulting from the impact of the extrusion presses causes metal to flow into the desired shape. This cost efficient, cold-forming of the metal results in a high quality, work hardened product with a superior finish. Products may be further processed with heat treating and precision machining. The parts are then delivered to customers' assembly lines, requiring little or no additional processing. The majority of Piper Impact's sales are to one customer, Autoliv Inc., for use in automotive air bag systems.

During 1997 the Company completed the construction of a greenfield manufacturing facility in New Albany, Mississippi, for the production of highly engineered, impact-extruded steel parts. Piper Impact's steel products plant was part of a two-year, \$42 million capital project to provide capacity for new customer programs primarily for the automotive air bag systems market. This includes passenger and side-impact air bags, "smart" bags with adjustable inflation force, and those with alternative inflation technologies. The Company believes that this project will provide Piper Impact with the technology and additional capacity for advanced applications, improved customer service, and cost effective manufacturing processes, thereby improving competitiveness and long-term growth opportunities.

The Fabricated Products Division manufactures aluminum window and patio door screens, window frames, and a broad line of custom designed, roll formed products and stamped shapes for manufacturers of premium wood windows and vinyl windows for the home improvement, residential, and commercial construction markets. AMSCO combines strong product design and development expertise with reliable,

just-in-time delivery. HFP also coats and/or paints aluminum sheet in many colors, sizes, and finishes, and it fabricates aluminum coil into rain carrying systems, soffit, exterior housing trim and roofing products.

#### RAW MATERIALS AND SUPPLIES

The Company's MACSTEEL plants purchase on the open market their principal raw material, steel scrap or substitutes such as pig iron, beach iron and hot briquetted iron. Collection and transportation of these raw materials to Company plants can be adversely affected by extreme weather conditions. Prices for scrap also vary in relation to the general business cycle, typically declining in periods of slow economic activity.

Nichols' principal raw material is aluminum scrap purchased on the open market, which can also be adversely affected by weather. Nichols purchases and sells in limited quantities aluminum ingot futures contracts on the London Metal Exchange to hedge against fluctuations in the price of aluminum scrap required to manufacture products for fixed-price sales contracts.

In the Engineered Products Group, Piper Impact's raw material consists of aluminum bars and slugs that it purchases on the open market and steel bars that it purchases from MACSTEEL. Piper Impact Europe purchases its raw material, aluminum slugs and steel sheet, on the open market in Europe and in the United States. Fabricated Products' primary raw material is coated and uncoated aluminum sheet purchased primarily from Nichols Aluminum.

#### BACKLOG

At October 31, 1999, Quanex's backlog of orders to be shipped in the next twelve months was \$164.1 million. This compares to \$183.8 million at October 31, 1998. Because many of the markets in which Quanex operates have short lead times, the Company does not believe that backlog figures are reliable indicators of annual sales volume or operating results.

#### COMPETITION

The Company's products are sold under highly competitive conditions. Quanex competes with a number of companies, some of which have greater financial and other resources. Competitive factors include product quality, price, delivery, and ability to manufacture to customer specifications. The amounts of engineered steel bars, aluminum mill sheet products, and engineered products made by the Company represent a small percentage of annual domestic production.

The Company's engineered bar plants compete primarily with two large integrated steel producers, two large non-integrated steel producers, and two smaller companies. Although these producers may be larger and have greater resources than the Company, Quanex believes that the technology used at MACSTEEL facilities permits it to compete effectively in the markets it serves.

The Company's aluminum mill sheet businesses compete with many small and large aluminum sheet manufacturers. Some of these competitors are divisions or subsidiaries of major corporations with substantially greater resources than the Company. The Company also competes with major aluminum producers in coil-coated and mill finished products, primarily on the basis of the breadth of product lines, the quality and responsiveness of its services, and price.

The Company's Engineered Products Group competes with many small metal fabricators and impact extruders, primarily on the basis of custom engineering, quality, service, and price.

#### SALES AND DISTRIBUTION

The Company's three businesses have sales organizations with sales representatives in many parts of the U. S. MACSTEEL sells hot rolled and cold finished engineered steel bars primarily to original equipment manufacturers (OEMs) through its sales organization and manufacturers' representatives. Nichols' products are sold directly to OEMs and through metal service centers. The Company's engineered products are sold primarily to OEMs, except for some residential building products, which are also sold through distributors.



## SEASONAL NATURE OF BUSINESS

With the exception of impact extrusions, which are not a seasonal business, the Company's aluminum mill sheet and Fabricated Products businesses are seasonal. The primary markets of these businesses are in the Northeast and Midwest regions of the United States, where winter weather reduces homebuilding and home improvement activity. Historically in these businesses, lowest sales have occurred during the Company's first fiscal quarter. Profits for the operations in these businesses tend to be lower in quarters with lower sales because a high percentage of their manufacturing overhead and operating expense is due to labor and other costs that are generally fixed throughout the year. The other businesses in which the Company competes are generally not seasonal. However, due to the holidays in the Company's first fiscal quarter and steel plant shutdowns for vacations and maintenance in the Company's third fiscal quarter, sales have historically been lower in those periods. As a result of these trends, combined with the effects of seasonality, the Company generally expects that, absent unusual activity or changes in economic conditions, its lowest sales will occur in the first fiscal quarter.

## SERVICE MARKS, TRADEMARKS, TRADE NAMES, AND PATENTS

The Company's Quanex, Quanex design, Seam-Free design, NitroSteel, MACGOLD, MACSTEEL, MACSTEEL design, MAC+, Ultra-Bar, Homeshield, Homeshield design, and "The Best Alloy & Specialty Bars" marks are registered trademarks or service marks. The Company's Piper Impact name is used as a service mark, but is not yet registered in the United States. The trade name Nichols-Homeshield and the Homeshield and the Homeshield design trademarks are used in connection with the sale of the Company's aluminum mill sheet products and residential building products. The Homeshield, Piper Impact, MACSTEEL and Quanex word and design marks and associated trade names are considered valuable in the conduct of the Company's business. The businesses conducted by the Company generally do not depend upon patent protection. Although the Company holds numerous patents, in many cases the proprietary technology that the Company has developed for using the patents is more important than the patents themselves.

## RESEARCH AND DEVELOPMENT

Expenditures for research and development of new products or services during the last three years were not significant. Although not technically defined as research and development, a significant amount of time, effort and expense is devoted to custom engineering and qualifying the Company's products for specific customer applications.

## ENVIRONMENTAL MATTERS

As a manufacturer of specialized metal products, Quanex is subject to extensive laws and regulations concerning the discharge of materials into the environment and the remediation of chemical contamination. Quanex is required to make capital and other expenditures on an ongoing basis in order to satisfy such requirements. The cost of environmental matters has not had a material adverse effect on Quanex's operations or financial condition in the past, and management is not aware of any existing conditions that it currently believes are likely to have a material adverse effect on Quanex's operations or financial condition.

Under applicable state and federal laws, the Company may be responsible for, among other things, all or part of the costs required to remove or remediate wastes or hazardous substances at locations Quanex has owned or operated at any time. The Company is currently participating in environmental assessments and remediation at a number of those locations.

From time to time, Quanex also has been alleged to be liable for all or part of the costs incurred to clean up third-party sites where it is alleged to have arranged for disposal of hazardous substances. The Company's allocable share of liability at those sites, taking into account the likelihood that other parties will pay their shares, has not been material to its operations or financial condition.

Total remediation reserves, at October 31, 1999, for Quanex's current plants, former operating locations, and disposal facilities were approximately \$20 million. Of that, approximately 80% is allocated to cleanup of historical soil and groundwater contamination and other corrective measures at a plant operated by the Company's Piper Impact subsidiary in New Albany, Mississippi. Depending upon such factors as

the nature and extent of contamination, the cleanup technologies employed, and regulatory concurrences, final remediation costs may be more or less than amounts accrued; however, management believes it has established adequate reserves for all probable and reasonably estimable remediation liabilities.

Environmental agencies continue to develop regulations implementing the Federal Clean Air Act. Depending on the nature of the regulations adopted, Quanex may be required to incur additional capital and other expenditures sometime in the next several years for air pollution control equipment, to maintain or obtain operating permits and approvals, and to address other air emission-related issues. The Company incurred capital expenditures totaling approximately \$20 million between 1996 and 1998 to meet those requirements. That amount included spending toward a significant upgrade to pollution control systems at MACSTEEL to ensure compliance with the air standards. Based upon its analysis and experience to date, Quanex does not believe that its compliance with Clean Air Act requirements will have a material effect on its operations or financial condition.

Quanex incurred approximately \$7 million and \$23 million during fiscal 1999 and 1998, respectively, in expenses and capital expenditures in order to comply with existing or proposed environmental regulations. The 1998 amount includes funds spent in connection with a significant upgrade to pollution control systems at MACSTEEL. The Company estimates spending of approximately \$7 million at various of its facilities during fiscal 2000 for continuing compliance with environmental regulations. Future expenditures relating to environmental matters will necessarily depend upon the application to Quanex and its facilities of future regulations and government decisions. Quanex will continue to have expenditures in connection with environmental matters beyond 2000, but it is not possible at this time to reasonably estimate the amount of these expenditures.

#### EMPLOYEES

At October 31, 1999, the Company employed 3,345 persons. Of the total employed, 37% were covered by collective bargaining agreements. A five-year contract was ratified by the United Steel Workers representing 190 employees at MACSTEEL's Michigan plant as of February 28, 1999. In January 1999, the production and maintenance employees at the MACSTEEL Arkansas plant voted to have the United Steel Workers as their bargaining representative. Negotiations of the first contract are ongoing. On June 30, 2000, the CAO Groot Metaal collective labor agreement representing 334 employees at Piper Europe will expire. Negotiations will begin in early calendar year 2000. No other collective bargaining agreements will expire during the fiscal year ending October 31, 2000.

#### FINANCIAL INFORMATION ABOUT FOREIGN AND DOMESTIC OPERATIONS

For financial information on the Company's foreign and domestic operations, see Note 13 of the Financial Statements contained in this Annual Report on Form 10-K.

## ITEM 2. PROPERTIES

The following table lists Quanex's principal plants together with their locations, general character and the industry segment which uses the facility. Each of the facilities identified as being owned by the Company is free of any material encumbrance.

LOCATION -----	PLANT -----	SQUARE FOOTAGE -----
Owned:	ENGINEERED STEEL BARS	
Fort Smith, Arkansas.....	MACSTEEL	464,000
Jackson, Michigan.....	MACSTEEL	281,000
Huntington, Indiana.....	Heat Treating	96,000
Leased (expires 2009):		
Kenosha, Wisconsin.....	NitroSteel	35,000
Owned:	ALUMINUM MILL SHEET PRODUCTS	
Lincolnshire, Illinois.....	Nichols Aluminum	142,000
Davenport, Iowa.....	Nichols Aluminum	236,000
Davenport, Iowa.....	Nichols Aluminum Casting	245,000
Leased (4 leases expiring 2003, 2004, 2005 and 2018):		
Decatur, Alabama.....	Nichols Aluminum Alabama	410,000
Owned:	ENGINEERED PRODUCTS	
Rice Lake, Wisconsin.....	AMSCO	290,800
Chatsworth, Illinois.....	Homeshield Fabricated Products (two plants)	212,000
New Albany, Mississippi.....	Piper Impact (two plants)	683,000
Zwolle, The Netherlands.....	Piper Impact Europe	110,000
Leased (expires 2010):	EXECUTIVE OFFICES	
Houston, Texas.....	Quanex Corporation	21,000

## ITEM 3. LEGAL PROCEEDINGS

On or about May 26, 1999, the federal government filed in the United States District Court for the Southern District of Texas a complaint and proposed consent decree with respect to alleged violations of the Clean Water Act by the Company and Vision Metals, Inc. at the Company's former facility in Rosenberg, Texas. Among other things, the complaint alleged that during the Company's ownership the plant had discharged water which contained pollutants at levels greater than applicable effluent limits, had not appropriately monitored its discharges, and had not adequately notified the federal Environmental Protection Agency of exceedances. The Company tendered this matter to Vision Metals for defense and indemnification pursuant to the purchase agreement by which Vision Metals acquired the Rosenberg facility and assumed certain environmental liabilities. Vision Metals accepted the Company's tender without reservation. Under the consent decree, all of the complaint's allegations against the Company are to be settled by payment of a civil penalty by Vision Metals in the amount of \$466,421 plus interest payable in three installments. The court approved and entered the consent decree on or about August 2, 1999. Pursuant to the consent decree, the first installment of \$155,474 plus interest, was paid by Vision Metals as of December 30, 1999.

On or about September 27, 1999, USEPA Region V sent to the Company's MACSTEEL Michigan division findings of violation, an administrative order for compliance, and a request for information pursuant to the Clean Water Act. The Agency alleged that the plant had violated the terms of its water discharge permit 236 times since March 1994 and directed the plant to comply with that permit. To date the Agency has not assessed any penalties for the alleged violations, but is reserving its rights to do so.

Other than the above matters and proceedings described under Item 1, "Environmental Matters", there are no material legal proceedings to which Quanex, its subsidiaries, or their property is subject.

## ITEM 4. SUBMISSION OF MATTERS TO VOTE OF SECURITY HOLDERS

None.

## PART II

## ITEM 5. MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Quanex's common stock, \$.50 par value, is traded on the New York Stock Exchange, under the ticker symbol: NX. Quarterly stock price information and annual dividend information for the common stock is as follows:

QUARTERLY COMMON STOCK DIVIDENDS	1999	1998	1997	1996	1995
Quarter Ended:					
January.....	.16	.16	.15	.15	.14
April.....	.16	.16	.15	.15	.15
July.....	.16	.16	.15	.15	.15
October.....	.16	.16	.16	.15	.15
Total.....	.64	.64	.61	.60	.59

QUARTERLY COMMON STOCK SALES PRICE	1999	1998	1997	1996	1995
(High & Low) Quarter Ended:					
January.....	23 7/8	30 7/16	29 1/8	21 1/8	24 5/8
April.....	16 13/16	27 1/16	24 1/4	18	20
July.....	26 1/4	33 13/16	27 7/8	22 3/8	23 7/8
October.....	15 3/8	28 1/2	23 3/8	19 5/8	21
January.....	29	32 3/16	34 1/8	23 7/8	26 5/8
April.....	25 1/8	27 1/4	25 1/8	19 3/8	22 1/8
July.....	27 3/8	27 7/8	36 1/2	28 3/4	26
October.....	20 1/8	15 5/8	26 1/4	19 5/8	18 5/8

The terms of Quanex's revolving credit arrangements with certain banks limit the total amount of common and preferred stock dividends and other distributions on such stock. Under the most

restrictive test under such credit facilities, the total common stock dividends the Company may declare and pay is limited to \$21 million, plus 50% of consolidated net income earned after October 31, 1989, adjusted for other factors as set forth in the credit agreement. As of October 31, 1999, the aggregate amount available for dividends and other restricted payments under its credit facilities was approximately \$48 million.

There were 5,362 holders of Quanex common stock on record as of December 31, 1999.

#### ITEM 6. SELECTED FINANCIAL DATA

##### GLOSSARY OF TERMS

The exact definitions of commonly used financial terms and ratios vary somewhat among different companies and investment analysts. The following list gives the definition of certain financial terms that are used in this report:

Capital expenditures:	Additions to property, plant and equipment.
Book value per common share:	Stockholders' equity less the stated value of preferred stock divided by the number of common shares outstanding.
Asset turnover:	Net sales divided by average total assets.
Current ratio:	Current assets divided by current liabilities.
Return on investment:	The sum of net income and the after-tax effect of interest expense less capitalized interest divided by the sum of the averages for long-term debt and stockholders' equity.
Return on common stockholders' equity:	Net income attributable to common stockholders divided by average common stockholders' equity.

## ITEM 6. SELECTED FINANCIAL DATA

## FINANCIAL SUMMARY 1994 -- 1999

	FISCAL YEARS ENDED OCTOBER 31,					
	1999	1998	1997	1996	1995	1994
	(\$ THOUSANDS, EXCEPT PER SHARE DATA)					
<b>REVENUES AND EARNINGS</b>						
Net sales(1).....	810,094	797,490	746,093	620,069	603,985	435,983
Cost of sales including depreciation.....	681,799	683,954	644,041	526,886	521,521	376,077
Gross profit.....	128,295	113,536	102,052	93,183	82,464	59,906
Piper Impact Restructuring Charge.....		58,500(2)				
Other depreciation and amortization.....	3,434	5,059	3,669	1,791	1,258	1,266
Selling, general and administrative expenses.....	53,104	47,713	43,375	44,959	33,746	31,893
Operating income.....	71,757	2,264	55,008	46,433	47,460	26,747
Percent of net sales.....	8.9	0.3	7.4	7.5	7.9	6.1
Other income (expense) -- net.....	1,383	2,278	1,637	4,544	1,721	2,765
Interest expense -- net.....	12,791	10,506	14,002	11,360	8,870	10,178
Income (loss) before income taxes, extraordinary items, cumulative effect of accounting change, and income from discontinued operations.....	60,349	(5,964)	42,643	39,617	40,311	19,334
Income taxes (credit).....	21,048	(2,087)	14,925	16,639	16,931	8,120
Income (loss) from continuing operations.....	39,301	(3,877)	27,718	22,978	23,380	11,214
Income from discontinued operations.....	0	0	5,176	9,912	10,480	7,638
Gain on sale of discontinued operations.....	0	13,046	36,290			
Extraordinary items -- early extinguishment of debt, net of taxes.....	415	--	--	(2,522)	(2,021)	--
Net income.....	39,716	9,169	69,184	30,368	31,839	18,852
Percent of net sales.....	4.9	1.1(5)	9.3(4)	4.9	5.3	4.3
<b>PER SHARE DATA</b>						
Basic Earnings per share:						
Income (loss) from continuing operations.....	2.76	(0.27)	2.01	1.70	1.44	0.40
Income from discontinued operations.....	--	--	0.37	0.73	0.78	0.57
Gain on sale of discontinued operations.....	--	0.92	2.63	--	--	--
Extraordinary items and cumulative effect of accounting change.....	0.03	--	--	(0.19)	(0.15)	--
Net earnings (loss).....	2.79	0.65(5)	5.01	2.24	2.07	0.97
Cash dividends declared.....	0.64	0.64	0.61	0.60	0.59	0.56
Book value.....	21.24	19.19	19.13	14.50	12.81	11.04
Average shares outstanding (000).....	14,234	14,149	13,807	13,524	13,443	13,342
Market closing price range						
High.....	28 15/16	33 1/2	36 1/2	28 5/8	26	27
Low.....	15 1/2	16	23 3/8	18 3/8	18 3/8	16 1/4
<b>FINANCIAL POSITION -- YEAR END</b>						
Working capital.....	76,247	62,979	52,818	88,238	53,629	100,007
Property, plant and equipment -- net.....	406,841	395,054	379,071	319,165	233,982	239,642
Other assets.....	71,218	69,422	119,738	117,142	55,989	54,736
Total assets.....	690,446	674,288	685,705	638,948	466,458	491,329
Noncurrent deferred income taxes.....	43,910	33,412	48,111	40,454	45,740	39,298
Long-term debt.....	179,121	188,302	201,858	253,513	111,894	107,442
Stockholders' equity.....	301,061	272,044	268,823	197,009	172,814	233,883
Total capitalization.....	480,182	460,346	470,681	450,522	284,708	341,325
Long-term debt percent of capitalization.....	37.3	40.9	42.9	56.3	39.3	31.5
<b>OTHER DATA</b>						
Asset turnover.....	1.2	1.2	1.1	1.0	1.3	0.9
Current ratio.....	1.6 to 1	1.4 to 1	1.4 to 1	1.8 to 1	1.4 to 1	2.0 to 1
Return on average investment -- percent.....	10.0	3.4(5)	16.7(4)	9.8	11.1	6.9
Return on average common equity -- percent.....	13.9	3.4(5)	29.7(4)	16.4	17.4	9.0
Working capital provided by operations(3).....	94,682	82,830	73,321	60,378	57,767	39,326
Depreciation and amortization.....	45,883	42,400	37,865	36,499	29,062	25,520
Capital expenditures.....	60,934	60,936	69,146	34,737	21,629	42,297
Backlog for shipment in next 12 months.....	164,128	183,847	225,498	123,382	94,464	109,626
Number of stockholders.....	5,113	5,720	5,488	3,425	3,659	3,454
Average number of employees.....	3,393	3,261	2,994	1,950	1,653	1,530
Sales per employee.....	239	245	249	318	365	285

Note: Several acquisitions and divestitures have been made in the past three years. See Notes 2 and 3 to the financial statements for a description of these transactions.

(1) Excludes sales from discontinued operations for the years 1997-1994, respectively of \$187,123, \$275,641, \$287,210 and \$263,331.

- (2) During the fourth quarter of 1998, Piper Impact recorded a \$58.5 million non-recurring restructuring charge as the result of impairment as described by Statement of Financial Accounting Standards No. 121. See Footnote 4 to the financial statements for further information.
- (3) Working capital provided by operations is a supplemental financial measurement used in the company's business and should not be construed as an alternative to operating income or cash provided by operating activities since it excludes the effects of changes in working capital. Working capital from operations is calculated as income from continuing operations, net of taxes, adjusted for non-cash and nonrecurring items.
- (4) Includes gain on sale of discontinued operations.
- (5) Includes effect of Piper Impact's restructuring charge (\$58.5 million) and gain on sale of discontinued operations (\$13 million).

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

## GENERAL

The discussion and analysis of the Company's financial condition and results of operations should be read in conjunction with the Selected Financial Data and the Consolidated Financial Statements of the Company and the accompanying notes.

## PRIVATE SECURITIES LITIGATION REFORM ACT

Certain forward-looking information contained herein is being provided in accordance with the provisions of the Private Securities Litigation Reform Act. Such information is subject to certain assumptions and beliefs based on current information known to the Company and is subject to factors that could produce actual results materially different from those anticipated in the forward-looking statements contained in this report. Such factors include domestic and international economic activity, prevailing prices of steel and aluminum scrap and other raw material costs, interest rates, construction delays, market conditions for the Company's customers, any material changes in purchases by the Company's principal customers, environmental regulations and changes in estimates of costs for known environmental remediation projects and situations, world-wide political stability and economic growth, the Company's successful implementation of its internal operating plans, performance issues with key customers, suppliers and subcontractors, and regulatory changes and legal proceedings. Accordingly, there can be no assurance that the forward-looking statements contained herein will occur or that objectives will be achieved.

## RESULTS OF OPERATIONS

## Overview

## Summary Information as % of Sales:

	FISCAL YEAR ENDED OCTOBER 31,					
	1999		1998		1997	
	DOLLAR AMOUNT	% OF SALES	DOLLAR AMOUNT	% OF SALES	DOLLAR AMOUNT	% OF SALES
	(DOLLARS IN MILLIONS)					
Net Sales.....	\$810.1	100%	\$797.5	100%	\$746.1	100%
Cost of Sales.....	639.9	79	647.2	81	610.4	82
Selling, general and admin....	53.1	6	47.7	6	43.4	6
Depreciation and amortization.....	45.3	6	41.8	5	37.3	5
Restructuring Charge.....	--	--	58.5	7	--	--
Operating Income.....	71.8	9%	2.3	1%	55.0	7%
Interest Expense.....	(14.4)	(2)	(14.9)	(2)	(17.5)	(2)
Capitalized Interest.....	1.6	0	4.4	1	3.5	0
Other, net.....	1.4	0	2.2	0	1.6	0
Income tax benefit (expense)....	(21.1)	(2)	2.1	0	(14.9)	(1)
Income (loss) from continuing operations.....	\$ 39.3	5%	\$ (3.9)	0%	\$ 27.7	4%

For the seventh consecutive year, the Company's continuing operations achieved higher sales from the previous fiscal year. These continued increases are a result of the Company's growth strategies through internal investments as well as acquisitions. The Company's internal growth investments, principally at the MACSTEEL Division and at Piper Impact, Inc. ("Piper Impact") were focused toward capacity expansions, new product offerings, quality improvements, and enhanced customer service capabilities.



## Acquisitions/Divestitures Since October 31, 1996

In April 1997, the Company completed the sale of its LaSalle Steel Company ("LaSalle") subsidiary. LaSalle's results of operations have been classified as discontinued operations and prior periods have been restated. For business segment reporting purposes, LaSalle's data was previously classified as "Cold Finished Steel Bars".

In October 1997, the Company, through its Dutch subsidiary, Piper Impact Europe B.V. ("Piper Impact Europe"), purchased the net assets of Advanced Metal Forming C.V., a Dutch limited partnership, for approximately \$30 million. The Company's income statement for the twelve months ended October 31, 1997 does not include results for Piper Impact Europe.

In December 1997, the Company completed the sale of its tubing operations ("Tubing Operations"), comprised of Michigan Seamless Tube, Gulf States Tube, and the Tube Group Administrative Office. The results of the Tubing Operations have been classified as discontinued operations and prior periods have been restated. For business segment reporting purposes, these businesses were previously classified as "Steel Tubes". Two small divisions, Heat Treat Division and NitroSteel Division, which were previously included with this segment, were retained by the Company and are now included in the Engineered Steel Bars segment.

In October 1998, the Company acquired the stock of Decatur Aluminum Corp., a Decatur, Alabama based aluminum sheet manufacturer for approximately \$19 million. The newly acquired company has been renamed Nichols Aluminum-Alabama, Inc. ("Nichols Aluminum Alabama") in alignment with Quanex's other aluminum mill sheet businesses in its Nichols Aluminum division. Nichols Aluminum Alabama's operations include cold rolling aluminum sheet to specific gauge, annealing, leveling, custom painting and slitting to width.

On December 15, 1999, the Company announced that it had signed a contract to acquire the assets of Alcoa's Fort Lupton, Colorado-based aluminum sheet production facility for \$8 million plus working capital value which is estimated at \$17 million. Consummation of the sale is subject to government approval.

The acquisition of the Fort Lupton mill will increase the casting, cold-finishing and value-added painting capacities of Nichols Aluminum, Quanex's aluminum sheet business. The Fort Lupton mill can produce more than 40-million pounds annually of high-grade aluminum sheet for a variety of applications, including beverage cans and other food packaging, home furnishing, and other consumer durable products.

## Business Segments

The Company adopted Statement of Financial Accounting Standards No. 131, "SFAS 131" for the fiscal year ended 1998. SFAS 131 requires that the Company disclose certain information about its operating segments where operating segments are defined as "components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance". Generally, financial information is required to be reported on the basis that it is used internally for evaluating segment performance and deciding how to allocate resources to segments.

Pursuant to SFAS 131, the Company has three reportable segments: engineered steel bars, aluminum mill sheet products, and engineered products. The engineered steel bar segment consists of engineered steel bars manufacturing, steel bar and tube heat treating services and steel bar and tube wear and corrosion resistant finishing services. The aluminum mill sheet segment manufactures mill finished and coated aluminum sheet. The engineered products segment manufactures impact-extruded aluminum and steel parts, aluminum window and patio door screens, window frames and other roll formed products and stamped shapes.

The following table sets forth selected operating data for the Company's three business segments:

	YEARS ENDED OCTOBER 31,		
	1999	1998(4)	1997(4)
	(IN THOUSANDS)		
Engineered Steel Bars:			
Net sales.....	\$297,369	\$327,296	\$319,468
Operating income.....	60,446	58,908	50,762
Depreciation and amortization.....	16,293	13,097	13,940
Identifiable assets.....	\$241,783	\$219,727	\$192,937
Aluminum Mill Sheet Products:(1)			
Net sales.....	\$311,763	\$266,355	\$261,041
Operating income.....	15,306	7,788	1,753
Depreciation and amortization.....	12,334	10,670	10,154
Identifiable assets.....	\$200,733	\$198,596	\$163,637
Engineered Products:(2)(3)			
Net sales.....	\$227,362	\$230,012	\$206,831
Operating income (loss).....	12,153	(52,606)	15,444
Depreciation and amortization.....	16,185	17,928	13,055
Identifiable assets.....	\$209,153	\$220,161	\$281,943

- (1) 1998 results include three weeks of Nichols Aluminum Alabama's operations acquired October 9, 1998. (See Note 2 to financial statements)
- (2) 1997 data does not include the results of Piper Impact Europe. However, identifiable assets as of October 31, 1997 include Piper Impact Europe, acquired October 29, 1997. (See Note 2 to financial statements)
- (3) During 1998, Piper Impact recorded a \$58.5 million non-recurring restructuring charge as the result of impairment as described by Statement of Financial Accounting No. 121. This restructuring charge is included in operating income. (See Note 4 to financial statements)
- (4) At the start of fiscal 1999, Quanex changed its inventory valuation method for measuring segment results from LIFO to FIFO. This change has no impact on consolidated results, which remain LIFO based. Prior data have not been restated above. (See footnote 13 to the consolidated financial statements for further information.)

The engineered steel bar business posted record annual operating income, benefiting from strong demand in the transportation markets and favorable raw material costs, which helped to offset softness in other markets. Pricing has been under intense pressure, and it is expected to continue in the year ahead. In fiscal 1999, MACSTEEL finished its Phase IV expansion project, doubling production capacity for MACPLUS cold-finished steel bars, its most premium value-added product. Work continues on Phase V, which will increase capacity at MACSTEEL's engineered bar mills and the MACSTEEL Heat Treating Division and will improve operational efficiency at MACSTEEL NitroSteel.

The aluminum mill sheet business achieved a breakthrough year, consistently improving its quarterly performance during fiscal 1999. Operating income, which increased 97% on 17% higher sales was helped by the acquisition of Nichols Aluminum Alabama and improved spreads from lower aluminum scrap prices as well as benefits resulting from the Rotary Furnace project at its mini-mill in Davenport, Iowa. The backlog for the first quarter is seasonally normal with some pricing pressures and short lead times.

The engineered products business also had significantly improved earnings on slightly lower sales. Adjusting for the one-time restructuring charge of \$58.5 million recorded at Piper Impact in fiscal 1998 and the resulting lower amortization, the operating income from the engineered products business improved by 47% in fiscal 1999. Lower raw material costs, stringent cost controls and implementation of lean manufacturing techniques contributed to the success. However, fierce competition in the air bag market will continue to pose significant challenges for Piper Impact until it can diversify its business in new markets with new products. The fabricated products businesses, AMSCO and Homeshield Fabricated

Products, continue to expand their markets by leveraging their product design and engineering expertise to develop applications for new customers.

#### Outlook

The Company currently expects that the overall business levels for fiscal 2000 should be similar to those experienced during 1999, except for its engineered products business which is experiencing product mix change resulting in lower sales. Domestic and global market factors will also impact the Company and any slowdown in the U.S. economy could affect demand and pricing for many of the Company's products. Improved financial results will be dependent upon, among other things, whether the continued strength of the economy can be sustained, improvements in the markets which the Company serves, successful new product development efforts at engineered products business and whether the improvements in the price spreads of aluminum mill sheet products can be sustained.

#### 1999 Compared to 1998

Net Sales -- Consolidated net sales for fiscal 1999 were \$810.1 million, representing an increase of \$12.6 million, or 2%, when compared to fiscal 1998. This increase reflects higher net sales at the aluminum mill sheet business partially offset by lower net sales at the Company's engineered steel bar and engineered products businesses. Nichols Aluminum Alabama, which was acquired in October 1998, contributed a full year of sales in fiscal 1999.

Net sales from the Company's engineered steel bar business for fiscal 1999, were \$297.4 million, representing a decrease of \$29.9 million, or 9%, when compared to fiscal 1998. This decline was principally due to the reduced demand in some of the durable goods market, inventory adjustments by some customers and pricing pressures resulting from global sourcing of engineered bars and forged components.

Net sales for fiscal 1999 from the Company's aluminum mill sheet products business increased by \$45.4 million or 17% to \$311.8 million when compared to fiscal 1998. This increase was largely due to the acquisition of Nichols Aluminum Alabama in October of 1998.

Net sales from the Company's engineered products business for fiscal 1999 were \$227.4 million, representing a decrease of \$2.7 million, or 1% from last year. The decrease was largely due to reduced demand for older generation aluminum airbag components at the Piper facilities, partially offset by sales of new non-airbag products as well as increased demand for traditional window and door products in the Fabricated Products division.

Operating income -- Consolidated operating income for fiscal 1999 was \$71.8 million. This represents an increase of \$11.0 million, or 18%, when compared to the operating income in fiscal 1998 of \$60.8 million, excluding the one-time \$58.5 million restructuring charge. During fiscal 1999 all business segments had increased operating income, partially offset by increased expenses at the corporate office for Year 2000 readiness efforts, relocation expenses and consulting expenses for systems implementation.

At the start of fiscal year 1999, Quanex changed its inventory valuation method for measuring segment results from LIFO to FIFO. See Note 13 to the financial statements for further discussion. This change has no impact on consolidated results, which remain LIFO based.

Operating income from the Company's engineered steel bar business was \$60.4 million for fiscal 1999, representing an increase of \$1.5 million, or 3%, when compared to fiscal 1998. The increase achieved, despite the lower net sales, was largely due to the higher spreads resulting from lower material prices, increased sales of value-added products and productivity improvements realized from the Phase III project completed in 1998. Additionally, approximately \$2 million of benefits were realized as a result of an insurance recovery and a litigation settlement received in fiscal 1999.

Operating income for fiscal 1999 from the Company's aluminum mill sheet products business was \$15.3 million, representing an increase of \$7.5 million or 97% from last year. This increase was largely due to higher sales and operating efficiencies realized from the acquisition of Nichols Aluminum Alabama and improved spreads resulting from lower aluminum scrap prices as well as benefits from the new rotary furnaces and the dross recovery system. Also, the operating income in fiscal 1998 was based on inventory valuation using LIFO method (see Note 13 to the financial statements).

Operating income from the Company's engineered products business was \$12.2 million for fiscal 1999. For comparison purposes, fiscal 1998 operating loss of \$52.6 million should be adjusted for the one-time restructuring charge of \$58.5 million and the decreased amortization expense of \$2.4 million, both recorded at Piper Impact. When compared to the adjusted operating income of \$8.3 million, fiscal 1999 operating income from the engineered products business represents an increase of \$3.9 million or 47%. The improvement was largely due to lower material costs and some success at cost management measures.

In addition to the three operating segments mentioned above, operating expenses for corporate and other for fiscal 1999 were \$16.1 million, representing an increase of \$4.3 million over the \$11.8 million recorded in fiscal 1998. Included in corporate and other are the corporate office expenses, impact of inventory accounting using LIFO method and inter-segment eliminations. (See notes 8 and 13 to the financial statements regarding LIFO valuation method of inventory accounting.)

Selling, general and administrative expenses -- Selling, general and administrative expenses increased by \$5.4 million, or 11% in fiscal 1999 as compared to last year. This increase is largely a result of the acquisition of Nichols Aluminum Alabama, Year 2000 readiness efforts, relocation expenses and consulting expenses for system implementations.

Depreciation and amortization -- Depreciation and amortization increased by \$3.5 million, or 8% in fiscal 1999 as compared to last year. The increase is principally due to increased depreciation at the engineered steel bar and aluminum mill sheet products businesses for recently completed projects as well as the inclusion of Nichols Aluminum Alabama, which was acquired in October 1998, partially offset by lower amortization at the engineered products business.

Interest expense -- Interest expense decreased by \$500 thousand in fiscal 1999 primarily resulting from the purchase of \$9.7 million face value subordinated debentures.

Capitalized interest -- Capitalized interest decreased by \$2.8 million in fiscal 1999 as compared to fiscal 1998 primarily due to the completion of significant capital projects at MACSTEEL during 1998.

Other, net -- "Other, net" decreased by \$900 thousand in fiscal 1999 as compared to last year primarily as a result of reduced investment income on lower cash balances.

Income from continuing operations -- The Company earned income from continuing operations of \$39.3 million in fiscal 1999. This represents an increase of \$5.2 million or 15% when compared to fiscal 1998 income from continuing operations of \$34.1 million, excluding the restructuring charge. The increase in fiscal 1999 was principally due to increased operating earnings from all three business segments of the Company and inclusion of a full year's earnings from Nichols Aluminum Alabama, which was acquired in October 1998.

Net income -- Fiscal 1999 net income was \$39.7 million, compared to \$9.2 million for fiscal 1998. Included in net income for fiscal 1999 were \$415 thousand of extraordinary items representing net gain on early extinguishment of debt. Fiscal 1998 net income included an after-tax non-recurring restructuring charge of \$38.0 million at Piper Impact and an after-tax gain of \$13.0 million on the sale of discontinued operations.

#### 1998 Compared to 1997

Net Sales -- Net sales for fiscal 1998 were \$797.5 million, representing an increase of \$51.4 million when compared to fiscal 1997. This increase reflects higher net sales in all three business segments as well as an increase of \$14.4 million resulting from sales to discontinued operations which were previously reflected as intersegment sales and eliminated in 1997. These sales are now third-party sales and are not eliminated in 1998. Piper Impact Europe, which was acquired in October 1997, contributed a full year of sales in fiscal 1998.

Net sales for fiscal 1998 from the Company's engineered steel bar business were \$327.3 million, representing an increase of \$7.8 million, or 2%, when compared to fiscal 1997. This increase was primarily attributable to a better mix of product sales with a higher percentage of MACPLUS and bearing steels.

Net sales from the Company's aluminum mill sheets products business for fiscal 1998 were \$266.4 million, representing an increase of \$5.3 million, or 2%, when compared to fiscal 1997. This increase was primarily attributable to strong demand, which yielded a 5% increase in volume.

Net sales from the engineered products group increased \$23.2 million to \$230.0 million. The majority of the increase resulted from the addition of Piper Impact Europe offset by a decrease in net sales at Piper Impact.

Restructuring Charge -- During the year ended October 31, 1998, the Company recorded a restructuring charge of \$58.5 million related to its subsidiary, Piper Impact.

Components of this special charge include \$51.2 million for goodwill impairment; \$6.7 million for impairment of property, plant and equipment; and \$600 thousand for severance benefits to be paid to employees of the Park City, Utah plant. Piper Impact experienced significant changes in market conditions and the relationship with its major customer in fiscal 1998, which led to substantial declines in sales and operating cash flow. Management began an evaluation of the operations of Piper Impact in August 1998. As a result of this evaluation, in September 1998, management approved a plan to close the Park City, Utah facility and move its production to the New Albany, Mississippi facility.

Due to the significance of the changes discussed above and the decision to close one of the acquired production facilities, management performed an evaluation of the recoverability of all of the assets of Piper Impact, excluding the new steel plant, as described in Statement of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of". Management concluded from the results of this evaluation that a significant impairment of intangible as well as long-lived assets had occurred. An impairment charge was required because estimated fair value was less than the carrying value of the assets. Considerable management judgment is necessary to estimate fair value. Accordingly, actual results could vary significantly from management's estimates.

The one-time restructuring charge resulted in an after-tax impact on net income of \$38 million or \$2.68 per share.

Operating Income -- Consolidated operating income for fiscal 1998 was \$2.3 million. Included in operating income was the one-time \$58.5 million restructuring charge discussed above. Operating income excluding this restructuring charge was \$60.8 million, representing an increase of \$5.8 million, or 10%, when compared to fiscal 1997. Primary contributing factors to this increase were: 1) Increased sales and operating income from the engineered steel bar and aluminum mill sheet business and 2) the inclusion of a full year of Piper Impact Europe in the engineered products business. These improvements were partly offset by lower operating income from Piper Impact of the engineered products business.

Operating income from the Company's engineered steel bar business for fiscal 1998 was \$58.9 million, representing an increase of \$8.1 million, or 16%, when compared to fiscal 1997. This increase was principally due to increased sales from strong demand in the transportation markets as well as lower material prices. These results represented a record year for this business.

Operating income from the Company's aluminum mill sheet products business for fiscal 1998 was \$7.8 million, representing an increase of \$6.0 million, or 344%, when compared to fiscal 1997. This increase was principally due to increased volume and net sales accompanied by lower scrap prices. During the fourth quarter of 1998, this business experienced a turnaround with strong demand and favorable material costs.

The Company's engineered products business experienced an operating loss of \$52.6 million for fiscal 1998. Included in this loss was the non-recurring restructuring charge of \$58.5 million described above. Operating income for 1998 excluding this restructuring charge was \$5.9 million, a decrease of \$9.6 million or 62% from 1997. This decline is largely a result of operating losses experienced at Piper Impact. While Piper Impact Europe made a solid contribution in its first full year with the Company, slack demand in Asia and the General Motors strike adversely affected sales for Piper Impact products in North American markets. The fabricated products lines within this business showed modest improvement over fiscal 1997.

Selling, General and Administrative Expenses -- Selling, general and administrative expenses increased in fiscal 1998 by \$4.3 million, or 10%, compared to fiscal 1997. This increase is largely a result of the inclusion of a full year of Piper Impact Europe, which was not included in 1997.

Depreciation and Amortization -- Depreciation and amortization increased by \$4.5 million in fiscal 1998 compared to fiscal 1997. This increased depreciation resulted from the inclusion of Piper Impact

Europe in 1998 and the increased depreciation at Piper Impact for the steel products plant partially offset by lower depreciation at the engineered steel bar business.

Interest Expense and Capitalized Interest -- Interest expense decreased by \$2.6 million compared to fiscal 1997 as a result of reducing bank borrowings with proceeds received from the sale of LaSalle and the Tubing operations. Capitalized interest increased by \$859 thousand in 1998 compared to 1997 primarily due to Phase III and IV of the MACSTEEL expansion projects.

Other -- "Other, net" consists largely of investment income and remained relatively constant.

Income From Continuing Operations -- The Company had a loss from continuing operations of \$3.9 million in 1998. Included in this loss was the after-tax non-recurring restructuring charge of \$38.0 million. Income from continuing operations excluding the restructuring charge was \$34.1 million, an improvement of \$6.4 million, or 23%, compared to fiscal 1997. The improvement was attributable to improved results in the Company's engineered steel bars and aluminum mill sheet businesses, and the inclusion of a full year of Piper Impact Europe and lower interest expense. These improvements were partially offset by lower operating results at Piper Impact. The Company's effective income tax rate was 35% for fiscal 1998 and 1997.

Income from Discontinued Operations -- Income from discontinued operations, net of income taxes, for fiscal 1997, was \$5.2 million, which consisted of the Tubing Operations and LaSalle Steel. There was no income from discontinued operations in fiscal 1998. (See Note 3 to the financial statements)

Net Income -- Fiscal 1998 net income was \$9.2 million, compared to \$69.2 million for fiscal 1997. Included in net income for fiscal 1998 is an after-tax non-recurring restructuring charge of \$38.0 million and an after-tax gain of \$13.0 million on the sale of discontinued operations. Included in net income for 1997 was an after-tax gain of \$36.3 million on the sale of discontinued operations.

#### LIQUIDITY AND CAPITAL RESOURCES

Total capitalization at October 31, 1999 was \$490.7 million, consisting of \$189.7 million of debt and \$301.0 million of equity. The debt-to-capitalization ratio at the end of fiscal 1999 was 38.7% compared with 42.4% at the end of fiscal 1998. The lower debt-to-capitalization ratio results primarily from the purchase of subordinated debentures.

The Company's principal sources of funds are cash on hand, cash flow from operations, and borrowings under an unsecured \$250 million Revolving Credit and Term Loan Agreement ("Bank Agreement"). The Bank Agreement currently consists of a revolving line of credit ("Revolver"). In July 1997, the term loan provisions of the Bank Agreement expired. The Bank Agreement expires July 23, 2003 and provides for up to \$25 million for standby letters of credit, limited to the undrawn amount available under the Revolver. As of October 31, 1999, there was \$75 million outstanding under the Revolver. See footnote 11 to the financial statements for a detailed description of all of the Company's debt instruments, outstanding balances and aggregate maturities over each of the next five years and beyond.

The Bank Agreement contains customary affirmative and negative covenants and requirements to maintain a minimum consolidated tangible net worth, as defined. The Bank Agreement limits the payment of dividends and certain restricted investments. At October 31, 1999, retained earnings of approximately \$48 million were available for dividends and other restricted payments. As of October 31, 1999, the Company was in compliance with all covenants under the Bank Agreement.

During fiscal 1999, the Company accepted unsolicited block offers to buy back \$9.7 million principal amount of convertible subordinated debentures for \$8.8 million in cash. An after-tax extraordinary gain of \$415 thousand was recorded on these transactions. The outstanding balance of these debentures as of October 31, 1999 was \$73.7 million.

On June 1, 1999, the Company borrowed \$3 million through unsecured Scott County, Iowa Variable Rate Demand Industrial Waste Recycling Revenue Bonds Series 1999.

At October 31, 1999, the Company had commitments of \$15 million for the purchase or construction of capital assets. The most significant project included in this total relates to the Company's continued expansions at MACSTEEL. The Company plans to fund these capital expenditures through cash flow from operations and, if necessary, additional borrowings.

On December 9, 1999, the Company announced that its Board of Directors approved a program to repurchase shares of the Company's common stock. Under terms of the program, the Company may periodically purchase up to a total of 2 million shares of its common stock in the open market or in privately negotiated transactions. The repurchase plan does not have a time limit, and funds for the program will be provided from the Company's available working capital and bank credit line.

The Company believes that it has sufficient funds and adequate financial sources available to meet its anticipated liquidity needs. The Company also believes that cash flow from operations, cash balances and available borrowings will be sufficient for the foreseeable future to finance anticipated working capital requirements, capital expenditures, debt service requirements, environmental expenditures and dividends.

#### Operating Activities

Cash provided by operating activities during fiscal 1999 was \$77.7 million. This represents an increase of \$13.6 million, or 21%, compared to fiscal 1998. This increase primarily resulted from 1) increased cash from improved operating earnings in fiscal 1999 as compared to 1998 and 2) a decreased use of cash for working capital.

#### Investment Activities

Net cash used by investment activities in fiscal 1999 was \$62.7 million compared to \$39.8 million in fiscal 1998. Fiscal 1998 cash from investing activities included the acquisition of Decatur Aluminum Corp. and proceeds from the sale of the Tubing Operations. There were no acquisitions or divestitures in fiscal 1999. Capital expenditures increased from \$58.5 million in 1998 to \$60.8 million in 1999. The Company estimates that fiscal 2000 capital expenditures will approximate \$50 million.

#### Financing Activities

Net cash used by financing activities for fiscal 1999 was \$15.4 million, compared to \$24.9 million in the prior year. During fiscal 1999, the Company used \$8.8 million to purchase subordinated debentures, whereas it repaid approximately \$17 million of bank borrowings in fiscal 1998. Dividend payments amounted to approximately \$9 million in both fiscal 1999 and fiscal 1998. Proceeds from the issuance of stock totaled \$1.6 million in fiscal 1999 compared to \$3.2 million in fiscal 1998.

#### EFFECTS OF INFLATION

Inflation has not had a significant effect on earnings and other financial statement items.

#### NEW ACCOUNTING PRONOUNCEMENTS

In June 1998, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities," which is effective for the Company's year ending October 31, 2000. This statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. In June 1999, the FASB issued SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities -- Deferral of the Effective Date of FASB Statement No. 133" which defers the effective date of SFAS No. 133 until the Company's year ending October 31, 2001. The Company will be analyzing SFAS No. 133 to determine what, if any, impact or additional disclosure requirements this pronouncement will have.

#### YEAR 2000

The Company, like other businesses, faced the Year 2000 issue, (also known as Y2K issue). Many computer systems and equipment with embedded chips or processors use only two digits to represent the calendar year. This could result in computational or operational errors as dates are compared across the century boundary causing possible disruptions in business operations. The Y2K issue could have occurred at any point in the Company's supply, manufacturing, processing, distribution, and financial chains.

The Company began addressing the Y2K issue in 1997, with an initial assessment of Y2K readiness efforts at each of its operating units. Based on responses from the operating units, a standardized Year 2000 Plan format was developed. By July 1998, each operating unit had developed a Year 2000 Plan that included:

- a) inventory,
- b) assessment,
- c) remediation and replacement,
- d) testing, and
- e) third party relationships.

The Year 2000 issue was addressed within the Company by its individual business units, and progress was reported periodically to management. The Company committed necessary resources to conduct risk assessment and to take corrective actions, where required.

By the end of November 1999, the Company had assessed, replaced or remediated, and tested all the critical and non-critical business information systems. Also, all of the non-information technology (Non-IT) systems were assessed, tested or vendor certified, and replaced, where necessary. The Company's business units surveyed approximately 700 major suppliers and 500 major customers for their Year 2000 readiness efforts. Monitoring risk in this area continued through the fourth quarter of calendar 1999.

Contingency plans were developed to mitigate possible disruption in business operations that may result from the Year 2000 issue. These plans included carrying necessary materials and parts inventories, securing alternative sources of supply, adjusting of facility shutdown and start-up schedules, development of manual procedures to execute transactions and complete processes. Once developed, these contingency plans were continually refined, as additional information became available.

The Company commissioned third party reviews of its Y2K program, assessed the progress and identified areas where additional resources were needed. As a result of these reviews, the Company augmented the staff resources working on the Y2K program to address the requirements that were identified. The Company also retained a consultant to provide Y2K program coordination support for the corporate office, and to assist in the audit of readiness efforts at the business segments.

Year 2000 activities and associated costs were managed within each business unit. The historical costs of remediation, replacement, testing and other activities directly connected with Year 2000 issues incurred through the successful completion of the project were less than \$3.0 million. Although the Company believes that it successfully avoided any significant disruption from the Year 2000 issue relating to the century rollover, it will continue to monitor all critical systems for the appearance of delayed complications or disruptions, problems relating to the leap year and problems encountered through suppliers, customers and other third parties with whom Quanex deals. Although these and other unanticipated Year 2000 issues could have an adverse effect on the results of operations or financial condition of the Company, it is not possible to anticipate the extent of impact at this time..

#### EUROPEAN MONETARY UNION

Within Europe, the European Economic and Monetary Union (the "EMU") introduced a new currency, the Euro, on January 1, 1999. The new currency is in response to the EMU's policy of economic convergence to harmonize trade policy, eliminate business costs associated with currency exchange and to promote the free flow of capital, goods and services among the participating countries.

On January 1, 1999, the participating countries adopted the Euro as their local currency, initially available for currency trading on currency exchanges and non-cash (banking) transactions. The existing local currencies, or legacy currencies, will remain legal tender through January 1, 2002. Beginning on January 1, 2002, Euro-denominated bills and coins will be issued for cash transactions. For a period of six months from this date, both legacy currencies and the Euro will be legal tender. On or before July 1, 2002, the participating countries will withdraw all legacy currency and use exclusively the Euro.

At the current time, the Company does not believe that the conversion to the Euro will have a material impact on its business or its financial statements.

#### ITEM 7A. QUANTITATIVE/QUALITATIVE DISCLOSURE

The following discussion of the Company and its subsidiaries' exposure to various market risks contains "forward looking statements" that involve risks and uncertainties. These projected results have been prepared utilizing certain assumptions considered reasonable in light of information currently available to the Company. Nevertheless, because of the inherent unpredictability of interest rates, foreign currency rates and metal commodity prices as well as other factors, actual results could differ materially from those projected in such forward looking information. For a description of the Company's significant accounting policies associated with these activities, see Notes 1 and 16 to the Consolidated Financial Statements.



## Interest Rate Risk

The Company and its subsidiaries have a Revolving Credit Facility, Convertible Subordinated Debentures, interest rate swap agreements and other long-term debt which subject the Company to the risk of loss associated with movements in market interest rates.

At October 31, 1999 and 1998, the Company had fixed-rate debt totaling \$90 and \$101 million respectively. This debt is fixed-rate and, therefore, does not expose the Company to the risk of earnings loss due to changes in market interest rates (see Notes 11 and 16 to the Company's Consolidated Financial Statements). The conversion feature of the Company's Subordinated Debentures makes it impractical to estimate the effect of a hypothetical 10% change in interest rates. This is due to the high correlation between the market value of these instruments and the market value of the Company's common stock. In general, any changes in fair value would impact earnings and cash flows only if the Company were to reacquire all or a portion of these instruments in the open market prior to their maturity.

The Company and certain of its subsidiaries' floating-rate obligations total \$99 million at October 31, 1999 and 1998 (see Note 11 to the Company's Consolidated Financial Statements). The exposure of these obligations to increases in short-term interest rates is limited by interest rate swap agreements entered into by the Company. These swap agreements effectively fix the interest rate on all of the Company's variable rate debt, thus limiting the potential impact that increasing interest rates would have on earnings. Under these swap agreements, payments are made based on a fixed rate (\$50 million at 7.025%, and \$50 million at 6.755%) and received on a LIBOR based variable rate (6.21% and 5.22% at October 31, 1999 and 1998, respectively). At October 31, 1999 and 1998, the unrealized losses related to the interest rate swap agreements are \$2.0 and \$8.5 million. If the floating rates were to change by 10% from October 31 levels, the fair market value of these swaps would change by approximately \$1.9 and \$1.7 million as of October 31, 1999 and 1998, respectively. However, it should be noted that any change in value of these contracts, real or hypothetical, would be significantly offset by an inverse change in the value of the underlying hedged item.

## Foreign Currency Exchange Rate Risk

The Company is subject to significant exposure from fluctuations in US Dollar/Dutch Guilder exchange rates. As further described in Note 16 of the Consolidated Financial Statements, the Company utilizes foreign currency forward contracts to limit transactional exposure to changes in currency exchange rates. At October 31, 1999 the Company had no such contracts open as the transactional exposure was immaterial. As of October 31, 1998, the Company had 11 separate contracts maturing in monthly increments to purchase an aggregate notional amount of \$4.675 million in foreign currency. These forward contracts did not extend beyond September 30, 1999. Unrealized pretax gains on these forward contracts totaled approximately \$137 thousand at October 31, 1998. A hypothetical 10% change in applicable October 31, 1998 forward rates would increase or decrease the pretax gain by approximately \$463 thousand related to these positions. However, it should be noted that any change in value of these contracts, real or hypothetical, would be significantly offset by an inverse change in the value of the underlying hedged item.

In addition, the Company utilizes a range forward zero-cost agreement to protect its initial equity investment in its Netherlands subsidiary, Piper Impact Europe. This agreement, which was entered into with a major financial institution, has a notional value of 30 million guilders. By establishing minimum and maximum exchange rates, this agreement limits the potential devaluation of the Company's initial investment in its subsidiary while also limiting any potential appreciation. If, at the expiration date of the agreement, the Dutch guilder/US dollar exchange rate is within the range of 1.80 to 2.05, this agreement will expire at no cost to either party. At October 31, 1998, there was no financial statement impact as the exchange rate fell within the range. At October 31, 1999, the Company booked a gain to stockholder's equity of \$378 thousand. A hypothetical 10% increase in the October 31, 1999 and 1998 exchange rate would result in a positive adjustment to stockholders' equity of approximately \$1.3 million and \$10 thousand, respectively. In contrast, a hypothetical 10% decrease would result in a negative adjustment to stockholder's equity of approximately \$378 thousand and \$1.2 million, respectively. However, it should be noted that any change in the value of this agreement, real or hypothetical, would be significantly offset by an inverse change in the value of the underlying hedged position.

## Commodity Price Risk

In the normal course of business, the Company enters into long-term firm price aluminum sheet sales contracts. In order to hedge the risk of higher prices for the anticipated aluminum purchases required to fulfill these long-term contracts, the Company enters into long futures positions. At October 31, 1999 and 1998, the Company had open futures contracts at fair values of \$5.3 and \$3.3 million, respectively, and an unrealized gain of \$117 thousand and an unrealized loss of \$369 thousand, respectively, on such contracts. These contracts covered a notional volume of 7,716,170 and 5,511,557 pounds of aluminum. A hypothetical 10% change from the October 31, 1999 and 1998 average London Metal Exchange ("LME") ingot price of \$.688 and \$.60, respectively, per pound would increase or decrease the unrealized pretax losses related to these contracts by approximately \$530 and \$330 thousand, respectively. However, it should be noted that any change in the value of these contracts, real or hypothetical, would be significantly offset by an inverse change in the cost of purchased aluminum scrap.

## ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTAL DATA

## INDEPENDENT AUDITORS' REPORT

Board of Directors and Stockholders  
Quanex Corporation  
Houston, Texas

We have audited the accompanying consolidated balance sheets of Quanex Corporation and subsidiaries as of October 31, 1999 and 1998, and the related consolidated statements of income, stockholders' equity and cash flows for each of the three years in the period ended October 31, 1999. Our audits also included the financial statement schedule listed in the index at Item 14. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Quanex Corporation and subsidiaries as of October 31, 1999 and 1998, and the results of their operations and their cash flows for each of the three years in the period ended October 31, 1999 in conformity with generally accepted accounting principles. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ DELOITTE & TOUCHE LLP  
Deloitte & Touche LLP

Houston, Texas  
Date: November 19, 1999

## RESPONSIBILITY FOR FINANCIAL REPORTING

The accompanying consolidated financial statements of Quanex Corporation and subsidiaries were prepared by management, which is responsible for their integrity and objectivity. The statements were prepared in accordance with generally accepted accounting principles and include amounts that are based on management's best judgments and estimates.

Quanex's system of internal controls is designed to provide reasonable assurance, at justifiable cost, as to the reliability of financial records and reporting and the protection of assets. The system of controls provides for appropriate division of responsibility and the application of policies and procedures that are consistent with high standards of accounting and administration. Internal controls are monitored through recurring internal audit programs and are updated as our businesses and business conditions change.

The Audit Committee, composed solely of outside directors, determines that management is fulfilling its financial responsibilities by meeting periodically with management, Deloitte & Touche LLP, and Quanex's internal auditors, to review internal accounting control and financial reporting matters. The internal and independent auditors have free and complete access to the Audit Committee.

We believe that Quanex's system of internal controls, combined with the activities of the internal and independent auditors and the Audit Committee, provides reasonable assurance of the integrity of our financial reporting.

/s/ VERNON E. OECHSLE  
Vernon E. Oechsle  
Chairman and Chief Executive Officer

/s/ TERRY M. MURPHY  
Terry M. Murphy  
Vice President -- Finance and  
Chief Financial Officer

QUANEX CORPORATION  
CONSOLIDATED BALANCE SHEETS

ASSETS

	OCTOBER 31,	
	----- 1999	1998 -----
	( IN THOUSANDS )	
Current assets:		
Cash and equivalents.....	\$ 25,874	\$ 26,279
Accounts and notes receivable, less allowance for doubtful accounts of \$12,154,000 in 1999 and \$11,752,000 in 1998.....	87,204	85,166
Inventories.....	78,463	85,397
Deferred income taxes.....	19,146	11,560
Prepaid expenses.....	1,700	1,410
	-----	-----
Total current assets.....	212,387	209,812
Property, plant and equipment, net.....	406,841	395,054
Goodwill, net.....	48,990	52,281
Other assets.....	22,228	17,141
	-----	-----
	\$690,446	\$674,288
	=====	=====

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:		
Accounts payable.....	\$ 70,187	\$ 75,160
Accrued expense.....	54,305	56,125
Current maturities of long-term debt.....	10,545	12,248
Income taxes payable.....	1,103	3,300
	-----	-----
Total current liabilities.....	136,140	146,833
Long-term debt.....	179,121	188,302
Deferred pension credits.....	6,691	7,832
Deferred postretirement welfare benefits.....	7,490	7,092
Deferred income taxes.....	43,910	33,412
Other liabilities.....	16,033	18,773
	-----	-----
Total liabilities.....	389,385	402,244
Stockholders' equity:		
Preferred stock, no par value, 1,000,000 shares authorized; issued & outstanding -- none in 1999 and 1998.....	--	--
Common stock, \$.50 par value, 50,000,000 shares authorized; 14,269,800 shares in 1999 and 14,179,834 shares in 1998 issued.....	7,135	7,090
Common stock held by rabbi trust -- 94,606 shares in 1999 and no shares in 1998.....	(2,322)	--
Additional paid-in capital.....	110,317	108,624
Retained earnings.....	186,867	156,278
Unearned compensation.....	(171)	--
Accumulated other comprehensive income.....	(765)	52
	-----	-----
Total stockholders' equity.....	301,061	272,044
	-----	-----
	\$690,446	\$674,288
	=====	=====

See notes to consolidated financial statements.

QUANEX CORPORATION  
CONSOLIDATED STATEMENTS OF INCOME

	YEARS ENDED OCTOBER 31,		
	1999	1998	1997
	(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)		
Net sales.....	\$810,094	\$797,490	\$746,093
Costs and expenses:			
Cost of sales.....	639,911	647,179	610,412
Selling, general and administrative.....	53,104	47,713	43,375
Depreciation and amortization.....	45,322	41,834	37,298
Restructuring charge.....	--	58,500	--
Operating income.....	71,757	2,264	55,008
Other income (expense):			
Interest expense.....	(14,402)	(14,904)	(17,541)
Capitalized interest.....	1,611	4,398	3,539
Other, net.....	1,383	2,278	1,637
Income (loss) from continuing operations before income taxes and extraordinary gain.....	60,349	(5,964)	42,643
Income tax benefit (expense).....	(21,048)	2,087	(14,925)
Income (loss) from continuing operations and before extraordinary gain.....	39,301	(3,877)	27,718
Income from discontinued operations, net of income taxes...	--	--	5,176
Gain on sale of discontinued operations, net of income taxes.....	--	13,046	36,290
Income before extraordinary gain.....	39,301	9,169	69,184
Extraordinary gain on early extinguishment of debt, net of income taxes.....	415	--	--
Net income attributable to common stockholders.....	\$ 39,716	\$ 9,169	\$ 69,184
Earnings per common share:			
Basic:			
Continuing operations.....	\$ 2.76	\$ (0.27)	\$ 2.01
Discontinued operations.....	--	--	0.37
Gain on sale of discontinued operations.....	--	0.92	2.63
Extraordinary gain.....	0.03	--	--
Total basic net earnings.....	\$ 2.79	\$ 0.65	\$ 5.01
Diluted:			
Continuing operations.....	\$ 2.56	\$ (0.27)	\$ 1.90
Discontinued operations.....	--	--	0.31
Gain on sale of discontinued operations.....	--	.92	2.17
Extraordinary gain.....	0.03	--	--
Total diluted net earnings.....	\$ 2.59	\$ 0.65	\$ 4.38
Weighted average number of shares outstanding			
Basic.....	14,234	14,149	13,807
Diluted.....	16,776	14,149	16,725

See notes to consolidated financial statements.

## QUANEX CORPORATION

## CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

YEARS ENDED OCTOBER 31, 1999, 1998, AND 1997	COMMON STOCK		COMMON STOCK HELD BY RABBI TRUST	ADDITIONAL PAID-IN CAPITAL	RETAINED EARNINGS
	SHARES	AMOUNT			
(DOLLAR AMOUNTS IN THOUSANDS)					
BALANCE AT OCTOBER 31, 1996....	13,590,400	\$6,795		\$ 94,251	\$ 96,623
Comprehensive income:					
Net income.....	--	--		--	69,184
Adjustment for minimum pension liability (net of tax expense of \$112).....					
Foreign currency translation adjustment.....					
Total Comprehensive income.....					
Common dividends (\$.61 per share).....	--	--		--	(8,422)
Unearned compensation.....	--	--		--	--
Other.....	460,011	230		10,895	(857)
BALANCE AT OCTOBER 31, 1997....	14,050,411	\$7,025		\$105,146	\$156,528
Comprehensive income:					
Net income.....					9,169
Adjustment for minimum pension liability (net of tax benefit of \$500).....					
Foreign currency translation adjustment.....					
Total Comprehensive income.....					
Common dividends (\$.64 per share).....					(9,059)
Other.....	129,423	65		3,478	(360)
BALANCE AT OCTOBER 31, 1998....	14,179,834	\$7,090		\$108,624	\$156,278
Comprehensive income:					
Net income.....					39,716
Adjustment for minimum pension liability (net of tax expense of \$395).....					
Foreign currency translation adjustment.....					
Total Comprehensive income.....					
Common dividends (\$.64 per share).....					(9,124)
Common stock held by Rabbi Trust.....			(2,322)		
Other.....	89,966	45		1,693	(3)
BALANCE AT OCTOBER 31, 1999....	14,269,800	\$7,135	\$(2,322)	\$110,317	\$186,867

YEARS ENDED OCTOBER 31, 1999, 1998, AND 1997	OTHER COMPREHENSIVE INCOME			TOTAL STOCKHOLDERS' EQUITY
	MINIMUM PENSION LIABILITY	FOREIGN CURRENCY TRANSLATION	OTHER	
(DOLLAR AMOUNTS IN THOUSANDS)				
BALANCE AT OCTOBER 31, 1996....	\$ (475)	--	\$(185)	\$197,009
Comprehensive income:				
Net income.....				69,184
Adjustment for minimum pension liability (net of tax expense of \$112).....	177			177
Foreign currency translation adjustment.....		422		422
Total Comprehensive income.....				
Common dividends (\$.61 per share).....				(8,422)
Unearned compensation.....			185	185
Other.....	--	--	--	10,268
BALANCE AT OCTOBER 31, 1997....	\$ (298)	\$ 422	\$ 0	\$268,823
Comprehensive income:				
Net income.....				9,169
Adjustment for minimum pension liability (net of tax benefit of \$500).....	(782)			(782)

Foreign currency translation adjustment.....		710		710
				-----
Total Comprehensive income.....				9,097
Common dividends (\$.64 per share).....				(9,059)
Other.....	--	--	--	3,183
	-----	-----	-----	-----
BALANCE AT OCTOBER 31, 1998....	\$(1,080)	\$1,132	\$ 0	\$272,044
Comprehensive income:				
Net income.....				39,716
Adjustment for minimum pension liability (net of tax expense of \$395).....	618			618
Foreign currency translation adjustment.....		(1,435)		(1,435)
				-----
Total Comprehensive income.....				38,899
Common dividends (\$.64 per share).....				(9,124)
Common stock held by Rabbi Trust.....				(2,322)
Other.....			(171)	1,564
	-----	-----	-----	-----
BALANCE AT OCTOBER 31, 1999....	\$ (462)	\$ (303)	\$(171)	\$301,061

See notes to consolidated financial statements.



QUANEX CORPORATION  
CONSOLIDATED STATEMENTS OF CASH FLOW

	YEARS ENDED OCTOBER 31,		
	1999	1998	1997
(IN THOUSANDS)			
<b>OPERATING ACTIVITIES:</b>			
Net Income.....	\$ 39,716	\$ 9,169	\$ 69,184
Adjustments to reconcile net income to cash provided by operating activities:			
Income from discontinued operations (net of taxes).....	--	--	(5,176)
Gain on sale of discontinued operations (net of taxes).....	--	(13,046)	(36,290)
Restructuring charge (net of deferred taxes of \$20,475).....	--	38,025	--
Extraordinary gain on early extinguishment of debt.....	(638)	--	--
Depreciation and amortization.....	45,883	42,400	37,865
Deferred income taxes.....	10,150	6,059	7,545
Deferred pension and postretirement benefits.....	(429)	223	193
Changes in assets and liabilities net of effects from acquisitions and dispositions:			
Decrease (increase) in accounts and notes receivable...	(2,665)	3,664	2,957
Decrease (increase) in inventory.....	6,485	(10,994)	8,898
Increase (decrease) in accounts payable.....	(4,648)	(2,262)	112
Increase (decrease) in accrued expenses.....	(1,510)	(346)	2,919
Other, net.....	(14,656)	(8,822)	(8,868)
Cash provided by continuing operations.....	77,688	64,070	79,339
Cash provided by discontinued operations.....	--	--	89
Cash provided by operating activities.....	77,688	64,070	79,428
<b>INVESTMENT ACTIVITIES:</b>			
Acquisition of Decatur Aluminum Corp., net of cash and equivalents acquired.....	--	(9,573)	--
Acquisition of Advanced Metal Forming, C.V., net of cash and equivalents acquired.....	--	--	(33,584)
Acquisition of Piper Impact, Inc., net of cash and equivalents acquired.....	--	--	(5,575)
Net proceeds from sale of LaSalle Steel Company.....	--	1,366	63,900
Net proceeds from sale of the Tubing Operations.....	--	30,068	--
Capital expenditures, net of retirements.....	(60,848)	(58,513)	(68,916)
Capital expenditures of discontinued operations.....	--	--	(3,868)
Other, net.....	(1,832)	(3,168)	(1,550)
Cash (used) by investment activities.....	(62,680)	(39,820)	(49,593)
Cash provided by operating and investment activities...	15,008	24,250	29,835
<b>FINANCING ACTIVITIES:</b>			
Bank borrowings (repayments), net.....	1,035	(17,124)	(41,828)
Purchase of subordinated debentures.....	(8,799)	(1,500)	--
Common dividends paid.....	(9,124)	(9,059)	(8,422)
Issuance of common stock, net.....	1,567	3,183	10,453
Other, net.....	(60)	(429)	429
Cash (used) by financing activities.....	(15,381)	(24,929)	(39,368)
Effect of exchange rate changes on cash and equivalents.....	(32)	107	422
Decrease in cash and equivalents.....	(405)	(572)	(9,111)
Cash and equivalents at beginning of period.....	26,279	26,851	35,962
Cash and equivalents at end of period.....	\$ 25,874	\$ 26,279	\$ 26,851

See notes to consolidated financial statements.

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## 1. SIGNIFICANT ACCOUNTING POLICIES

## Principles of Consolidation

The consolidated financial statements include the accounts of Quanex Corporation and its subsidiaries (the "Company"), all of which are wholly owned. All significant intercompany balances and transactions have been eliminated in consolidation.

## Scope of Operations

The Company operates primarily in three industry segments: manufacturing of engineered steel bars, aluminum mill sheet products and engineered products. The Company's products include engineered steel bars, coiled aluminum sheet (mill finish and coated), aluminum and steel fabricated products and impact extrusions. The Company's manufacturing operations are conducted primarily in the United States.

## Revenues

The Company recognizes revenues when products are shipped and the title and risk of ownership pass to the customer.

## Statements of Cash Flows

The Company generally considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents. Similar investments with original maturities beyond three months are considered short-term investments. For fiscal years 1999, 1998 and 1997 cash paid for income taxes was \$22,005,000, \$20,860,000, and \$13,906,000, respectively. These amounts are before refunds of \$1,181,000, \$172,000, and \$471,000, respectively. Cash paid for interest for fiscal 1999, 1998 and 1997 was \$13,931,000, \$14,404,000, and \$17,964,000, respectively.

## Inventories

Inventories are valued at the lower of cost or market. The accounting methods used in valuing the Company's inventories are described in Note 8.

## Long-Lived Assets

Property, plant and equipment is stated at cost and is depreciated using the straight-line method over the estimated useful lives of the assets. The estimated useful lives of certain categories are as follows:

	YEARS -----
Land improvements.....	10 to 25
Buildings.....	10 to 40
Machinery and equipment.....	3 to 20

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Goodwill represents the excess of the purchase price over the fair value of acquired companies and is being amortized on a straight line basis over forty years for the goodwill resulting from the acquisition of Nichols Homeshield in 1989, and over twenty-five years for the goodwill resulting from the acquisitions of Piper Impact Europe B.V. ("Piper Impact Europe") in 1997 and Nichols Aluminum Alabama, Inc. in 1998 (See Note 2). Goodwill from the acquisition of Piper Impact, Inc. ("Piper Impact") in 1996 was being amortized over 25 years, however, during the fourth quarter of 1998, the balance of goodwill associated with Piper Impact was written off in accordance with Statement of Financial Accounting Standard ("SFAS") No. 121. (See Note 4) At October 31, 1999 and 1998, accumulated amortization was \$11,035,000, and \$9,255,000, respectively.

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. (See Note 4 -- regarding the impact of this statement.)

#### Hedging

The Company enters into various derivative instruments to protect itself from fluctuating prices and rates. The Company uses futures contracts to hedge a portion of its exposure to price fluctuations of aluminum. Hedging gains and losses are recognized concurrently with related sales transactions. The Company enters into interest rate swap agreements, which effectively exchange variable interest rate debt for fixed interest rate debt. The agreements are used to reduce the exposure to possible increases in interest rates. The Company enters into these swap agreements with major financial institutions. The Company uses foreign currency swap agreements to protect the value of its investment in Piper Impact Europe as well as to protect itself from currency fluctuations on certain sales and purchases. The impact of the foreign currency instruments which protect the investment in Piper Impact Europe are recorded as a foreign currency translation adjustment in the equity section of the financial statements when exchange rates go outside of the limits. The gains and losses on the forward contracts related to the sales and purchases are deferred off-balance sheet and included as a component of the related transaction when recorded. (See Note 16)

#### Earnings Per Share Data

Basic earnings per share excludes dilution and is computed by dividing net income available to common stockholders by the weighted average number of common shares outstanding for the period. Diluted earnings per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity.

#### Foreign Currency Translation

Assets and liabilities of foreign subsidiaries are translated into U.S. dollars at year-end exchange rates, and income and expense items are translated at the average exchange rates for the year. Resulting translation adjustments are reported as a separate component of stockholders' equity.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## Use of Estimates

The preparation of the financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

## Reclassification

Certain amounts for prior periods have been reclassified in the accompanying consolidated financial statements to conform to fiscal 1999 presentations.

## New Accounting Pronouncements

In June 1997, the Financial Accounting Standards Board ("FASB") issued SFAS No. 130, "Reporting Comprehensive Income", which establishes standards for the reporting and displaying of comprehensive income and its components. The Company has adopted this pronouncement as of October 31, 1999 and the accompanying consolidated financial statements are presented in accordance with this statement.

In February 1998, the FASB issued SFAS No. 132, "Employer's Disclosures about Pensions and Other Postretirement Benefits", which defines new disclosure requirements for pension and other postretirement benefits in an effort to facilitate financial analysis by adding useful information and deleting disclosures that the FASB considers no longer useful. The Company has adopted this pronouncement as of October 31, 1999 and disclosures required by this statement have been made in Note 13 for all periods presented.

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities", which is effective for the Company's year ending October 31, 2000. This statement establishes accounting and reporting standards for derivative instruments, including certain derivative instruments embedded in other contracts, and for hedging activities. In June 1999, the FASB issued SFAS No. 137, "Accounting for Derivative Instruments and Hedging Activities -- Deferral of the Effective Date of FASB Statement No. 133" which defers the effective date of SFAS No. 133 until the Company's year ending October 31, 2001. The Company will be analyzing SFAS No. 133 to determine what, if any, impact or additional disclosure requirements this pronouncement will have.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 2. ACQUISITIONS

On October 29, 1997, the Company, through its Dutch subsidiary, Piper Impact Europe, acquired the net assets of Advanced Metal Forming C.V., a Dutch limited partnership, for approximately \$30 million. Goodwill associated with Piper Impact Europe is approximately NLG 26 million or \$12 million. The income statement for the year ended October 31, 1997 does not include the operations of Piper Impact Europe.

Piper Impact Europe produces aluminum impact extrusions and precision steel stampings for the automotive and electronics industries in Europe and North America. Piper Impact Europe employs approximately 300 people, and its manufacturing facilities are located near Zwolle in The Netherlands.

On October 9, 1998, the Company acquired the stock of Decatur Aluminum Corp., a Decatur, Alabama based coiled aluminum sheet manufacturer for approximately \$19 million. Included in the purchase price was debt totaling \$5 million and other specified liabilities for \$5 million assumed by the Company. The newly acquired company has been renamed Nichols Aluminum-Alabama, Inc. ("Nichols Aluminum Alabama"), in alignment with Quanex's other aluminum mill sheet businesses in its Nichols Aluminum division. Goodwill associated with Nichols Aluminum Alabama is approximately \$10 million. Nichols Aluminum Alabama's operations include cold rolling aluminum sheet to specific gauge, annealing, leveling, custom painting and slitting to width.

## 3. DISCONTINUED OPERATIONS

In April 1997, the Company completed the sale of its LaSalle Steel Company ("LaSalle") subsidiary. The Company recorded an after tax gain on the sale of \$36,290,000 in the second quarter of fiscal 1997. During 1998, an additional after tax gain of \$668,000 was recorded as a result of post-closing adjustments. LaSalle's results of operations have been classified as discontinued operations and prior periods have been restated. For business segment reporting purposes, LaSalle's data was previously reported as the segment "Cold Finished Steel Bars".

In December 1997, the Company completed the sale of its tubing operations, comprised of Michigan Seamless Tube, Gulf States Tube, and the Tube Group Administrative Office ("Tubing Operations"). The sale was effective November 1, 1997. The Company recorded an after tax gain on the sale of \$12,378,000 during fiscal 1998. Included in the gain is an accrual for the Company's best estimate of potential environmental clean-up costs at one of the discontinued operating facilities. Results of these operations have been classified as discontinued and prior periods have been restated. For business segment reporting purposes, Tubing Operations were previously classified as "Steel Tubes".

Net sales and income from discontinued operations are as follows:

	YEAR ENDED OCTOBER 31, 1997 ----- (IN THOUSANDS)
Net sales.....	\$187,123
Operating income.....	7,962
Income tax expense.....	(2,786)
Income from discontinued operations.....	\$ 5,176

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 4. PIPER IMPACT IMPAIRMENT DISCLOSURE

During the year ended October 31, 1998, the Company recorded a restructuring charge of \$58.5 million related to its subsidiary, Piper Impact.

Components of this special charge include \$51.2 million for goodwill impairment; \$6.7 million for impairment of property, plant and equipment; and \$600 thousand for severance benefits to be paid to employees of the Park City, Utah plant. Piper Impact experienced significant changes in market conditions and the relationship with its major customer in fiscal 1998, which led to substantial declines in sales and operating cash flow. Management began an evaluation of the operations of Piper Impact in August 1998. As a result of this evaluation, in September 1998, management approved a plan to close the Park City, Utah facility and move its production to the New Albany, Mississippi facility. Production ceased at the Utah facility and its operations were consolidated in Mississippi by May 1999.

Due to the significance of the changes discussed above and the decision to close one of the acquired production facilities, management performed an evaluation of the recoverability of all of the assets of Piper Impact, excluding the new steel plant, as described in Statement of Financial Accounting Standards No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of". Management concluded from the results of this evaluation that a significant impairment of intangible as well as long-lived assets had occurred. An impairment charge was required because estimated fair value was less than the carrying value of the assets. Considerable management judgment is necessary to estimate fair value. Accordingly, actual results could vary significantly from management's estimates.

The one-time restructuring charge resulted in an after-tax impact on net income of \$38 million or \$2.68 per share.

## 5. EXTRAORDINARY ITEM

During fiscal 1999, the Company accepted unsolicited block offers to buy back \$9.7 million principal amount of the 6.88% Convertible Subordinated Debentures for \$8.8 million in cash. An after tax extraordinary gain of \$415 thousand was recorded on these transactions in the second fiscal quarter of 1999.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 6. EARNINGS PER SHARE

The computational components of basic and diluted earnings per share are as follows (Shares and dollars in thousands except per share amounts):

	FOR THE YEAR ENDED OCTOBER 31, 1999		
	NUMERATOR (INCOME)	DENOMINATOR (SHARES)	PER SHARE AMOUNT
BASIC EPS			
Income from continuing operations.....	\$39,301	14,234	\$2.76
Extraordinary gain on early extinguishment of debt.....	415		0.03
	-----		-----
Total basic net income.....	\$39,716		\$2.79
	=====		=====
EFFECT OF DILUTIVE SECURITIES			
Effect of common stock equivalents arising from stock options.....	--	56	
Effect of common stock held by rabbi trust.....	--	16	
Effect of conversion of subordinated debentures...	3,663	2,470	
	-----	-----	
DILUTED EPS			
Income from continuing operations.....	42,964	16,776	\$2.56
		=====	
Extraordinary gain on early extinguishment of debt.....	415		0.03
	-----		-----
Total diluted net income.....	\$43,379		\$2.59
	=====		=====

	FOR THE YEAR ENDED OCTOBER 31, 1998		
	NUMERATOR (INCOME)	DENOMINATOR (SHARES)	PER SHARE AMOUNT
BASIC EPS			
Loss from continuing operations.....	\$(3,877)	14,149	\$(0.27)
Gain on sale of discontinued operations.....	13,046		\$ 0.92
	-----		-----
Total basic net income.....	\$ 9,169		\$ 0.65
	=====		=====
EFFECT OF DILUTIVE SECURITIES			
Effect of common stock equivalents arising from stock options(1).....	--	--	
Effect of conversion of subordinated debentures(1).....	--	--	
	-----	-----	
DILUTED EPS			
Loss from continuing operations.....	\$(3,877)	14,149	\$(0.27)
		=====	
Gain on sale of discontinued operations.....	13,046		\$ 0.92
	-----		-----
Total diluted net income.....	\$ 9,169		\$ 0.65
	=====		=====

(1) The effect of both common stock equivalents arising from stock options and the conversion of subordinated debentures was anti-dilutive.

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

	FOR THE YEAR ENDED OCTOBER 31, 1997		
	NUMERATOR	DENOMINATOR	PER SHARE
	(INCOME)	(SHARES)	AMOUNT
	-----	-----	-----
BASIC EPS			
Income from continuing operations.....	\$27,718	13,807	\$2.01
Income from discontinued operations.....	5,176		0.37
Gain on sale of discontinued operations.....	36,290		2.63
	-----		-----
Total basic net income.....	\$69,184		\$5.01
	=====		=====
EFFECT OF DILUTIVE SECURITIES			
Effect of common stock equivalents arising from stock options.....		222	
Effect of conversion of subordinated debentures...	\$ 3,997	2,696	
	-----	-----	
DILUTED EPS			
Income from continuing operations.....	\$31,715	16,725	\$1.90
		=====	
Income from discontinued operations.....	5,176		0.31
Gain on sale of discontinued operations.....	36,290		2.17
	-----		-----
Total diluted net income.....	\$73,181		\$4.38
	=====		=====



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 7. INCOME TAXES

Income taxes are provided on taxable income at the statutory rates applicable to such income.

Income tax expense (benefit) consists of the following:

	YEARS ENDED OCTOBER 31,		
	1999	1998	1997
	----- (IN THOUSANDS) -----		
Current:			
Federal.....	\$17,819	\$ 9,312	\$ 846
State.....	1,066	4,190	2,829
Foreign.....	(372)	507	--
	-----	-----	-----
	18,513	14,009	3,675
Deferred.....	2,535	(16,096)	11,250
	-----	-----	-----
Income taxes from continuing operations.....	21,048	(2,087)	14,925
Income taxes from discontinued operations.....	--	--	2,786
Income taxes from sale of discontinued operations.....	--	3,441	13,178
Income taxes from extinguishment of debt.....	223	--	--
	-----	-----	-----
Total.....	\$21,271	\$ 1,354	\$30,889
	=====	=====	=====

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes.

Significant components of the Company's net deferred tax liability are as follows:

	OCTOBER 31,	
	1999	1998
	----- (IN THOUSANDS) -----	
Deferred tax liability:		
Property, plant and equipment.....	\$ 51,477	\$ 44,723
Inventory.....	(573)	(1,161)
Other.....	16,085	16,926
	-----	-----
	66,989	60,488
Deferred tax assets:		
Intangibles.....	14,411	19,678
Postretirement benefit obligation.....	3,345	3,149
Other employee benefit obligations.....	9,448	9,314
Other.....	15,021	6,495
	-----	-----
	42,225	38,636
Net deferred tax liability.....	\$ 24,764	\$ 21,852
	=====	=====
Deferred income tax non-current liability.....	\$ 43,910	\$ 33,412
Deferred tax current assets.....	(19,146)	(11,560)
	-----	-----
Net deferred tax liability.....	\$ 24,764	\$ 21,852
	=====	=====

Deferred taxes have not been provided on the Company's foreign subsidiary's cumulative undistributed earnings of \$241,000, since such amounts are expected to be reinvested indefinitely. If these earnings were remitted to the Company, there would be little or no additional federal income tax because of the availability of foreign tax credits.

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Income tax expense (benefit) differs from the amount computed by applying the statutory federal income tax rate to income from continuing operations before income taxes for the following reasons:

	YEARS ENDED OCTOBER 31,		
	1999	1998	1997
	----- (IN THOUSANDS) -----		
Income tax expense (benefit) at statutory tax rate.....	\$21,123	\$(2,087)	\$14,925
Increase (decrease) in taxes resulting from:			
State income taxes, net of federal effect.....	1,118	(250)	1,655
Goodwill.....	334	345	334
Other items, net.....	(1,527)	(95)	(1,989)
	\$21,048	\$(2,087)	\$14,925
	=====	=====	=====

The Company reached a settlement with the Internal Revenue Service with respect to its tax audit of fiscal years 1992 through 1994. During 1997, the Company made a payment of \$2,016,000 of tax and related interest. Adequate provisions had been made in prior years and the settlement did not have a material effect on earnings for fiscal 1997. The Company's 1996 tax year is currently under audit.

## 8. INVENTORIES

Inventories consist of the following:

	OCTOBER 31,	
	1999	1998
	----- (IN THOUSANDS) -----	
Raw materials.....	\$24,617	\$25,167
Finished goods and work in process.....	46,958	52,485
	71,575	77,652
Other.....	6,888	7,745
Total.....	\$78,463	\$85,397
	=====	=====

The values of inventories in the consolidated balance sheets are based on the following accounting methods:

LIFO.....	\$58,968	\$57,594
FIFO.....	19,495	27,803
Total.....	\$78,463	\$85,397
	=====	=====

With respect to inventories valued using the LIFO method, replacement cost exceeded the LIFO value by approximately \$11,300,000 and \$12,300,000 at October 31, 1999 and 1998, respectively.

At the beginning of fiscal 1999, Quanex changed its inventory valuation method for measuring segment results from LIFO to FIFO. The change has no impact on consolidated results, which remain LIFO based. See Note 13 regarding industry segment information.

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 9. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following:

	OCTOBER 31,	
	1999	1998
	-----	
	(IN THOUSANDS)	
Land and land improvements.....	\$ 18,502	\$ 18,376
Buildings.....	101,166	100,009
Machinery and equipment.....	591,942	545,677
Construction in progress.....	42,201	38,893
	-----	
	753,811	702,955
Less accumulated depreciation and amortization.....	(346,970)	(307,901)
	-----	
	\$ 406,841	\$ 395,054
	=====	=====

The Company had commitments for the purchase or construction of capital assets amounting to approximately \$15 million at October 31, 1999.

## 10. ACCRUED EXPENSES

Accrued expenses consist of the following:

	OCTOBER 31,	
	1999	1998
	-----	
	(IN THOUSANDS)	
Accrued contribution to pension funds.....	\$ 1,783	\$ 1,125
Interest.....	2,364	2,544
Payroll, payroll taxes and employee benefits.....	28,745	24,497
State and local taxes.....	2,288	1,942
Other.....	19,125	26,017
	-----	
	\$54,305	\$56,125
	=====	=====

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 11. LONG-TERM DEBT AND FINANCING ARRANGEMENTS

Long-term debt consists of the following:

	OCTOBER 31,	
	1999	1998
	(IN THOUSANDS)	
"Bank Agreement" Revolver.....	\$ 75,000	\$ 80,000
Convertible subordinated debentures.....	73,720	83,420
Piper Impact Europe "Credit Facility".....	22,703	22,363
Industrial Revenue and Economic Development Bonds, unsecured, payable in annual installments through the year 2005, bearing interest ranging from 6.50% to 8.375%.....	3,275	3,275
State of Alabama Industrial Development Bonds.....	4,755	4,755
Scott County, Iowa Industrial Waste Recycling Revenue Bonds.....	3,000	--
Other.....	7,213	6,737
	-----	-----
	\$189,666	\$200,550
Less maturities due within one year included in current liabilities.....	10,545	12,248
	-----	-----
	\$179,121	\$188,302
	=====	=====

In July 1996, the Company entered into an unsecured \$250 million Revolving Credit and Term Loan Agreement ("Bank Agreement"). The Bank Agreement consists of a revolving line of credit ("Revolver"). In July 1997, the term loan provisions of the Bank Agreement expired. The Bank Agreement expires July 23, 2003, and provides for up to \$25 million for standby letters of credit, limited to the undrawn amount available under the Revolver. All borrowings under the Revolver bear interest, at the option of the Company, at either (a) the prime rate or the federal funds rate plus one percent, whichever is higher, or (b) a Eurodollar based rate. At October 31, 1999 and 1998, the Company had \$75 and \$80 million, respectively, outstanding under the Revolver. The weighted average interest rates on borrowings under the Revolver were 5.7%, 6.2%, and 6.6% in 1999, 1998 and 1997, respectively. As of October 31, 1999, the Company was in compliance with all Bank Agreement covenants. Under the Company's most restrictive loan covenants, retained earnings of approximately \$48 million at October 31, 1999 were available for dividends and other restricted payments.

On June 30, 1995, the Company exercised its right under the terms of its Cumulative Convertible Exchangeable Preferred Stock to exchange such stock for an aggregate of \$84,920,000 of its 6.88% Convertible Subordinated Debentures due June 30, 2007 ("Debentures"). Interest is payable semi-annually on June 30 and December 31 of each year. The Debentures are subject to mandatory annual sinking fund payments sufficient to redeem 25% of the Debentures issued on each of June 30, 2005 and June 30, 2006, to retire a total of 50% of the Debentures before maturity. The Debentures are subordinate to all senior indebtedness of the Company and are convertible, at the option of the holder, into shares of the Company's common stock at a conversion price of \$31.50 per share.

During fiscal 1999 and 1998, respectively, the Company accepted unsolicited block offers to buy back \$9.7 and \$1.5 million, respectively, principal amount of its Convertible Subordinated Debentures. The outstanding balance as of October 31, 1999 is \$73,720,000.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

On October 28, 1997, Piper Impact Europe executed a stand-alone secured credit facility ("Credit Facility") providing an initial available credit line of 50 million Dutch Guilders ("NLG"). The available credit line is reduced each quarter by the principal payments on the Medium Term Loan described below. At October 31, 1999, the available credit line was 48 million NLG. At October 31, 1999 and 1998, 1 NLG was equal to .477 and .535 U.S. dollars, respectively. The Credit Facility consists of a Roll-Over Term Loan, a Medium Term Loan and an Overdraft Facility. The Roll-Over Term Loan provides NLG 15 million for loan periods of 1, 2, 3, 6, or 12 months with repayment of outstanding borrowings on October 27, 2002. Interest is payable on the repayment date at the Amsterdam Interbank Offering Rate (AIBOR) plus 90 basis points. In the case of a loan period of twelve months, interest is payable six months after the beginning of the loan period and on the repayment date. The Medium Term Loan provides NLG 15 million at 6.375% payable quarterly in arrears from March 1, 1998, with quarterly repayments of principal in equal amounts of NLG 500 thousand commencing January 1, 1999 through April 1, 2006. The Overdraft Facility provides an aggregate amount of NLG 20 million to cover overdrafts or up to NLG 15 million of loans for a period of one year, subject to annual renewal. Overdrafts bear interest at the Bank's published rate for overdraft facilities plus 1% per annum. Loans under the Overdraft Facility bear interest at AIBOR plus 45 to 55 basis points. The terms of Overdraft Facility loans are selected by Piper Impact Europe to be a period of 1, 2, 3, 6, or 12 months. Interest on overdrafts is paid quarterly in arrears.

Interest on loans under the Overdraft Facility is payable on the repayment date, however, in the case of a loan period of twelve months, interest is payable six months after the beginning of the loan period and on the repayment date. At October 31, 1999, and 1998, Piper Impact Europe had NLG 47.6 and 41.8 million, respectively, outstanding under the Credit Facility. As of October 31, 1999, Piper Impact Europe was in compliance with all Credit Facility covenants.

The State of Alabama Industrial Development bonds were assumed as part of the Nichols Aluminum Alabama acquisition (See Note 2). These bonds mature August 1, 2004 with interest payable monthly. The bonds bear interest at the weekly interest rate as determined by the remarketing agent under then prevailing market conditions to be the minimum interest rate, which, if borne by the Bonds on the effective date of such rate, would enable the remarketing agent to sell the Bonds on such business day at a price (without regard to accrued interest) equal to the principal amount of the bonds. The interest rate, however, may not exceed 13% per annum. The weekly interest rate during the year ended October 31, 1999 ranged from 2.45% to 4.25%. These bonds are secured by a Letter of Credit.

On June 1, 1999, the Company borrowed \$3 million through unsecured Scott County, Iowa Variable Rate Demand Industrial Waste Recycling Revenue Bonds Series 1999. The bonds require 15 annual principal payments of \$200 thousand beginning on July 1, 2000. The variable interest rate is established by the remarketing agent based on the lowest weekly rate of interest that would permit the sale of the bonds at par, on the basis of prevailing financial market conditions. Interest is payable on the first business day of each calendar month. Interest rates on these bonds during the five months that they have been outstanding in fiscal 1999 have ranged from 3.0% to 4.0%.

Aggregate maturities of long-term debt at October 31, 1999, are as follows (in thousands):

2000.....	\$ 10,545
2001.....	1,202
2002.....	8,359
2003.....	76,203
2004.....	12,727
Thereafter.....	80,630
	-----
	\$189,666
	=====

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 12. PENSION PLANS AND OTHER POSTRETIREMENT BENEFITS

The Company has a number of retirement plans covering substantially all employees. The Company provides both defined benefit and defined contribution plans. In general, the plant or location of his/her employment determines an employee's coverage for retirement benefits. The single employer defined benefit pension plans pay benefits to employees at retirement using formulas based upon years of service and compensation rates near retirement. The Company's funding policy is generally to make the minimum annual contributions required by applicable regulations. The plans invest primarily in marketable equity and debt securities.

The Company also provides certain healthcare and life insurance benefits for certain eligible retired employees employed prior to January 1, 1993. Certain employees may become eligible for those benefits if they reach normal retirement age while working for the Company. The Company continues to fund benefit costs on a pay-as-you-go basis; and, for fiscal year 1999, the Company made benefit payments totaling \$348,000, compared to \$410,000 and \$247,000 in fiscal 1998 and 1997, respectively.

In fiscal 1999, the Company adopted SFAS No. 132, "Employers' Disclosures about Pensions and Other Postretirement Benefits", which revises disclosures about pension and other postretirement benefits. The following information is provided in accordance with the requirements of this Statement.

A reconciliation of the beginning benefit obligation to the ending benefit obligation follows:

	PENSION BENEFITS		POSTRETIREMENT BENEFITS	
	1999	1998	1999	1998
	OCTOBER 31,			
	(IN THOUSANDS)			
Benefit obligation at beginning of year.....	\$27,665	\$21,960	\$7,984	\$6,611
Service cost.....	2,092	1,832	187	163
Interest cost.....	1,978	1,685	541	523
Amendments.....	818	38	--	--
Actuarial loss (gain).....	(2,111)	2,854	(633)	1,103
Benefits paid from plan assets.....	(556)	(385)	(348)	(410)
Administrative expenses.....	(298)	(321)	--	--
Foreign currency translation effect.....	(122)	--	--	--
Piper Impact Europe benefit obligation.....	1,098	--	--	--
Other.....	--	2	--	(6)
Benefit obligation at end of year.....	<u>\$30,564</u>	<u>\$27,665</u>	<u>\$7,731</u>	<u>\$7,984</u>

A reconciliation of the beginning fair value of plan assets to the ending fair value of plan assets follows:

	PENSION BENEFITS	
	1999	1998
	OCTOBER 31,	
	(IN THOUSANDS)	
Fair value of plan assets at beginning of year.....	\$17,692	\$16,253
Actual return on plan assets.....	2,491	433
Employer contributions.....	2,240	1,712
Employee contributions.....	47	--
Ins. premiums paid for surviving spouse coverage.....	(15)	--
Benefits paid.....	(556)	(385)
Administrative expenses.....	(298)	(321)
Foreign currency translation effect.....	(77)	--
Piper Impact Europe fair value of plan assets.....	681	--
Fair value of plan assets at end of year.....	<u>\$22,205</u>	<u>\$17,692</u>

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

A reconciliation of the funded status of the plans with the amounts recognized in the accompanying balance sheets is set forth below:

	PENSION BENEFITS		POSTRETIREMENT BENEFITS	
	OCTOBER 31,			
	1999	1998	1999	1998
	(IN THOUSANDS)			
Funded status.....	\$(8,359)	\$(9,973)	\$(7,731)	\$(7,984)
Unrecognized transition asset.....	(602)	(713)	--	--
Unrecognized prior service cost.....	1,344	591	--	--
Unrecognized net loss.....	1,363	3,683	238	888
Foreign currency translation effect.....	(12)	--	--	--
Other.....	22	--	3	4
Accrued benefit cost.....	(6,244)	(6,412)	(7,490)	(7,092)
Amounts recognized in the Balance Sheet:				
Deferred benefit credit.....	(6,691)	(7,832)	(7,490)	(7,092)
Accrued contribution to pension.....	(1,783)	(1,125)	--	--
Intangible asset.....	1,473	774	--	--
Accumulated other comprehensive income.....	757	1,771	--	--
Accrued benefit cost.....	\$(6,244)	\$(6,412)	\$(7,490)	\$(7,092)

Below is data related to pension plans in which accumulated benefit obligation exceeds plan assets.

	PENSION BENEFITS		POSTRETIREMENT BENEFITS	
	OCTOBER 31,			
	1999	1998	1999	1998
	(IN THOUSANDS)			
Accumulated benefit obligation.....	\$7,319	\$21,405	\$7,731	\$7,984
Fair value of plan assets.....	5,576	17,692	--	--

Below are the assumptions used.

	PENSION BENEFITS			POSTRETIREMENT BENEFITS		
	OCTOBER 31,					
	1999	1998	1997	1999	1998	1997
	(IN THOUSANDS)					
Discount rate.....	7.50%	6.75%	7.50%	7.50%	6.75%	7.50%
Expected return on plan assets....	10.00%	10.00%	10.00%	--	--	--
Rate of compensation increase.....	4.50%	4.00%	4.50%	--	--	--

The assumed health care cost trend rate was 7.5% in 1999, decreasing uniformly to 5.50% in the year 2003 and remaining level thereafter. If the health care cost trend rate assumptions were increased by 1%, the accumulated postretirement benefit obligation as of October 31, 1999 would be increased by 1.85%. The effect of this change on the sum of the service cost and interest cost would be an increase of 1.44%. If the health care cost trend rate assumptions were decreased by 1%, the accumulated postretirement benefit obligation as of October 31, 1999 would be decreased by 1.65%. The effect of this change on the sum of the service cost and interest cost would be a decrease of 1.27%.

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

Net pension costs for the single employer defined benefit pension plans were as follows:

	YEARS ENDED OCTOBER 31,		
	1999	1998	1997
	----- (IN THOUSANDS) -----		
Service Cost.....	\$ 2,092	\$ 1,832	\$ 1,371
Interest cost.....	1,978	1,685	1,511
Expected return on plan assets.....	(1,978)	(1,670)	(1,354)
Amortization of unrecognized transition asset.....	(111)	(111)	(47)
Amortization of unrecognized prior service cost.....	63	25	57
Amortization of unrecognized net loss.....	119	7	33
Other.....	(63)	--	--
	-----		
Net periodic pension cost.....	\$ 2,100	\$ 1,768	\$ 1,571
	=====	=====	=====

Net periodic costs for the postretirement benefit plans other than pensions were as follows:

	YEARS ENDED OCTOBER 31,		
	1999	1998	1997
	----- (IN THOUSANDS) -----		
Net periodic postretirement benefit cost:			
Service cost.....	\$187	\$163	\$148
Interest cost.....	541	523	472
Net amortization and deferral.....	17	(10)	3
Other.....	2	--	--
	-----		
Net periodic postretirement benefit cost.....	\$747	\$676	\$623
	=====	=====	=====

One of the Company's subsidiaries, Piper Impact Europe, participates in two multi-employer plans. The plans provide defined benefits to substantially all of Piper Impact Europe's employees. Amounts charged to pension cost and contributed to the plans as of October 31, 1999 and 1998 totaled approximately NLG 2,021,000 and NLG 1,551,000 or approximately \$1,000,000 and \$800,000, respectively. There was no pension cost in 1997 for these plans as Piper Impact Europe was acquired on October 29, 1997. (See Note 2)

The Company has various defined contribution plans in effect for certain eligible employees. The Company makes contributions to the plans subject to certain limitations outlined in the plans. Contributions to these plans were approximately \$3,366,000, \$2,978,000, and \$2,919,000, during fiscal 1999, 1998, and 1997, respectively.

The Company has a Supplemental Benefit Plan covering certain key officers of the Company. Earned vested benefits under the Supplemental Benefit Plan were approximately \$4,829,000, \$4,147,000, and \$3,724,000 at October 31, 1999, 1998 and 1997, respectively. These benefits are funded with life insurance policies purchased by the Company.



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 13. INDUSTRY SEGMENT INFORMATION

The Company adopted SFAS No. 131, "Disclosures about Segments of an Enterprise and Related Information", for fiscal year ended 1998. SFAS No. 131 requires that the Company disclose certain information about its operating segments where operating segments are defined as "components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance". Generally, financial information is required to be reported on the basis that it is used internally for evaluating segment performance and deciding how to allocate resources to segments.

Pursuant to SFAS No. 131, the Company has three reportable segments: engineered steel bars, aluminum mill sheet products, and engineered products. The Company's previously reported "Aluminum Products Group" has been split into two segments: "Aluminum Mill Sheet Products" and "Engineered Products". Prior years' presentation has been restated to conform to the new segment reporting. The engineered steel bar segment consists of engineered steel bars manufacturing, steel bar and tube heat treating services and steel bar and tube wear and corrosion resistant finishing services. The aluminum mill sheet segment manufactures mill finished and coated aluminum sheet. The engineered products segment manufactures impact-extruded aluminum and steel parts, aluminum window and patio door screens, window frames and other roll formed products and stamped shapes.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies, with the exception of the inventory valuation method. At the beginning of fiscal year 1999, Quanex changed its inventory valuation method for measuring segment results from LIFO to FIFO. This change has no impact on consolidated results, which remain LIFO based. Prior years' data have not been restated, however, information is provided below to allow comparability.

The Company accounts for intersegment sales and transfers as if the sales or transfers were to third parties, that is, at current market prices.

The Company's reportable segments are strategic business divisions that offer different products and services. These groups are managed separately because each business requires different expertise and marketing strategies. The Company evaluates performance based on operating income.

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

For the year-ended October 31, 1999, 12% of the Company's consolidated net sales were made to one customer. These sales are included in the engineered products segment.

YEAR ENDED OCTOBER 31, 1999	ENGINEERED STEEL BARS	ALUMINUM MILL SHEET PRODUCTS	ENGINEERED PRODUCTS	CORPORATE & OTHER(1)	CONSOLIDATED
(IN THOUSANDS)					
Net Sales:					
To unaffiliated companies.....	\$292,085	\$290,648	\$227,361	--	\$810,094
Intersegment(2).....	5,284	21,115	1	(26,400)	--
Total.....	\$297,369	\$311,763	\$227,362	\$(26,400)	\$810,094
Operating Income (loss).....	\$ 60,446	\$ 15,306	\$ 12,153	\$(16,148)	\$ 71,757
Depreciation and amortization:					
Operating.....	\$ 16,293	\$ 12,313	\$ 16,185	\$ 531	\$ 45,322
Other.....	--	21	--	540	561
Total.....	\$ 16,293	\$ 12,334	\$ 16,185	\$ 1,071	\$ 45,883
Capital expenditures(3).....	\$ 37,750	\$ 9,873	\$ 12,628	\$ 683	\$ 60,934
Identifiable assets.....	\$241,783	\$200,733	\$209,153	\$ 38,777	\$690,446

(1) Included in "Corporate and Other" are intersegment eliminations, and corporate expenses.

(2) Intersegment sales are conducted on an arm's-length basis.

(3) Includes capitalized interest.

For the year-ended October 31, 1998, 13% of the Company's consolidated net sales were made to one customer. These sales are included in the engineered products segment.

YEAR ENDED OCTOBER 31, 1998	ENGINEERED STEEL BARS	ALUMINUM MILL SHEET PRODUCTS(1)	ENGINEERED PRODUCTS(4)	CORPORATE & OTHER(2)	CONSOLIDATED(4)
(IN THOUSANDS)					
Net Sales:					
To unaffiliated companies.....	\$324,312	\$243,168	\$230,010	--	\$797,490
Intersegment(3).....	2,984	23,187	2	(26,173)	--
Total.....	\$327,296	\$266,355	\$230,012	(26,173)	\$797,490
Operating Income (loss)(6)...	\$ 58,908	\$ 7,788	\$(52,606)	\$(11,826)	\$ 2,264
Depreciation and amortization:					
Operating.....	\$ 13,097	\$ 10,670	\$ 17,928	\$ 139	\$ 41,834
Other.....	--	--	--	566	566
Total.....	\$ 13,097	\$ 10,670	\$ 17,928	\$ 705	\$ 42,400
Capital expenditures(5).....	\$ 31,116	\$ 13,109	\$ 16,442	\$ 269	\$ 60,936
Identifiable assets(6).....	\$219,727	\$198,596	\$220,161	\$ 35,804	\$674,288

## QUANEX CORPORATION

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

- (1) Identifiable assets include Nichols Aluminum Alabama, acquired on October 9, 1998.
- (2) Included in "Corporate and Other" are intersegment eliminations, and corporate expenses.
- (3) Intersegment sales are conducted on an arm's-length basis.
- (4) Operating income includes mostly non-cash non-recurring restructuring charge of \$58,500. See Note 4.
- (5) Includes capitalized interest.
- (6) As noted above, at the start of fiscal year 1999, Quanex changed its inventory valuation method for measuring segment results from LIFO to FIFO. This change has no impact on consolidated results, which remain LIFO based. Prior year's data have not been restated above, however, the following information is provided to allow comparability. The effect of switching to FIFO method of inventory valuation for segment reporting during 1998 would have been as follows:

	ENGINEERED STEEL BARS	ALUMINUM MILL SHEET PRODUCTS	ENGINEERED PRODUCTS	CORPORATE AND OTHER	CONSOLIDATED
Operating Income -- increase/(decrease).....	(1,100)	(5,011)	(165)	6,276	0
Identifiable Assets -- increase/(decrease).....	3,492	0	308	(3,800)	0

For the year ended October 31, 1997, 13% of the Company's consolidated net sales were made to one customer. These sales are included in the engineered products segment.

YEAR ENDED OCTOBER 31, 1997	ENGINEERED STEEL BARS	ALUMINUM MILL SHEET PRODUCTS	ENGINEERED PRODUCTS(1)	CORPORATE AND OTHER(2)	CONSOLIDATED
(IN THOUSANDS)					
Net Sales:					
To unaffiliated companies.....	\$301,436	\$237,836	\$206,821	--	\$746,093
Intersegment(3).....	18,032	23,205	10	\$(41,247)	--
Total.....	\$319,468	\$261,041	\$206,831	\$(41,247)	\$746,093
Operating Income (loss)(5).....	\$ 50,762	\$ 1,753	\$ 15,444	\$(12,951)	\$ 55,008
Depreciation and amortization:					
Operating.....	\$ 13,940	\$ 10,154	\$ 13,055	\$ 149	\$ 37,298
Other.....	--	--	--	567	567
Total.....	\$ 13,940	\$ 10,154	\$ 13,055	\$ 716	\$ 37,865
Capital expenditures(4).....	\$ 35,220	\$ 5,751	\$ 27,830	\$ 345	\$ 69,146
Identifiable assets(5).....	\$192,937	\$163,637	\$281,943	\$ 47,188	\$685,705

- (1) Identifiable assets include Advanced Metal Forming C.V., acquired on October 29, 1997.
- (2) Included in "Corporate and Other" are intersegment eliminations, corporate expenses and net assets of discontinued operations.
- (3) Intersegment sales are conducted on an arm's-length basis.
- (4) Includes capitalized interest.
- (5) As noted above, at the start of fiscal year 1999, Quanex changed its inventory valuation method for measuring segment results from LIFO to FIFO. This change has no impact on consolidated results, which remain LIFO based. Prior year's data have not been restated above, however, the following information is provided to allow comparability. The effect of switching to FIFO method of inventory valuation for segment reporting during 1997 would have been as follows:

	ENGINEERED STEEL BARS	ALUMINUM MILL SHEET PRODUCTS	ENGINEERED PRODUCTS	CORPORATE AND OTHER	CONSOLIDATED
Operating Income -- increase/(decrease).....	225	4,171	(71)	(4,325)	0
Identifiable Assets --					

increase/(decrease).....

4,592

5,011

473

(10,076)

0

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## GEOGRAPHIC INFORMATION

	YEAR ENDED OCTOBER 31,		
	1999	1998	1997
Net Sales(1)			
United States.....	\$745,265	\$741,067	713,596
Mexico.....	17,183	15,680	17,396
Canada.....	17,825	10,374	11,146
European countries.....	24,481	28,501	2,625
Other foreign countries.....	5,340	1,868	1,330
Total.....	\$810,094	\$797,490	\$746,093

(1) Net Sales are attributed to countries based on location of customer.

	YEAR ENDED OCTOBER 31,		
	1999	1998	1997
Net Sales(2)			
United States.....	\$777,441	\$763,775	\$746,093
The Netherlands.....	32,653	33,715	--
Total.....	\$810,094	\$797,490	\$746,093

(2) Net sales are attributed to countries based on location of operations.

	YEAR ENDED OCTOBER 31,		
	1999	1998	1997
Operating Income (Loss)(4)			
United States.....	\$71,774	\$ (144)(3)	\$55,008
The Netherlands.....	(17)	2,408	--
Total.....	\$71,757	\$2,264	\$55,008

(3) Including the restructuring charge of \$58.5 million. (See Note 4)

(4) Operating income (loss) is attributed to countries based on location of operations.

	YEAR ENDED OCTOBER 31,	
	1999	1998
Identifiable Assets(5)		
United States.....	\$648,145	\$627,969
The Netherlands.....	42,301	46,319
Total.....	\$690,446	\$674,288

(5) Identifiable assets are attributed to countries based on location of operations.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 14. PREFERRED STOCK PURCHASE RIGHTS

The Company declared a dividend in 1986 of one Preferred Stock Purchase Right (a "Right") on each outstanding share of its common stock. This action was intended to assure that all shareholders would receive fair treatment in the event of a proposed takeover of the Company. On April 26, 1989, the Company amended the Rights to provide for additional protection to shareholders and to provide the Board of Directors of the Company with needed flexibility in responding to abusive takeover tactics. On April 15, 1999, the Second Amended and Restated Rights Agreement went into effect. Each Right, when exercisable, entitles the holder to purchase 1/100th of a share of the Company's Series A Junior Participating Preferred Stock at an exercise price of \$90. Each 1/100th of a share of Series A Junior Participating Preferred Stock will be entitled to a dividend equal to the greater of \$.01 or the dividend declared on each share of common stock, and will be entitled to 1/100th of a vote, voting together with the shares of common stock. The Rights will be exercisable only if, without the Company's prior consent, a person or group of persons acquires or announces the intention to acquire 20% or more of the Company's common stock. If the Company is acquired through a merger or other business combination transaction, each Right will entitle the holder to purchase \$120 worth of the surviving company's common stock for \$90. Additionally, if someone acquires 20% or more of the Company's common stock, each Right not owned by the 20% or greater shareholder would permit the holder to purchase \$120 worth of the Company's common stock for \$90. The Rights are redeemable, at the option of the Company, at \$.02 per Right at any time until ten days after someone acquires 20% or more of the common stock. The Rights expire April 15, 2009.

As a result of the Rights distribution, 150,000 of the 1,000,000 shares of authorized Preferred Stock were reserved for issuance as Series A Junior Participating Preferred Stock.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 15. RESTRICTED STOCK AND STOCK OPTION PLANS

## Key Employee Plans:

The Company has restricted stock and stock option plans which provide for the granting of common shares or stock options to key employees. Under the Company's restricted stock plan, common stock may be awarded to key employees. The recipient is entitled to all of the rights of a shareholder, except that during the forfeiture period the shares are nontransferable. The award vests during the vesting period based on the price of the Company's stock. Upon issuance of stock under the plan, unearned compensation equal to the market value at the date of grant is charged to stockholders' equity and subsequently amortized to expense over the restricted period. There were 6,000 restricted shares granted in 1999. There were no restricted shares granted in 1998 or 1997. No compensation expense was charged in 1999 or 1998 related to the restricted stock. The amount charged to compensation expense in 1997 was \$185,000, relating to restricted stocks granted in 1994.

Under the Company's option plans, options are granted at prices determined by the Board of Directors which may not be less than the fair market value of the shares at the time the options are granted. Unless otherwise provided by the Board at the time of grant, options become exercisable in 33 1/3% increments maturing cumulatively on each of the first through third anniversaries of the date of grant and must be exercised no later than ten years from the date of grant. There were 276,776, 493,176, and 722,322 shares available for granting of options at October 31, 1999, 1998, and 1997, respectively. Stock option transactions for the three years ended October 31, 1999, were as follows:

	SHARES EXERCISABLE	SHARES UNDER OPTION	AVERAGE PRICE PER SHARE
	-----	-----	-----
Balance at October 31, 1996.....	726,609	1,257,646	\$22
	-----		
Granted.....		165,700	29
Exercised.....		(323,218)	18
Cancelled.....		(13,987)	25
		-----	
Balance at October 31, 1997.....	650,053	1,086,141	24
	-----		
Granted.....		264,550	21
Exercised.....		(95,416)	21
Cancelled.....		(35,404)	26
		-----	
Balance at October 31, 1998.....	770,075	1,219,871	23
	-----		
Granted.....		240,700	21
Exercised.....		(9,000)	15
Cancelled.....		(30,300)	24
		-----	
Balance at October 31, 1999.....	966,391	1,421,271	\$23
	=====	=====	

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

On October 1, 1992, Carl E. Pfeiffer retired as the Chief Executive Officer of the Company. In connection with such retirement, the Company replaced options to purchase 60,000 shares of Common Stock at a weighted average exercise price of \$15.85 held by Mr. Pfeiffer, under the Company's employee stock option plans with new options having the same exercise prices and expiration dates. Such options were substantially similar to the options previously held by him with the exception that vesting was not contingent upon his continued employment with the Company and the options expired on various dates between October 25, 1999 and October 13, 2001, instead of one year after retirement. During the year ended October 31, 1997, options for the entire 60,000 shares were exercised at an average price of \$15.85 per share.

## Non-Employee Director Plans:

The Company has various non-employee Director plans, which are described below:

## 1987 NON-EMPLOYEE DIRECTORS PLAN:

The Company's 1987 Non-employee Directors stock option plan provides for the granting of stock options to non-employee Directors to purchase up to an aggregate amount of 100,000 shares of common stock. The plan provides that each non-employee Director and each future non-employee Director, as of the first anniversary of the date of his/her election as a Director of the Company, will be granted an option to purchase 10,000 shares of common stock at a price per share of common stock equal to the fair market value of the common stock as of the date of the grant. During 1998, the Board of Directors passed a resolution, which reduced the number of options to be granted from 10,000 to 6,000.

Options become exercisable in 33 1/3% increments maturing cumulatively on each of the first through third anniversaries of the date of the grant and must be exercised no later than 10 years from the date of grant. No options may be granted under the plan after June 22, 1997. There were no shares available for granting of options at October 31, 1999, 1998 or 1997. Stock option transactions for the three years ended October 31, 1999, were as follows:

	SHARES EXERCISABLE	SHARES UNDER OPTION	AVERAGE PRICE PER SHARE
	-----	-----	-----
Balance at October 31, 1996.....	20,000	40,000	\$18
Granted.....	-----	--	--
Exercised.....		(15,000)	18
Cancelled.....		--	--
		-----	
Balance at October 31, 1997.....	11,666	25,000	18
Granted.....	-----	--	--
Exercised.....		(5,000)	14
Cancelled.....		--	--
		-----	
Balance at October 31, 1998.....	13,332	20,000	20
Granted.....	-----	--	--
Exercised.....		--	--
Cancelled.....		--	--
		-----	
Balance at October 31, 1999.....	20,000	20,000	\$20
	-----	-----	



## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 1989 NON-EMPLOYEE DIRECTORS PLAN:

The Company's 1989 Non-employee Directors stock option plan provides for the granting of stock options to non-employee Directors to purchase up to an aggregate of 210,000 shares of common stock. Each non-employee Director as of December 6, 1989 was granted an option to purchase 3,000 shares of common stock at a price per share of common stock equal to the fair market value of the common stock as of the date of grant. Also, each non-employee Director who is a director of the Company on any subsequent October 31, while the plan is in effect and shares are available for the granting of options hereunder, shall be granted on such October 31, an option to purchase 3,000 shares of common stock at a price equal to the fair market value of the common stock as of such October 31. During 1998, the Board of Directors passed a resolution, which decreased the number of options to be granted annually as prescribed above from 3,000 to 2,000. Options become exercisable at any time commencing six months after the grant and must be exercised no later than 10 years from the date of grant. No option may be granted under the plan after December 5, 1999. There were no shares available for granting of options at October 31, 1999 and 12,000, and 30,000 shares available for granting of options at October 31, 1998 and 1997, respectively. Stock option transactions for the three years ended October 31, 1999, were as follows:

	SHARES EXERCISABLE	SHARES UNDER OPTION	AVERAGE PRICE PER SHARE
	-----	-----	-----
Balance at October 31, 1996.....	102,000	123,000	\$22
Granted.....		21,000	28
Exercised.....		(30,000)	18
Cancelled.....		--	--
Balance at October 31, 1997.....	93,000	114,000	24
Granted.....		18,000	17
Exercised.....		(3,000)	19
Cancelled.....		--	--
Balance at October 31, 1998.....	111,000	129,000	23
Granted.....		12,000	22
Exercised.....		(5,000)	16
Cancelled.....		--	--
Balance at October 31, 1999.....	124,000	136,000	\$23
	=====	=====	

## 1997 NON-EMPLOYEE DIRECTORS PLAN:

The Company's 1997 Non-Employee Directors stock option plan provides for the granting of stock options to non-employee Directors to purchase up to an aggregate of 400,000 shares of common stock. There are two types of grants under this plan which are described below:

## AUTOMATIC ANNUAL GRANTS

While this plan is in effect and shares are available for the granting of options hereunder, each non-employee Director who is a director of the Company on October 31 and who has not received options under the 1989 Non-Employee Director plan shall be granted on such October 31, an option to purchase such number of shares of common stock as is determined by the Board of Directors at a price equal to the fair market value of the common stock as of such October 31. These options are exercisable in full immediately upon the date of grant.

## NEW DIRECTOR GRANTS

While this plan is in effect and shares are available for the granting of options hereunder, there shall be granted to each non-employee Director who was not granted an option under the 1987 Non-Employee Director Stock Option Plan as of the date upon which such director shall have continuously served as a director of the Company for a period of one year an option to purchase such number of Quanex Corporation shares of stock as is determined by the Board of Directors. These Plan options

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

become exercisable in 33 1/3% increments maturing cumulatively on each of the first through third anniversaries of the date of the grant and must be exercised no later than 10 years from the date of grant.

There were 382,000 shares available for granting of options at October 31, 1999. There were no transactions under this plan through October 31, 1998, however below is the activity through October 31, 1999:

	SHARES EXERCISABLE	SHARES UNDER OPTION	AVERAGE PRICE PER SHARE
	-----	-----	-----
Balance at October 31, 1998.....	--	--	--
Granted.....		18,000	\$21
Exercised.....		--	--
Cancelled.....		--	--
		-----	
Balance at October 31, 1999.....	2,000	18,000	\$21
	=====	=====	

## STOCK BASED COMPENSATION

In accordance with SFAS No. 123, "Accounting for Stock-Based Compensation", the Company continues to apply the rules for stock based compensation contained in Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and discloses the required pro forma effect on net income and earnings per share of the fair value based method of accounting for stock based compensation as required by SFAS No. 123.

The following pro forma summary of the Company's consolidated results of operations have been prepared as if the fair value based method of accounting for stock based compensation as required by SFAS No. 123 had been applied:

	YEARS ENDED OCTOBER 31,		
	1999	1998	1997
	-----	-----	-----
	(IN THOUSANDS)		
Net income attributable to common stockholders.....	\$39,716	\$ 9,169	\$69,184
SFAS No. 123 adjustment.....	(1,764)	(1,495)	(995)
	-----	-----	-----
Pro forma net attributable to common stockholders.....	\$37,952	\$ 7,674	\$68,189
	=====	=====	=====
Earnings per Common share:			
Basic as reported.....	\$ 2.79	\$ 0.65	\$ 5.01
Basic pro forma.....	\$ 2.67	\$ 0.54	\$ 4.94
Diluted as reported.....	\$ 2.59	\$ 0.65	\$ 4.38
Diluted pro forma.....	\$ 2.48	\$ 0.54	\$ 4.32

Fair value of the options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions.

	1999	1998	1997
	-----	-----	-----
Risk-free interest rate.....	5.93%	4.49%	5.39%
Dividend yield.....	2.80%	3.00%	2.23%
Volatility factor.....	40.21%	31.57%	29.83%
Weighted average expected life.....	5 years	5 years	5 years

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 16. FINANCIAL INSTRUMENTS

The Company uses futures contracts to hedge a portion of its exposure to price fluctuations of aluminum. The exposure is related to the Company's backlog of aluminum sales orders with committed prices as well as future aluminum sales for which a sales price increase would lag a raw material cost increase. Firm price commitments associated with these futures contracts do not extend beyond December 2000. Hedging gains and losses are included in "Cost of sales" in the income statement concurrently with the hedged sales. Unrealized gains and losses related to open contracts are not reflected in the consolidated statements of income. At October 31, 1999 and 1998, the Company had open futures contracts at fair values of \$5.3 and \$3.3 million, respectively, and an unrealized gain of \$117 thousand and an unrealized loss of \$369 thousand, respectively, on such contracts. At October 31, 1999 and 1998, these contracts covered a notional volume of 7,716,170 and 5,511,557 pounds of aluminum.

In the fourth quarter of fiscal 1996, the Company entered into interest rate swap agreements, which effectively converted \$100 million of its variable rate debt under the Bank Agreement, to fixed rate. Under these agreements, payments are made based on a fixed rate (\$50 million at 7.025%, and \$50 million at 6.755%) and received on a LIBOR based variable rate (6.21% at October 31, 1999). Differentials to be paid or received under the agreements are recognized as interest expense. The agreements mature in 2003. The unrealized losses related to the interest rate swaps are \$2.0 million on October 31, 1999 and \$8.5 million on October 31, 1998 on the total notional amount of \$100 million for fiscal 1999 and fiscal 1998.

The Company utilizes foreign currency forward contracts to hedge identifiable foreign currency commitments associated with transactions in the regular course of the Company's foreign operations. These forward contracts establish the exchange rates at which the Company will purchase a contracted amount of foreign currency for a specified amount of US dollars. At October 31, 1999, there were no open contracts. At October 31, 1998, the Company had 11 separate contracts maturing in monthly increments to purchase an aggregate notional amount of \$4.675 million in foreign currency. Unrealized pretax gains on these forward contracts totaled approximately \$137 thousand at October 31, 1998.

In December 1997, the Company entered into a zero-cost range forward (foreign currency swap) agreement on a notional value of 30 million Guilders with a major financial institution to hedge its initial equity investment in its Netherlands subsidiary, Piper Impact Europe. This agreement limits the Company's exposure to large fluctuations in the US Dollar/Dutch Guilder exchange rate. Under the terms of the agreement, Quanex has the option to let the agreement expire at no cost if the exchange rate remains within an established range on the expiration date of October 25, 2000. At October 31, 1998, there was no effect on the financial statements from this agreement as the exchange rate remained within this range. At October 31, 1999, the Company booked a \$378 thousand gain to stockholders' equity's cumulative foreign currency translation adjustment.

The fair values of the Company's financial assets approximate the carrying values reported on the consolidated balance sheet. The fair value of long-term debt was \$186.0 million and \$190.6 million, as of October 31, 1999 and 1998, respectively, as compared to carrying values at October 31, 1999 and 1998 of \$189.7 million and \$200.6 million, respectively.

The fair value of long-term debt was based on the quoted market price, recent transactions, or based on rates available to the Company for instruments with similar terms and maturities. The fair value of interest rate swaps was estimated by discounting expected cash flows using quoted market interest rates. The fair value of the aluminum and foreign currency instruments was determined by obtaining the LME price per pound and the foreign currency translation rates as of October 31, 1999 and valuing the outstanding notional volumes under the agreements.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS -- (CONTINUED)

## 17. CONTINGENCIES

Quanex is subject to loss contingencies arising from federal, state, and local environmental laws. Environmental expenditures are expensed or capitalized depending on their future economic benefit. The Company accrues its best estimates of its remediation obligations and adjusts such accruals as further information and circumstances develop. Those estimates may change substantially depending on information about the nature and extent of contamination, appropriate remediation technologies, and regulatory approvals. Costs of future expenditures for environmental remediation are not discounted to their present value. When environmental laws might be deemed to impose joint and several liability for the costs of responding to contamination, the Company accrues its allocable share of liability taking into account the number of companies participating, their ability to pay their shares, the volumes and nature of the wastes involved, the nature of anticipated response actions, and the nature of the Company's alleged connections. It is management's opinion that the Company has established appropriate reserves for environmental remediation obligations at various of its plant sites and disposal facilities. Those amounts are not expected to have a material adverse effect on the Company's financial condition. Total remediation reserves, at October 31, 1999, were approximately \$20 million. These reserves include, without limitation, the Company's best estimate of liabilities related to costs for further investigations, environmental remediation, and corrective actions related to the acquisition of Piper Impact, the acquisition of Nichols Aluminum Alabama and a facility previously part of the former Tubing Operations. Actual cleanup costs at the Company's current plant sites, former plants, and disposal facilities could be more or less than the amounts accrued for remediation obligations. It is not possible at this point to reasonably estimate the amount of any obligation for remediation in excess of current accruals that would be material to Quanex's financial statements because of uncertainties as to the extent of environmental impact and concurrence of governmental authorities.

## 18. SUBSEQUENT EVENTS

On December 9, 1999, the Company announced that its Board of Directors approved a program to repurchase shares of the Company's common stock. Under terms of the program, the Company may periodically purchase up to a total of 2 million shares of its common stock in the open market or in privately negotiated transactions. The repurchase plan does not have a time limit, and funds for the program will be provided from the Company's available working capital and bank credit line.

On December 15, 1999, the Company announced that it had signed a contract to acquire the assets of Alcoa's Fort Lupton, Colorado-based aluminum sheet production facility for \$8 million plus working capital value which is estimated at \$17 million. Consummation of the sale is subject to government approval.

The acquisition of the Fort Lupton mill will increase the casting, cold-finishing and value-added painting capacities of Nichols Aluminum, Quanex's aluminum sheet business. The Fort Lupton mill can produce more than 40-million pounds annually of high-grade aluminum sheet for a variety of applications, including beverage cans and other food packaging, home furnishing, and other consumer durable products.

QUANEX CORPORATION  
SUPPLEMENTARY FINANCIAL DATA

QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

The following sets forth the selected quarterly information for the years ended October 31, 1999 and 1998.

	FIRST QUARTER	SECOND QUARTER	THIRD QUARTER	FOURTH QUARTER
	(IN THOUSANDS EXCEPT PER SHARE AMOUNTS)			
1999:				
Net sales.....	\$183,103	\$202,879	\$206,619	\$217,493
Gross profit.....	23,536	32,046	35,048	37,665
Income from continuing operations.....	3,869	9,777	12,331	13,324
Extraordinary gain.....	--	415	--	--
Net income.....	3,869	10,192	12,331	13,324
Earnings per share:				
Basic:				
Income from continuing operations.....	0.27	0.69	0.86	0.94
Extraordinary gain.....	--	0.03	--	--
Net earnings (loss).....	0.27	0.72	0.86	0.94
Diluted.....	\$ 0.27	\$ 0.66	\$ 0.79	\$ 0.85
1998:				
Net sales.....	\$180,982	\$203,428	\$204,854	\$208,226
Gross profit.....	17,219	27,395	30,876	38,046
Income from continuing operations(1).....	2,293	7,756	10,285	(24,211)
Gain on sale of discontinued operations.....	13,606	--	--	(560)
Net income(1).....	15,899	7,756	10,285	(24,771)
Earnings per share:				
Basic:				
Income from continuing operations(1).....	0.16	0.55	0.73	(1.71)
Gain on sale of discontinued operations.....	0.97	--	--	(0.04)
Net earnings (loss)(1).....	1.13	0.55	0.73	(1.75)
Diluted.....	\$ 1.11	\$ 0.51	\$ 0.66	\$ (1.75)

(1) Includes an after-tax non-recurring restructuring charge of \$38,025 or \$2.68 per share.

SCHEDULE II -- VALUATION AND QUALIFYING ACCOUNTS

DESCRIPTION	BALANCE AT BEGINNING OF YEAR	CHARGED TO COSTS & EXPENSES	WRITE-OFFS	OTHER	BALANCE AT END OF YEAR
	(IN THOUSANDS)				
ALLOWANCE FOR DOUBTFUL ACCOUNTS:					
Year ended October 31, 1999.....	\$11,752	\$ 921	\$(188)	\$(331)	\$12,154
Year ended October 31, 1998.....	\$10,338	\$1,088	\$(202)	\$ 528	\$11,752
Year ended October 31, 1997.....	\$ 7,703	\$2,674	\$( 39)	\$ --	\$10,338

## QUANEX CORPORATION

QUARTERLY FINANCIAL RESULTS  
(FROM CONTINUING OPERATIONS)

	1999	1998	1997
	-----	-----	-----
NET SALES (millions)			
January.....	183.10	180.98	167.96
April.....	202.87	203.43	186.00
July.....	206.62	204.85	196.58
October.....	217.50	208.23	195.55
Total.....	810.09	797.49	746.09
GROSS PROFIT (millions)			
January.....	23.54	17.22	20.61
April.....	32.05	27.39	26.14
July.....	35.05	30.88	28.68
October.....	37.66	38.05	26.62
Total.....	128.30	113.54	102.05
INCOME (LOSS) FROM CONTINUING OPERATIONS (millions)			
January.....	3.87	2.29	3.37
April.....	9.78	7.76	7.34
July.....	12.33	10.28	8.61
October(1).....	13.32	(24.21)	8.40
Total.....	39.30	(3.88)	27.72
INCOME (LOSS) FROM CONTINUING OPERATIONS PER BASIC COMMON SHARE			
January.....	.27	.16	.25
April.....	.69	.55	.53
July.....	.86	.73	.62
October(1).....	.94	(1.71)	.60
Year.....	2.76	(.27)	2.01
QUARTERLY COMMON STOCK DIVIDENDS			
January.....	.16	.16	.15
April.....	.16	.16	.15
July.....	.16	.16	.15
October.....	.16	.16	.16
Total.....	.64	.64	.61
COMMON STOCK SALES PRICE (High & Low)			
January.....	23 7/8	30 7/1	29 1/8
April.....	16 13/16	27 1/1	24 1/4
July.....	26 1/4	33 3/1	27 7/8
October.....	15 3/8	28 1/2	23 3/8
Year.....	29	32 3/1	34 1/8
October.....	25 1/8	27 1/4	25 1/8
Year.....	27 3/8	27 7/8	36 1/2
October.....	20 1/8	15 5/8	26 1/4

(1) Fiscal 1998 fourth quarter income (loss) from continuing operations includes an after-tax non-recurring restructuring charge of \$38 million or \$2.68 per share.

## ITEM 9. DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

## PART III

## ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Pursuant to General Instruction G(3) to Form 10-K, information on directors and executive officers of the Registrant is incorporated herein by reference from the Registrant's Definitive Proxy Statement to be filed pursuant to Regulation 14A within 120 days after the close of the fiscal year ended October 31, 1999.

## ITEM 11. EXECUTIVE COMPENSATION

Pursuant to General Instruction G(3) to Form 10-K, information on executive compensation is incorporated herein by reference from the Registrant's Definitive Proxy Statement to be filed pursuant to Regulation 14A within 120 days after the close of the fiscal year ended October 31, 1999.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Pursuant to General Instruction G(3) to Form 10-K, information on security ownership of certain beneficial owners and management is incorporated herein by reference from the Registrant's Definitive Proxy Statement to be filed pursuant to Regulation 14A within 120 days after the close of the fiscal year ended October 31, 1999.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Pursuant to General Instruction G(3) to Form 10-K, information on certain relationships and related transactions is incorporated herein by reference from the Registrant's Definitive Proxy Statement to be filed pursuant to Regulation 14A within 120 days after the close of the fiscal year ended October 31, 1999.

## PART IV

## ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

## (a) 1. Financial Statements

	PAGE
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Independent Auditors' Report.....	24
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2. Financial Statement Schedule	
Schedule II -- Valuation and qualifying accounts.....	56
Schedules not listed or discussed above have been omitted as they are either inapplicable or the required information has been given in the consolidated financial statements or the notes thereto.	
3. Exhibits.....	60



EXHIBIT  
NUMBER

## DESCRIPTION OF EXHIBITS

- 
- 3.1 -- Restated Certificate of Incorporation of the Registrant dated as of November 10, 1995 filed as Exhibit 3.1 of the Registrant's Annual Report on Form 10-K for the fiscal year ended October 31, 1995 and incorporated herein by reference.
  - \*3.2 -- Certificate of Amendment to Restated Certificate of Incorporation of the Registrant dated as of February 27, 1997.
  - \*3.3 -- Amendment to Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Stock of the Registrant dated as of April 15, 1999.
  - \*3.4 -- Certificate of Correction of Amendment to Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Stock dated as of April 16, 1999.
  - 3.5 -- Amended and Restated Bylaws of the Registrant, as amended through August 26, 1999 filed as Exhibit 3 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended July 31, 1999, and incorporated herein by reference.
  - 4.1 -- Form of Registrant's Common Stock certificate, filed as Exhibit 4.1 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended April 30, 1987, and incorporated herein by reference.
  - 4.2 -- Second Amended and Restated Rights agreement dated as of April 15, 1999, between The Registrant and American Stock Transfer & Trust Co. as Rights Agent, filed as Exhibit 4.1 to the Registrant's Form 8-K dated April 15, 1999, and incorporated herein by reference.
  - 4.3 -- Amended and Restated Certificate of Designation, Preferences and Rights of the Registrant's Series A Junior Participating Preferred Stock, filed as Exhibit 1 to Amendment No. 1 to the Registrant's Form 8-A dated April 28, 1989, and incorporated herein by reference.
  - 4.4 -- Form of Indenture relating to the Registrant's 6.88% Convertible Subordinated Exhibit Debentures due 2007 between the Registrant and Chemical Bank, as Trustee, filed as 19.2 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended April 30, 1992, and incorporated herein by reference.
  - 4.5 -- \$250,000,000 Revolving Credit and Term Loan Agreement dated as of July 23, 1996, among the Company, Comerica Bank, as Agent, and Harris Trust and Savings Bank and Wells Fargo Bank (Texas), NA as Co-Agents, filed as Exhibit 4.1 of the Company's Report on Form 8-K, dated August 9, 1996, and incorporated herein by reference.
  - +10.1 -- Quanex Corporation 1988 Stock Option Plan, as amended, and form of Stock Option year Agreement filed as Exhibit 10.4 to the Registrant's Annual Report on Form 10-K for the ended October 31, 1988, together with the amendment filed as Exhibit 10.17 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended January 31, 1995, and incorporated herein by reference.
  - \*+10.2 -- Amendment to the Quanex Corporation 1988 Stock Option Plan, dated of December 1997.
  - \*+10.3 -- Amendment to the Quanex Corporation 1988 Stock Option Plan, dated of December 9, 1999.
  - \*+10.4 -- Quanex Corporation Deferred Compensation Plan, as amended and restated, dated September 29, 1999.
  - \*+10.5 -- First Amendment to Quanex Corporation Deferred Compensation Plan, dated December 7, 1999.

EXHIBIT  
NUMBER

## DESCRIPTION OF EXHIBITS

- 
- 
- +10.6 -- Quanex Corporation 1978 Stock Option Plan, as amended, filed as Exhibit 10.6 to the Annual Report on Form 10-K for the year ended October 31, 1988, together with the amendment filed as Exhibit 10.16 of the Registrant's Quarterly Report Form 10-Q for the quarter ended January 31, 1995, and incorporated herein by reference.
  - \*+10.7 -- Amendment to Quanex Corporation 1978 Stock Option Plan, dated December 1997.
  - \*+10.8 -- Quanex Corporation Executive Incentive Compensation Plan, as amended and restated, dated October 12, 1995.
  - \*+10.9 -- Quanex Corporation Supplemental Benefit Plan, as amended and restated effective June 1, 1999.
  - \*+10.10 -- Form of Change in Control Agreement, between the Registrant and each executive officer of the Registrant.
  - +10.11 -- Quanex Corporation Stock Option Loan Plan for Key Officers, filed as Exhibit 10.13 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1988, and incorporated herein by reference.
  - +10.12 -- Quanex Corporation 1987 Non-Employee Director Stock Option Plan, as amended, and the related form of Stock Option Agreement, filed as Exhibit 10.14 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1988, together with the amendment filed as Exhibit 10.14 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended January 31, 1995, and incorporated herein by reference.
  - \*+10.13 -- Amendment to the Quanex Corporation 1987 Non-Employee Director Stock Option Plan, dated December 1997.
  - \*+10.14 -- Amendment to the Quanex Corporation 1987 Non-Employee Director Stock Option Plan, dated December 9, 1999.
  - +10.15 -- Quanex Corporation 1989 Non-Employee Director Stock Option Plan, as amended, filed as Exhibit 4.4 of the Registrant's Form S-8, Registration No. 33-35128, together with the amendment filed as Exhibit 10.15 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended January 31, 1995, and incorporated herein by reference.
  - \*+10.16 -- Amendment to the Quanex Corporation 1989 Non-Employee Director Stock Option Plan, dated December 1997.
  - \*+10.17 -- Amendment to the Quanex Corporation 1989 Non-Employee Director Stock Option Plan, dated December 9, 1999.
  - +10.18 -- Quanex Corporation Employee Stock Option and Restricted Stock Plan, as amended, filed as Exhibit 10.14 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1994, and incorporated herein by reference.
  - \*+10.19 -- Amendment to the Quanex Corporation Employee Stock Option and Restricted Stock Plan, dated December 1997.
  - \*+10.20 -- Amendment to the Quanex Corporation Employee Stock Option and Restricted Stock Plan, dated December 9, 1999.
  - +10.21 -- Retirement Agreement dated as of September 1, 1992, between the Registrant and Carl E. Pfeiffer, filed as Exhibit 10.20 to the Registrant's Annual Report on Form 10-K for the year ended October 31, 1992, and incorporated herein by reference.
  - +10.22 -- Stock Option Agreement dated as of October 1, 1992, between the Registrant and Carl E. Pfeiffer, filed as Exhibit 10.21 to the Registrant's Annual Report on Form 10-K for the year ended October 31, 1992, and incorporated herein by reference.

EXHIBIT NUMBER -----	DESCRIPTION OF EXHIBITS -----
+10.23	-- Deferred Compensation Agreement dated as of July 31, 1992, between the Registrant and Carl E. Pfeiffer, filed as Exhibit 10.22 to the Registrant's Annual Report on Form 10-K for the year ended October 31, 1992, and incorporated herein by reference.
+10.24	-- Quanex Corporation Non-Employee Director Retirement Plan, filed as Exhibit 10.18 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1994, and incorporated herein by reference.
+10.25	-- Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan, filed as Exhibit 10.19 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1996, and incorporated herein by reference.
*+10.26	-- Amendment to Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan, dated December 1997.
*+10.27	-- Amendment to Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan, dated December 9, 1999.
+10.28	-- Quanex Corporation Deferred Compensation Trust filed as Exhibit 4.8 of the Registrant's Registration Statement on Form S-3, Registration No. 333-36635, and incorporated herein by reference.
*+10.29	-- Amendment to Quanex Corporation Deferred Compensation Trust, dated December 9, 1999.
10.30	-- Quanex Corporation 1997 Non-Employee Director Stock Option Plan filed as Exhibit 10.21 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1997 and incorporated herein by reference.
*+10.31	-- Amendment to Quanex Corporation 1997 Non-Employee Director Stock Option Plan, dated December 9, 1999.
10.32	-- Asset Purchase Agreement dated July 31, 1996, among the Company, Piper Impact, Inc., a Delaware corporation, Piper Impact, Inc., a Tennessee corporation, B. F. Sammons And M. W. Robbins, filed as Exhibit 2.1 of the Company's Report on Form 8-K, dated August 9, 1996, and incorporated herein by reference.
10.33	-- Stock Purchase Agreement dated April 18, 1997, by and among Niagara Corporation, Niagara Cold Drawn Corp., and Quanex Corporation filed as Exhibit 2.1 to the Company's Current Report on Form 8-K, dated May 5, 1997, and incorporated herein by reference.
10.34	-- Purchase Agreement dated December 3, 1997, among Quanex Corporation, Vision Metals Holdings, Inc., and Vision Metals, Inc., filed as Exhibit 2.1 to the Company's Current Report on Form 8-K, dated December 3, 1997, and incorporated herein by reference.
10.35	-- Lease Agreement between The Industrial Development Board of the City of Decatur and Fruehauf Trailer Company dated May 1, 1963, filed as Exhibit 10.22 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.36	-- Lease Agreement between The Industrial Development Board of the City of Decatur and Fruehauf Corporation dated May 1, 1964, filed as Exhibit 10.23 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.37	-- Lease Agreement between The Industrial Development Board of the City of Decatur and Fruehauf Corporation dated October 1, 1965, filed as Exhibit 10.24 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.

EXHIBIT NUMBER -----	DESCRIPTION OF EXHIBITS -----
10.38	-- Lease Agreement between The Industrial Development Board of the City of Decatur (Alabama) and Fruehauf Corporation dated December 1, 1978, filed as Exhibit 10.25 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.39	-- Assignment and Assumption Agreement between Fruehauf Trailer Corporation and Decatur Aluminum Corp. (subsequently renamed Nichols Aluminum-Alabama, Inc.) dated October 9, 1998, filed as Exhibit 10.26 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.40	-- Agreement between The Industrial Development Board of the City of Decatur and Decatur Aluminum Corp. (subsequently renamed Nichols Aluminum-Alabama, Inc.) dated September 23, 1998, filed as Exhibit 10.27 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
*21	-- Subsidiaries of the Registrant.
*23	-- Consent of Deloitte & Touche LLP.
*27	-- Financial Data Schedule

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+ Management Compensation or Incentive Plan

\* Filed herewith

As permitted by Item 601(b)(4)(iii)(A) of Regulation S-K, the Registrant has not filed with this Annual Report on Form 10-K certain instruments defining the rights of holders of long-term debt of the Registrant and its subsidiaries because the total amount of securities authorized under any of such instruments does not exceed 10% of the total assets of the Registrant and its subsidiaries on a consolidated basis. The Registrant agrees to furnish a copy of any such agreements to the Securities and Exchange Commission upon request.

(b) Reports on Form 8-K

No Reports on Form 8-K were filed by the Company during the quarter ended October 31, 1999.

## SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

QUANEX CORPORATION

By: /s/ VERNON E. OECHSLE

January 7, 2000

-----  
 Vernon E. Oechsle  
 Chairman of the Board and  
 Chief Executive Officer  
 (Principal Executive Officer)

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

By: /s/ VERNON E. OECHSLE

January 7, 2000

-----  
 Vernon E. Oechsle  
 Chairman of the Board and  
 Chief Executive Officer

By: /s/ JAMES H. DAVIS

January 7, 2000

-----  
 James H. Davis  
 President and  
 Chief Operating Officer  
 (Principal Operating Officer)

By: /s/ CARL E. PFEIFFER

January 7, 2000

-----  
 Carl E. Pfeiffer  
 Director

By: /s/ JOHN D. O'CONNELL

January 7, 2000

-----  
 John D. O'Connell  
 Director

By: /s/ DONALD G. BARGER, JR.

January 7, 2000

-----  
 Donald G. Barger, Jr.  
 Director

By: /s/ VINCENT R. SCORSONE

January 7, 2000

-----  
Vincent R. Scorsone  
Director

By: /s/ MICHAEL J. SEBASTIAN

January 7, 2000

-----  
Michael J. Sebastian  
Director

By: /s/ RUSSELL M. FLAUM

January 7, 2000

-----  
Russell M. Flaum  
Director

By: /s/ SUSAN F. DAVIS

January 7, 2000

-----  
Susan F. Davis  
Director

By: /s/ TERRY M. MURPHY

January 7, 2000

-----  
Terry M. Murphy  
Vice President -- Finance and  
Chief Financial Officer  
(Principal Financial Officer)

By: /s/ VIREN M. PARIKH

January 7, 2000

-----  
Viren M. Parikh  
Controller  
(Principal Accounting Officer)

## INDEX TO EXHIBITS

EXHIBIT NUMBER -----	DESCRIPTION OF EXHIBITS -----
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*3.2	-- Certificate of Amendment to Restated Certificate of Incorporation of the Registrant dated as of February 27, 1997.
*3.3	-- Amendment to Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Stock of the Registrant dated as of April 15, 1999.
*3.4	-- Certificate of Correction of Amendment to Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Stock dated as of April 16, 1999.
3.5	-- Amended and Restated Bylaws of the Registrant, as amended through August 26, 1999 filed as Exhibit 3 to the Registrant's Quarterly Report on Form 10-Q for the fiscal quarter ended July 31, 1999, and incorporated herein by reference.
4.1	-- Form of Registrant's Common Stock certificate, filed as Exhibit 4.1 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended April 30, 1987, and incorporated herein by reference.
4.2	-- Second Amended and Restated Rights agreement dated as of April 15, 1999, between The Registrant and American Stock Transfer & Trust Co. as Rights Agent, filed as Exhibit 4.1 to the Registrant's Form 8-K dated April 15, 1999, and incorporated herein by reference.
4.3	-- Amended and Restated Certificate of Designation, Preferences and Rights of the Registrant's Series A Junior Participating Preferred Stock, filed as Exhibit 1 to Amendment No. 1 to the Registrant's Form 8-A dated April 28, 1989, and incorporated herein by reference.
4.4	-- Form of Indenture relating to the Registrant's 6.88% Convertible Subordinated Exhibit Debentures due 2007 between the Registrant and Chemical Bank, as Trustee, filed as 19.2 to the Registrant's Quarterly Report on Form 10-Q for the quarter ended April 30, 1992, and incorporated herein by reference.
4.5	-- \$250,000,000 Revolving Credit and Term Loan Agreement dated as of July 23, 1996, among the Company, Comerica Bank, as Agent, and Harris Trust and Savings Bank and Wells Fargo Bank (Texas), NA as Co-Agents, filed as Exhibit 4.1 of the Company's Report on Form 8-K, dated August 9, 1996, and incorporated herein by reference.
+10.1	-- Quanex Corporation 1988 Stock Option Plan, as amended, and form of Stock Option year Agreement filed as Exhibit 10.4 to the Registrant's Annual Report on Form 10-K for the ended October 31, 1988, together with the amendment filed as Exhibit 10.17 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended January 31, 1995, and incorporated herein by reference.
*+10.2	-- Amendment to the Quanex Corporation 1988 Stock Option Plan, dated of December 1997.
*+10.3	-- Amendment to the Quanex Corporation 1988 Stock Option Plan, dated of December 9, 1999.
*+10.4	-- Quanex Corporation Deferred Compensation Plan, as amended and restated, dated September 29, 1999.
*+10.5	-- First Amendment to Quanex Corporation Deferred Compensation Plan, dated December 7, 1999.

EXHIBIT  
NUMBER

## DESCRIPTION OF EXHIBITS

- 
- +10.6 -- Quanex Corporation 1978 Stock Option Plan, as amended, filed as Exhibit 10.6 to the Annual Report on Form 10-K for the year ended October 31, 1988, together with the amendment filed as Exhibit 10.16 of the Registrant's Quarterly Report Form 10-Q for the quarter ended January 31, 1995, and incorporated herein by reference.
  - \*+10.7 -- Amendment to Quanex Corporation 1978 Stock Option Plan, dated December 1997.
  - \*+10.8 -- Quanex Corporation Executive Incentive Compensation Plan, as amended and restated, dated October 12, 1995.
  - \*+10.9 -- Quanex Corporation Supplemental Benefit Plan, as amended and restated effective June 1, 1999.
  - \*+10.10 -- Form of Change in Control Agreement, between the Registrant and each executive officer of the Registrant.
  - +10.11 -- Quanex Corporation Stock Option Loan Plan for Key Officers, filed as Exhibit 10.13 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1988, and incorporated herein by reference.
  - +10.12 -- Quanex Corporation 1987 Non-Employee Director Stock Option Plan, as amended, and the related form of Stock Option Agreement, filed as Exhibit 10.14 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1988, together with the amendment filed as Exhibit 10.14 of the Registrant's Quarterly Report on Form 10-Q For the quarter ended January 31, 1995, and incorporated herein by reference.
  - \*+10.13 -- Amendment to the Quanex Corporation 1987 Non-Employee Director Stock Option Plan, dated December 1997.
  - \*+10.14 -- Amendment to the Quanex Corporation 1987 Non-Employee Director Stock Option Plan, dated December 9, 1999.
  - +10.15 -- Quanex Corporation 1989 Non-Employee Director Stock Option Plan, as amended, filed as Exhibit 4.4 of the Registrant's Form S-8, Registration No. 33-35128, together with the amendment filed as Exhibit 10.15 of the Registrant's Quarterly Report on Form 10-Q for the quarter ended January 31, 1995, and incorporated herein by reference.
  - \*+10.16 -- Amendment to the Quanex Corporation 1989 Non-Employee Director Stock Option Plan, dated December 1997.
  - \*+10.17 -- Amendment to the Quanex Corporation 1989 Non-Employee Director Stock Option Plan, dated December 9, 1999.
  - +10.18 -- Quanex Corporation Employee Stock Option and Restricted Stock Plan, as amended, filed as Exhibit 10.14 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1994, and incorporated herein by reference.
  - \*+10.19 -- Amendment to the Quanex Corporation Employee Stock Option and Restricted Stock Plan, dated December 1997.
  - \*+10.20 -- Amendment to the Quanex Corporation Employee Stock Option and Restricted Stock Plan, dated December 9, 1999.
  - +10.21 -- Retirement Agreement dated as of September 1, 1992, between the Registrant and Carl E. Pfeiffer, filed as Exhibit 10.20 to the Registrant's Annual Report on Form 10-K for the year ended October 31, 1992, and incorporated herein by reference.
  - +10.22 -- Stock Option Agreement dated as of October 1, 1992, between the Registrant and Carl E. Pfeiffer, filed as Exhibit 10.21 to the Registrant's Annual Report on Form 10-K for the year ended October 31, 1992, and incorporated herein by reference.



EXHIBIT NUMBER -----	DESCRIPTION OF EXHIBITS -----
+10.23	-- Deferred Compensation Agreement dated as of July 31, 1992, between the Registrant and Carl E. Pfeiffer, filed as Exhibit 10.22 to the Registrant's Annual Report on Form 10-K for the year ended October 31, 1992, and incorporated herein by reference.
+10.24	-- Quanex Corporation Non-Employee Director Retirement Plan, filed as Exhibit 10.18 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1994, and incorporated herein by reference.
+10.25	-- Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan, filed as Exhibit 10.19 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1996, and incorporated herein by reference.
*+10.26	-- Amendment to Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan, dated December 1997.
*+10.27	-- Amendment to Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan, dated December 9, 1999.
+10.28	-- Quanex Corporation Deferred Compensation Trust filed as Exhibit 4.8 of the Registrant's Registration Statement on Form S-3, Registration No. 333-36635, and incorporated herein by reference.
*+10.29	-- Amendment to Quanex Corporation Deferred Compensation Trust, dated December 9, 1999.
10.30	-- Quanex Corporation 1997 Non-Employee Director Stock Option Plan filed as Exhibit 10.21 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1997 and incorporated herein by reference.
*+10.31	-- Amendment to Quanex Corporation 1997 Non-Employee Director Stock Option Plan, dated December 9, 1999.
10.32	-- Asset Purchase Agreement dated July 31, 1996, among the Company, Piper Impact, Inc., a Delaware corporation, Piper Impact, Inc., a Tennessee corporation, B. F. Sammons And M. W. Robbins, filed as Exhibit 2.1 of the Company's Report on Form 8-K, dated August 9, 1996, and incorporated herein by reference.
10.33	-- Stock Purchase Agreement dated April 18, 1997, by and among Niagara Corporation, Niagara Cold Drawn Corp., and Quanex Corporation filed as Exhibit 2.1 to the Company's Current Report on Form 8-K, dated May 5, 1997, and incorporated herein by reference.
10.34	-- Purchase Agreement dated December 3, 1997, among Quanex Corporation, Vision Metals Holdings, Inc., and Vision Metals, Inc., filed as Exhibit 2.1 to the Company's Current Report on Form 8-K, dated December 3, 1997, and incorporated herein by reference.
10.35	-- Lease Agreement between The Industrial Development Board of the City of Decatur and Fruehauf Trailer Company dated May 1, 1963, filed as Exhibit 10.22 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.36	-- Lease Agreement between The Industrial Development Board of the City of Decatur and Fruehauf Corporation dated May 1, 1964, filed as Exhibit 10.23 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.37	-- Lease Agreement between The Industrial Development Board of the City of Decatur and Fruehauf Corporation dated October 1, 1965, filed as Exhibit 10.24 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.

EXHIBIT  
NUMBER

## DESCRIPTION OF EXHIBITS

EXHIBIT NUMBER	DESCRIPTION OF EXHIBITS
10.38	-- Lease Agreement between The Industrial Development Board of the City of Decatur (Alabama) and Fruehauf Corporation dated December 1, 1978, filed as Exhibit 10.25 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.39	-- Assignment and Assumption Agreement between Fruehauf Trailer Corporation and Decatur Aluminum Corp. (subsequently renamed Nichols Aluminum-Alabama, Inc.) dated October 9, 1998, filed as Exhibit 10.26 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
10.40	-- Agreement between The Industrial Development Board of the City of Decatur and Decatur Aluminum Corp. (subsequently renamed Nichols Aluminum-Alabama, Inc.) dated September 23, 1998, filed as Exhibit 10.27 of the Registrant's Annual Report on Form 10-K for the year ended October 31, 1998 and incorporated herein by reference.
*21	-- Subsidiaries of the Registrant.
*23	-- Consent of Deloitte & Touche LLP.
*27	-- Financial Data Schedule

- - - - -  
+ Management Compensation or Incentive Plan

\* Filed herewith

QUANEX CORPORATION  
CERTIFICATE OF AMENDMENT  
TO  
RESTATED CERTIFICATE OF INCORPORATION

Quanex Corporation, a corporation organized and existing under and by virtue of the General Corporation Law of the State of Delaware (the "Company"), does hereby certify:

FIRST: That the Board of Directors of the Company, at a meeting duly called and held on December 12, 1996, adopted resolutions proposing and declaring advisable the following amendment to the Restated Certificate of Incorporation of the Company and directed that such amendment be considered at the next annual meeting of stockholders of the Company:

To amend the first paragraph of Article Fourth of the Restated Certificate of Incorporation in its entirety to read as follows:

"FOURTH: The total number of shares of all classes of stock which the Corporation shall have authority to issue is Fifty-One Million (51,000,000), of which Fifty Million (50,000,000) shall be shares of Common Stock, par value Fifty Cents (\$.50) per share, and of which One Million (1,000,000) shares shall be Preferred Stock, no par value."

SECOND: That at the annual meeting of stockholders of the Company duly called and held on February 27, 1997, in accordance with Section 222 of the General Corporation Law of the State of Delaware, the holders of a majority of the shares of Common Stock of the Company entitled to vote on such amendment voted in favor of such amendment.

THIRD: That the aforesaid amendment was duly adopted in accordance with the applicable provisions of Section 242 of the General Corporation Law of the State of Delaware.

IN WITNESS WHEREOF, the Company has caused this Certificate of Amendment to be signed by Wayne M. Rose, its Vice President-Finance and Chief Financial Officer, this 27th day of February, 1997.

QUANEX CORPORATION

By: /s/ WAYNE M. ROSE

-----  
Wayne M. Rose  
Vice President-Finance and  
Chief Financial Officer

AMENDMENT TO CERTIFICATE OF DESIGNATION,  
PREFERENCES AND RIGHTS OF SERIES A  
JUNIOR PARTICIPATING PREFERRED STOCK OF  
QUANEX CORPORATION

Pursuant to Section 151 of the General Corporation Law of the State of Delaware, Quanex Corporation, a corporation organized and existing under the General Corporation Law of the State of Delaware, in accordance with the provisions of Section 103 thereof, HEREBY CERTIFIES THAT:

1. By the Certificate of Designation of Series A Participating Preferred Stock filed as an exhibit to the Restated Certificate of Incorporation of Quanex Corporation on November 17, 1995 (the "Original Certificate"), the Corporation created a series of 150,000 shares of Preferred Stock without par value classified as Series A Junior Participating Preferred Stock (the "Junior Preferred").

2. No shares of Junior Preferred have been issued.

3. Pursuant to the authority conferred upon the Board of Directors of this Corporation by the Restated Certificate of Incorporation of the Corporation and by Section 151 of the General Corporation Law of the State of Delaware, the Board has authorized certain amendments to the Original Certificate as set forth in the following duly adopted resolutions of the Board:

RESOLVED, that pursuant to the authority vested in the Board of Directors of the Corporation in accordance with the provisions of its Restated Certificate of Incorporation and Section 151 of the General Corporation Law of the State of Delaware, this Board approves and adopts the following amendments to the voting power, preferences and relative, participating, optional and other special rights of the Junior Preferred as set forth in the Certificate of Designation, Preferences and Rights filed as an exhibit to the Restated Certificate of Incorporation of Quanex Corporation on November 17, 1995 (the "Original Certificate") creating the Junior Preferred:

I. Section 2 of the Original Certificate is amended to read as follows:

Section 2. Dividends and Distributions.

(A) Subject to the prior and superior rights of the holders of any shares of any series of Preferred Stock ranking prior and superior to the shares of Series A Junior Participating Preferred

Stock with respect to dividends, the holders of shares of Series A Junior Participating Preferred Stock, in preference to the holders of shares of Common Stock, par value \$0.50 per share (the "Common Stock"), of the Corporation and any other junior stock, shall be entitled to receive, when, as and if declared by the Board of Directors out of funds legally available for the purpose, quarterly dividends payable in cash on the first day of March, June, September and December in each year (each such date being referred to herein as a "Quarterly Dividend Payment Date"), commencing on the first Quarterly Dividend Payment Date after the first issuance of a share or fraction of a share of Series A Junior Participating Preferred Stock in an amount per share (rounded to the nearest cent) equal to the greater of (a) \$1.00, or (b) subject to the provision for adjustment hereinafter set forth, 1000 times the aggregate per share amount of all cash dividends, and 1000 times the aggregate per share amount (payable in kind) of all non-cash dividends or other distributions other than a dividend payable in shares of Common Stock or a subdivision of the outstanding shares of Common Stock (by reclassification or otherwise), declared on the Common Stock, since the immediately preceding Quarterly Dividend Payment Date, or, with respect to the first Quarterly Dividend Payment Date, since the first issuance of any share or fraction of a share of Series A Junior Participating Preferred Stock. In the event the Corporation shall at any time after February 28, 1999 (the "Rights Declaration Date") (i) declare any dividend on Common Stock payable in shares of Common Stock, (ii) subdivide the outstanding Common Stock, or (iii) combine the outstanding Common Stock into a smaller number of shares, then in each such case the amount to which holders of shares of Series A Junior Participating Preferred Stock were entitled immediately prior to such event under clause (b) of the preceding sentence shall be adjusted by multiplying such amount by a fraction the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

(B) The Corporation shall declare a dividend or distribution on the Series A Junior Participating Preferred Stock as provided in paragraph (A) above immediately after it declares a dividend or distribution on the Common Stock (other than a dividend payable in shares of Common Stock); provided that, in the event no dividend or distribution shall have been declared on the Common Stock during the period between any Quarterly Dividend Payment Date and the next

subsequent Quarterly Dividend Payment Date, a dividend of \$1.00 per share on the Series A Junior Participating Preferred Stock shall nevertheless be payable on such subsequent Quarterly Dividend Payment Date.

(C) Dividends shall begin to accrue and be cumulative on outstanding shares of Series A Junior Participating Preferred Stock from the Quarterly Dividend Payment Date next preceding the date of issue of such shares of Series A Junior Participating Preferred Stock unless the date of issue of such shares is prior to the record date for the first Quarterly Dividend Payment Date, in which case dividends on such shares shall begin to accrue from the date of issue of such shares, or unless the date of issue is a Quarterly Dividend Payment Date or is a date after the record date for the determination of holders of shares of Series A Junior Participating Preferred Stock entitled to receive a quarterly dividend and before such Quarterly Dividend Payment Date in either of which events such dividends shall begin to accrue and be cumulative from such Quarterly Dividend Payment Date. Accrued but unpaid dividends shall not bear interest. Dividends paid on the shares of Series A Junior Participating Preferred Stock in an amount less than the total amount of such dividends at the time accrued and payable on such shares shall be allocated pro rata on a share-by-share basis among all such shares at the time outstanding. The Board of Directors may fix a record date for the determination of holders of shares of Series A Junior Participating Preferred Stock entitled to receive payment of a dividend or distribution declared thereon, which record date shall be no more than 30 days prior to the date fixed for the payment thereof.

II. Section 6 of the Original Certificate is amended to read as follows:

Section 6. Liquidation, Dissolution or Winding Up.

(A) Upon any liquidation (voluntary or otherwise), dissolution or winding up of the Corporation, no distribution shall be made to the holders of shares of stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series A Junior Participating Preferred Stock unless, prior thereto, the holders of shares of Series A Junior Participating Preferred Stock shall have received per share, the greater of 1000 times the exercise price per Right (as such term is defined in the Second Amended and Restated Rights Agreement dated as of February , 1999) or 1000 times the payment made per share of Common Stock, plus an amount equal to accrued

and unpaid dividends and distributions thereon, whether or not declared, to the date of such payment (the "Series A Liquidation Preference"). Following the payment of the full amount of the Series A Liquidation Preference, no additional distributions shall be made to the holders of shares of Series A Junior Participating Preferred Stock unless, prior thereto, the holders of shares of Common Stock shall have received an amount per share (the "Common Adjustment") equal to the quotient obtained by dividing (i) the Series A Liquidation Preference by (ii) 1000 (as appropriately adjusted as set forth in subparagraph C below to reflect such events as stock splits, stock dividends and recapitalizations with respect to the Common Stock) (such number in clause (ii), the "Adjustment Number"). Following the payment of the full amount of the Series A Liquidation Preference and the Common Adjustment in respect of all outstanding shares of Series A Junior Participating Preferred Stock and Common Stock, respectively, holders of Series A Junior Participating Preferred Stock and holders of shares of Common Stock shall receive their ratable and proportionate share of the remaining assets to be distributed in the ratio of the Adjustment Number to 1 with respect to such Preferred Stock and Common Stock, on a par share basis, respectively.

(B) In the event there are not sufficient assets available to permit payment in full of the Series A Liquidation Preference and the liquidation preferences of all other series of Preferred Stock, if any, which rank on a parity with the Series A Junior Participating Preferred Stock then such remaining assets shall be distributed ratably to the holders of such parity shares in proportion to their respective liquidation preferences. In the event there are not sufficient assets available to permit payment in full of the Common Adjustment, then such remaining assets shall be distributed ratably to the holders of Common Stock.

(C) In the event the Corporation shall at any time after the Rights Declaration Date (i) declare any dividend on Common Stock payable in shares of Common Stock, (ii) subdivide the outstanding Common Stock, or (iii) combine the outstanding Common Stock into a smaller number of shares, then in each such case the Adjustment Number in effect immediately prior to such event shall be adjusted by multiplying such Adjustment Number by a fraction the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the

denominator of which is the number of shares of Common Stock that were outstanding immediately prior to such event.

III. Section 7 of the Original Certificate is amended to read as follows:

Section 7. Consolidation, Merger, etc. In case the Corporation shall enter into any consolidation, merger, combination or other transaction in which the shares of Common Stock are exchanged for or changed into other stock or securities, cash and/or any other property, then in any such case the shares of Series A Junior Participating Preferred Stock shall at the same time be similarly exchanged or changed in an amount per share (subject to the provision for adjustment hereinafter set forth) equal to 1000 times the aggregate amount of stock, securities, cash and/or any other property (payable in kind), as the case may be, into which or for which each share of Common Stock is changed or exchanged. In the event the Corporation shall at any time after the Rights Declaration Date (i) declare any dividend on Common Stock payable in shares of Common Stock, (ii) subdivide the outstanding Common Stock, or (iii) combine the outstanding Common Stock into a smaller number of shares, then in each such case the amount set forth in the preceding sentence with respect to the exchange or change of shares of Series A Junior Participating Preferred Stock shall be adjusted by multiplying such amount by a fraction the numerator of which is the number of shares of Common Stock outstanding immediately after such event and the denominator of which is the number of shares of Common Stock that are outstanding immediately prior to such event.

IV. Section 12 of the Original Certificate is hereby added to read as follows:

Section 12. Conversion. If the Corporation issues shares of Series A Junior Participating Preferred Stock, or fractions thereof pursuant to Section 11(a)(iii) of the Second Amended and Restated Rights Agreement dated April 15, 1999, between the Company and American Stock Transfer & Trust Co. as Rights Agent, and thereafter validly authorizes additional shares of Common Stock, the Corporation shall send written notice to each holder of one one-thousandth of a share of Series A Junior Participating Preferred Stock stating that the Corporation has authorized additional



shares of Common Stock. Any holder of Series A Junior Participating Preferred Stock may, for a period of sixty days after receipt by the holder of such notice, require the Corporation to convert each one one-thousandth of a share of Series A Junior Participating Preferred Stock held by such holder into one share of Common Stock. To convert shares of Series A Junior Participating Preferred Stock to shares of Common Stock, the holder must send written notice of the holder's intent to convert such shares within sixty days after receipt of the written notice from the Corporation stating that the Corporation has increased the authorized number of shares of Common Stock, together with the stock certificates or certificates duly endorsed evidencing such Series A Junior Participating Preferred Stock. Upon receipt by the Corporation of timely notice from a holder of Series A Junior Participating Preferred Stock of his intent to convert his shares of Series A Junior Participating Preferred Stock into shares of Common Stock, together with the stock certificates or certificates duly endorsed evidencing such Series A Junior Participating Preferred Stock, the Corporation must issue one share of Common Stock for every one one-thousandth of a share of Series A Junior Participating Preferred Stock so converted. If the Corporation has not authorized a sufficient number of shares of Common Stock to allow the conversion of every one one-thousandth of a share of Series A Junior Participating Preferred Stock into one share of Common Stock with respect to which the Company receives valid requests for conversion, then each holder shall be entitled to the number of shares of Common Stock equal to the product of multiplying (i) the number of one one-thousandths of a share of Series A Junior Participating Preferred Stock with respect to which the holder has validly requested conversion by (ii) a fraction, the denominator of which is the number of outstanding one one-thousandths of a share of Series A Junior Participating Preferred Stock of the Company with respect to which the Company receives valid requests for conversion, and the numerator of which is the number of unissued, authorized shares of Common Stock of the Company.

IN WITNESS WHEREOF, Quanex Corporation has caused this Certificate to be signed by its duly authorized officer as of April 15, 1999..

QUANEX CORPORATION

By: /s/ VIREN M. PARIKH

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Name: Viren M. Parikh

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Title: Corporate Controller  
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CERTIFICATE OF CORRECTION  
OF  
AMENDMENT TO CERTIFICATE OF DESIGNATION,  
PREFERENCES AND RIGHTS OF SERIES A JUNIOR  
PARTICIPATING PREFERRED STOCK

Pursuant to the provisions of Section 103(f) of the Delaware General Corporation Law, Quanex Corporation (the "Company") adopts the following Certificate of Correction:

FIRST: On April 15, 1999, the Company filed with the Secretary of State of the State of Delaware an Amendment to Certificate of Designation, Preferences and Rights of Series A Junior Participating Preferred Stock of Quanex Corporation dated April 15, 1999 (the "Amendment"). The Amendment contained an error in Section II(A) in that it failed to set forth correctly the date of the Second Amended and Restated Rights Agreement referred to in Section II(A).

SECOND: Paragraph (A) of Section II of the Amendment is corrected to read as follows:

"(A) Upon any liquidation (voluntary or otherwise), dissolution or winding up of the Corporation, no distribution shall be made to the holders of shares of stock ranking junior (either as to dividends or upon liquidation, dissolution or winding up) to the Series A Junior Participating Preferred Stock unless, prior thereto, the holders of shares of Series A Junior Participating Preferred Stock shall have received per share, the greater of 1000 times the exercise price per Right (as such term is defined in the Second Amended and Restated Rights Agreement dated as of April 15, 1999) or 1000 times the payment made per share of Common Stock, plus an amount equal to accrued and unpaid dividends and distributions thereon, whether or not declared, to the date of such payment (the "Series A Liquidation Preference"). Following the payment of the full amount of the Series A Liquidation Preference, no additional distributions shall be made to the holders of shares of Series A Junior Participating Preferred Stock unless, prior thereto, the holders of shares of Common Stock shall have received an amount per share (the "Common Adjustment") equal to the quotient obtained by dividing (i) the Series A Liquidation Preference by (ii) 1000 (as appropriately adjusted as set forth in subparagraph C below to reflect such events as stock splits, stock dividends and recapitalizations with respect to the Common Stock) (such number in clause (ii), the "Adjustment Number"). Following the payment of the full amount of the Series A Liquidation Preference and the Common Adjustment in respect of all outstanding shares of Series A Junior Participating Preferred Stock and Common Stock, respectively, holders of Series A Junior Participating Preferred Stock and holders of shares of Common Stock shall receive their ratable and proportionate share of the remaining assets to be distributed in the ratio of the Adjustment Number to 1 with respect to such Preferred Stock and Common Stock, on a par share basis, respectively."

IN WITNESS WHEREOF, Quanex Corporation, has caused this Certificate of Correction to be signed by its duly authorized officer on this 16 day of April, 1999.

QUANEX CORPORATION

By: /s/ MICHAEL W. CONLON

-----  
Michael W. Conlon  
Secretary

AMENDMENT TO THE  
QUANEX CORPORATION 1988 STOCK OPTION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1988 Stock Option Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, the Board of Directors of the Company agrees that Section 11 of the Plan is completely amended to provide as follows:

11. TRANSFERABILITY OF OPTIONS. Except as expressly provided otherwise in an Optionee's Agreement with respect to a Nonstatutory Stock Option, an Option shall not be transferable by the Optionee otherwise than by will or under the laws of descent and distribution, and shall be exercisable, during the Optionee's lifetime, only by him.

AMENDMENT TO  
THE QUANEX CORPORATION  
1988 STOCK OPTION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1988 Stock Option Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right in Paragraph 18 of the Plan to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, effective January 1, 2000, the Board of Directors of the Company agrees that Paragraph 12 of the Plan is hereby amended, effective with respect to all Options issued in the future under this Plan, as follows:

12. TERMINATION OF EMPLOYMENT OR DEATH OF OPTIONEE. Except as may be otherwise expressly provided herein with respect to an Option that is a Non-statutory Stock Option, all Options shall terminate on the earlier of the date of the expiration of the Option or one day less than three months after the date of severance, upon severance of the employment relationship between the Company and the optionee, whether with or without cause, for any reason other than the death, disability or, in the case of Non-statutory Stock Options only, Retirement of the optionee, during which period the optionee shall be entitled to exercise the Option in respect of the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Option on the date of such severance of employment. Whether authorized leave of absence, or absence on military or government service, shall constitute severance of the employment relationship between the Company and the optionee shall be determined by the Committee at the time thereof. In the event of severance because of the disability of the holder of any Incentive Stock Option while in the employ of the Company and before the date of expiration of such Incentive Stock Option, such Incentive Stock Option shall terminate on the earlier of such date of expiration or one year following the date of such severance because of disability, during which period the optionee shall be

entitled to exercise the Incentive Stock Option in respect to the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Incentive Stock Option on the date of such severance because of disability. In the event of the death of the holder of any Incentive Stock Option while in the employ of the Company and before the date of expiration of such Incentive Stock Option, such Incentive Stock Option shall terminate on the earlier of such date of expiration or one year following the date of death. After the death of the optionee, his executors, administrators or any person or person to whom his Incentive Stock Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of an Incentive Stock Option to exercise the Incentive Stock Option, in respect to the number of shares that the optionee would have been entitled to exercise if he had exercised the Incentive Stock Option on the date of his death while in employment. For purposes of Incentive Stock Options issued under this Plan, an employment relationship between the Company and the optionee shall be deemed to exist during any period in which the optionee is employed by the Company, a corporation issuing or assuming an option in a transaction to which Section 424(a) of the Code applies, or a parent or subsidiary corporation of such corporation issuing or assuming an option. For this purpose, the phrase "corporation issuing or assuming an option" shall be substituted for the word "Company" in the definitions of parent and subsidiary corporations in Section 4 and the parent-subsidiary relationship shall be determined at the time of the corporate action described in Section 424(a) of the Code.

In the event of the death, disability, or Retirement of a holder of a Non-statutory Stock Option, before the date of expiration of such Non-statutory Stock Option, such Non-statutory Stock Option shall continue fully in effect, including provisions providing for subsequent vesting of such Option, for a period of not less than three years commencing on the date of his death, disability or Retirement, and shall terminate on the earlier of the date of the expiration of such three-year period or the date of expiration of the Non-statutory Stock Option notwithstanding any provision to the contrary in the optionee's Option Agreement. After the death of the optionee, his executors, administrators or any person or person to whom his Non-statutory Stock Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of the Non-statutory Stock Option to exercise the Non-statutory Stock Option, in respect to the number of shares that the optionee would have been entitled to exercise if he were still alive. Notwithstanding the foregoing provisions of this Section, in the case of a Non-statutory Stock Option granted on or after December 8, 1994, the Committee may provide for a different option termination date in the Option Agreement with respect to such Option.

Dated: December 9, 1999

QUANEX CORPORATION  
DEFERRED COMPENSATION PLAN

AMENDED AND RESTATED

JUNE 1, 1999



QUANEX CORPORATION  
DEFERRED COMPENSATION PLAN

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QUANEX CORPORATION  
DEFERRED COMPENSATION PLAN

WHEREAS, Quanex Corporation originally established the Quanex Deferred Compensation Plan (the "Plan") effective October 1, 1981, which provides a mechanism by which certain highly compensated management personnel may defer their compensation under the Quanex Corporation Executive Incentive Compensation Plan prior to such compensation being earned and directors may defer their director's fees prior to their being earned;

WHEREAS, Quanex Corporation amended and restated the Plan effective October 12, 1995;

WHEREAS, Quanex Corporation desires to amend and restate the Plan effective June 1, 1999;

NOW, THEREFORE, Quanex Corporation amends and restates the Plan as follows:

ARTICLE I  
DEFINITIONS

1.1 "ACCOUNT" means a Participant's account in the Deferred Compensation Ledger maintained by the Committee which reflects the benefits a Participant is entitled to under the Plan.

1.2 "BENEFICIARY" means a person or entity designated by the Participant under the terms of the Plan to receive any amounts distributed under the Plan upon the death of the Participant.

1.3 "BOARD" means the Board of Directors of Quanex Corporation.

1.4 "CHANGE OF CONTROL" means the occurrence of one or more of the following events after June 1, 1999:

(a) the acquisition by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Covered Person") of beneficial ownership (within the meaning of rule 13d-3 promulgated under the Exchange Act) of 20 percent or more of either (i) the then outstanding shares of the common stock of Quanex (the "Outstanding Quanex Common Stock"), or (ii) the combined voting power of the then outstanding voting securities of Quanex entitled to vote generally in the election of directors (the "Outstanding Quanex Voting Securities"); provided, however, that for purposes of this subsection (a) of this Section, the following acquisitions shall not constitute a Change of Control of Quanex: (i) any acquisition directly from Quanex, (ii) any acquisition by Quanex, (iii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by Quanex or any entity controlled by Quanex, or (iv) any acquisition by any corporation pursuant to a transaction which complies with clauses (i), (ii) and (iii) of subsection (c) of this Section; or

(b) individuals who, as of June 1, 1999, constitute the Board (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board; provided, however, that any individual becoming a director subsequent to June 1, 1999 whose election, or nomination for election by Quanex's stockholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board shall be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial assumption of office occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents by or on behalf of a Covered Person other than the Board; or

(c) the consummation of (xx) a reorganization, merger or consolidation or sale of Quanex or (yy) a disposition of all or substantially all of the assets of the Company (a "Business Combination"), in each case, unless, following such Business Combination, (i) all or substantially all of the individuals and entities who were the beneficial owners, respectively, of the Outstanding Quanex Common Stock and Outstanding Quanex Voting Securities immediately prior to such Business Combination beneficially own, direct or indirectly, more than 80 percent of, respectively, the then outstanding shares of common stock and the combined voting power of the then outstanding voting securities entitled to vote generally in the election of directors, as the case may be, of the corporation resulting from such Business Combination (including, without limitation, a corporation which as a result of such transaction owns Quanex or all or substantially all of Quanex's assets either directly or through one or more subsidiaries) in substantially the same proportions as their ownership immediately prior to such Business Combination of the Outstanding Quanex Common Stock and Outstanding Quanex Voting Securities, as the case may be, (ii) no Covered Person (excluding any employee benefit plan (or related trust) of Quanex or such corporation resulting from such Business Combination) beneficially owns, directly or indirectly, 20 percent or more of, respectively, the then outstanding shares of common stock of the corporation resulting from such Business Combination or the combined voting power of the then outstanding voting securities of such corporation, except to the extent that such ownership existed prior to the Business Combination, and (iii) at least a majority of the members of the board of directors of the corporation resulting from such Business Combination, were members of the Incumbent Board at the time of the execution of the initial agreement, or of the action of the Board of Directors, providing for such Business Combination; or

(d) the approval by the stockholders of Quanex of a complete liquidation or dissolution of Quanex.

1.5 "CHANGE OF CONTROL VALUE" means the amount determined in clause (i), (ii) or (iii), whichever is applicable, as follows: (i) the per share price offered to stockholders of Quanex in the merger, consolidation, reorganization, sale of assets or dissolution transaction that constitutes a Change of Control, (ii) the price per share offered to stockholders of Quanex in any tender offer or exchange offer that constitutes a Change of Control, or (iii) if a Change of Control occurs other than a Change of Control specified in clause (i) or (ii), the fair market value per share of the Common Stock on the date of the Change of Control, based on the closing quotation as described in Section 4.2, on that day. If the consideration offered to stockholders of the Company in any transaction described above consists of anything other than cash, the Committee shall determine the cash equivalent of the fair market value of the portion of the consideration offered that is other than cash.

1.6 "CODE" means the Internal Revenue Code of 1986, as amended from time to time.

1.7 "COMMITTEE" means the persons who are from time to time serving as members of the committee administering the Plan.

1.8 "COMMON STOCK" means Quanex's common stock, \$.50 par value (or such other par value as may be designated by the vote of Quanex stockholders or such other equity securities of Quanex into which such common stock may be converted, reclassified or exchanged).

1.9 "COMPANY" means Quanex and any Subsidiary adopting the Plan.

1.10 "COMPANY MATCH" means the 20 percent match which the Company makes to the amount deferred in Common Stock during a Plan Year by a Participant under the Plan for three or more Plan Years.

1.11 "DEFERRED COMPENSATION LEDGER" means the ledger maintained by the Committee for each Participant which reflects the amount of compensation deferred for the Participant under the Plan, the Company match, and the amount of income credited on each of these amounts.

1.12 "DIRECTOR" means any person serving as a member of the Board of Directors.

1.13 "DIRECTOR FEES" means any amount paid to a Director for services in such capacity.

1.14 "DISABILITY" means a mental or physical disability that in the opinion of a physician selected by the Committee, shall prevent the Participant from engaging in any substantial gainful activity, can be expected to result in death or has lasted or can be expected to last for a

continuous period of not less than twelve months, and which: (a) was not contracted, suffered or incurred while the Participant was engaged in or did not result from having engaged in, a felonious criminal enterprise; (b) did not result from alcoholism or addiction to narcotics; and (c) did not result from an injury incurred while a member of the Armed Forces of the United States for which the Participant received a military pension.

1.15 "INCENTIVE BONUS" means a bonus awarded or to be awarded to the Participant under the Quanex Corporation Executive Incentive Compensation Plan.

1.16 "NORMAL RETIREMENT DATE" means the first day of the month that coincides with or next follows the date on which the Participant or former Participant attains age 65.

1.17 "NYSE" means the New York Stock Exchange.

1.18 "PARTICIPANT" means an employee or director of a Company who is participating in the Plan.

1.19 "PLAN" means the Quanex Corporation Deferred Compensation Plan set forth in this document, as amended from time to time.

1.20 "PLAN YEAR" means a one-year period that coincides with the fiscal year of Quanex, which begins on the first day of November of each calendar year and ends on October 31 of the next ensuing calendar year.

1.21 "QUANEX" means the Quanex Corporation, a Delaware corporation, the sponsor of the Plan.

1.22 "RABBI TRUST" means the Quanex Corporation Deferred Compensation Trust, which agreement was entered into between NBD Bank and Quanex.

1.23 "RETIREMENT" means the retirement of a Participant from any Company covered by the Plan under the terms of the Retirement Plan.



1.24 "RETIREMENT PLAN" means the Quanex Corporation Salaried Employees' Pension Plan, or if the Company does not maintain that plan, the defined contribution plan maintained by the Company that is intended to satisfy the requirements of section 401(a) of the Code.

1.25 "SECURITIES ACT" means the Securities Exchange Act of 1934, as amended from time to time.

1.26 "SUBSIDIARY" means any wholly owned subsidiary of Quanex.

1.27 "TERM OF DEFERRAL" means the period of deferral chosen by the Participant under the election procedure established in Section 3.1 or by the Committee which pertains to that portion of the Incentive Bonus or Director Fees for each given Plan Year and its accumulated income accrued that has been deferred under an election made prior to the commencement of the period during which it is earned.

1.28 "VOTING SECURITIES" means any security which ordinarily possesses the power to vote in the election of the Board without the happening of any precondition or contingency.

ARTICLE II  
ELIGIBILITY

Initially, all participants in the Quanex Corporation Executive Incentive Compensation Plan and all Directors will be eligible to participate in the Plan. However, the Committee retains the right to establish such additional eligibility requirements for participation in the Plan as it may determine are appropriate or necessary from time to time and has the right to determine, in its sole discretion, that any one or more persons who meet the eligibility requirements will not be eligible to participate for one or more Plan Years beginning after the date they are notified of this decision by the Committee.

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## ARTICLE III

## DEFERRALS AND COMPANY CONTRIBUTIONS

3.1 DEFERRAL ELECTION. A Participant may elect during the election period established by the Committee prior to the beginning of any Plan Year:

(1) the percentage of his Incentive Bonus earned during the ensuing Plan Year which is to be paid as soon as conveniently possible after the Plan Year and the percentage which is to be deferred under the Plan;

(2) the percentage of his Director Fees earned during the ensuing Plan Year which is to be paid during such year and the percentage which is to be deferred under the Plan;

(3) the percentage of the amount deferred, if any, to be deferred in the form of Common Stock and the percentage, if any, to be deferred in the form of cash;

(4) the length of the period of deferral, if any amount has been elected to be deferred, whether in cash or in Common Stock, which deferral shall be for a period of years, to a date certain, to termination of employment with the Company or to his Retirement; and

(5) the form of payment of the amount that has been elected to be deferred -- a lump sum, or quarterly or annual installment payments of the principal amount plus the interest accrued after the distribution date, or last installment paid, if later, in the case of a deferral in the form of cash or of the total shares of Common Stock credited to him as of the date of distribution plus any other shares, cash or other property credited as dividends or other rights on those shares after the distribution date or last installment distributed, if later, in the case of a deferral in the form of Common Stock, over no less than three nor more than 20 years.

If a Participant elects a deferral period to Retirement, he shall also specify whether the deferral period shall end at the date of his termination of employment with the Company or at his Normal Retirement Date, in the event of termination other than as a result of death, Disability

or Retirement. If a Participant elects a deferral period of a number of years or to a date certain, the deferral period shall end upon the Participant's Retirement, if earlier.

The deferrals in the form of Common Stock elected by Participants to be allocated to their Accounts in any Plan Year must not exceed one percent of the shares of Common Stock outstanding on the first day of the Plan Year. In the event this maximum would be exceeded, each Participant who elected to defer in the form of Common Stock shall have his election reduced on a pro rata basis as compared to all Participants who elected to defer in the form of Common Stock until those deferrals in the aggregate for that Plan Year equal the maximum and the portion of his Incentive Bonus which would have been deferred in the form of Common Stock shall instead be distributed to the Participant as provided in the Quanex Corporation Executive Incentive Compensation Plan.

Once an election has been made it becomes irrevocable for that Plan Year, except that the Participant may change his election of the form of payment he previously elected under Section 3.1(5) during a 30-day period ending one year prior to the end of the deferral period. In the event a Participant originally elected a deferral period of a number of years or until a date certain and, as a result of the Participant's election to take Retirement, the Participant will retire before the end of the elected deferral period, the Participant may elect to change the form of payment during a 30- day period ending one year prior to the Retirement date chosen by the Participant by written notice to the Company. In the event a Participant changes his election, if the deferral period terminates early for any reason, which is beyond the control of the Participant, such as involuntary termination of employment, death or Disability, then the distribution or the first installment, whichever is applicable, shall not be made until one year after the election was changed; however, if the deferral period terminates early for any reason which is within the control of the Participant,

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such as Retirement or voluntary termination of employment, then the change of election will be ineffective. If for any reason the deferral period does not end one year after the end of such 30-day period because of a postponement of Retirement or otherwise, the change of election shall remain in effect and no further changes of election shall be permitted.

The election to participate in the Plan for a given Plan Year will be effective only upon receipt by the Committee of the Participant's election on such form as will be determined by the Committee from time to time. If the Participant does not exercise his right to defer, subject to Section 3.3 below, the Participant will be deemed to have elected not to defer any part of his Incentive Bonus or Director Fees for that Plan Year and all of his Incentive Bonuses and Director Fees will be paid in cash. If the percentage of the Incentive Bonus and Director Fees elected to be deferred in Common Stock results in a fractional share, it shall be reduced to the next lowest full share and the fractional share shall be paid or deferred, as the case may be, in cash.

3.2 COMPANY MATCH. The Company will credit to the Account of each Participant who has a portion of his Incentive Bonus or Director Fees deferred under the Plan in the form of Common Stock for a period of three full years or more additional shares of Common Stock equal to 20 percent of the amount which is deferred in the form of Common Stock, rounded to the next highest number of full shares.

3.3 MANDATORY DEFERRAL. If a Participant becomes entitled to a cash payment of part or all of an Incentive Bonus because the Participant did not elect to defer all of the Incentive Bonus but the Company determines that section 162(m) of the Code may not allow the Company to take a deduction for part or all of the Incentive Bonus, then, unless a Change of Control has occurred after June 1, 1999, the payment of the Incentive Bonus will be delayed until December 1st following the end of the Plan Year in which it occurred. Then on December 1st, if the Company's

deduction is determined by the Company not to be affected, the Incentive Bonus in total will be paid immediately. However, if the Company determines that some portion of the Incentive Bonus is affected, then only that portion of the Incentive Bonus which is deductible by the Company shall be paid on December 1st and the remaining portion of the Incentive Bonus will be delayed to the first day of the first complete month of the second Plan Year, at which time it will be paid. The Committee may waive the mandatory deferral required by this Section 3.3 with respect to a Participant who is not a member of the Committee but such waiver shall only be made on an individual basis and at the time the Incentive Bonus is determined and awarded.

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## ARTICLE IV

## ACCOUNT

4.1 ESTABLISHING A PARTICIPANT'S ACCOUNT. The Committee will establish an Account for each Participant in a special Deferred Compensation Ledger which will be maintained by the Company. The Account will reflect the amount of the Company's obligation to the Participant at any given time.

4.2 CREDIT OF THE PARTICIPANT'S DEFERRAL AND THE COMPANY'S MATCH. Upon completion of the Plan Year or quarter, as applicable, the Committee will determine, as soon as administratively practicable, the amount of a Participant's Incentive Bonus or Director Fees that has been deferred for that Plan Year or quarter, as applicable, and the amount of the Company Match, if any, and will credit that or those amounts to the Participant's Account as of the end of the Plan Year or quarter, as applicable, during which the Incentive Bonus or Director Fees were earned. If the Participant elected his deferral to be in the form of Common Stock, the number of shares credited to his Account as Common Stock shall be the number of full shares of Common Stock that could have been purchased with the dollar amount deferred, without taking into account any brokerage fees, taxes or other expenses which might be incurred in such a transaction, based upon the closing quotation on the NYSE, or if not traded on the NYSE, the principal market in which the Common Stock is traded on the date the amount would have been paid had it not been deferred pursuant to Article III, and any additional fractional amount shall be credited to the Participant's Account in the form of cash.

4.3 CREDITING OF DIVIDENDS, DISTRIBUTIONS AND INTEREST. When dividends are declared and paid, or other distributions, whether stock, property, cash, rights or other, are made with

respect to the Common Stock, those dividends and other distributions shall be accrued in a Participant's Account based upon the shares of Common Stock credited to his Account. The dividends or other distributions in the form of shares of Common Stock shall be credited to the Account as additional shares of Common Stock. The dividends or other distributions or rights in any other form shall be credited to the Participant's Account in the form of cash. For this purpose, all dividends and distributions not in the form of shares of Common Stock or cash shall be valued at the fair market value as determined by a resolution duly adopted by the Committee. Interest will be accrued on that portion of a Participant's Account held in the form of cash at the rate established by Section 4.4.

4.4 INTEREST RATE. Interest will be accrued on the last day of each calendar month on each portion of a Participant's Account held in the form of cash (whether resulting from a cash deferral, cash dividends or other cash distributions on Common Stock or the conversion of a Common Stock credit in his Account to cash) from the later of (a) the time it is credited to his Account or (b) the last previous calendar month end at a rate equal to (x) the rate of interest announced by Chase Manhattan Bank, N.A., or its successor, if applicable as its prime rate of interest on the last business day of the calendar quarter preceding the calendar quarter in which the month falls divided by (y) four. Interest so accrued on the last day of each calendar month shall be credited as cash to the Participant's Account and shall thereafter accrue interest. Interest will continue to be credited on the cash balance in the Participant's Account until the entire cash balance has been distributed.

4.5 COMMON STOCK CONVERSION ELECTION. At any time during a period of three years prior to the earliest time a Participant could retire under the Retirement Plan and ending on the Participant's Normal Retirement Date, the Participant may elect a Retirement date under the



Retirement Plan and may elect to have all or a portion of his shares of Common Stock in his Account converted to cash. In that event, all such shares of Common Stock shall be converted on the date notice is received by the Company based upon the closing quotation as described in Section 4.2, on that day, unless the Participant has specified no more than five different dates after the date of the notice on which the Participant desires all or a portion of the shares of Common Stock to be converted and the percentage of shares to be converted on each date. If the Participant has specified dates for and the percentage of shares to be converted, then the designated percentage of shares of Common Stock to be converted on each date shall be converted on the specified date based on the closing quotation as described in Section 4.2 on such specified dates.

At any time that is at least five years after Common Stock is credited to his Account pursuant to Section 4.2, a Participant may elect to have such Common Stock converted to cash and credited to his Account. In that event, all such shares of Common Stock specified by the Participant in a written notice to the Company which have been credited to the Participant's Account for at least five years prior to the giving of such notice shall be converted on the date notice is received by the Company based upon the closing quotation as described in Section 4.2, on that day.

#### 4.6 CONVERSION AND CASH-OUT UPON A CHANGE OF CONTROL.

Notwithstanding any other provision of the Plan, immediately upon the occurrence of a Change of Control, all shares of Common Stock credited to a current or former Participant's Account shall be converted to cash based on the Change of Control Value of such shares of Common Stock. Within five days after the date on which the Change of Control occurs, all current and former Participants shall be paid in cash lump sum payments the balances credited to their Accounts.

## ARTICLE V

## VESTING AND EVENTS CAUSING FORFEITURE

5.1 VESTING. All deferrals of the Incentive Bonus and Director Fees and all income accrued on the deferrals will be 100 percent vested except for the events of forfeiture described in Sections 5.3 and 5.4. All Company matching accruals and all income accrued on those matching accruals will be 100 percent vested except for the events of forfeiture described in Section 5.2, 5.3 and 5.4.

5.2 FORFEITURE OF COMPANY MATCH BECAUSE OF EARLY DISTRIBUTION. If, but for the provisions of this Section 5.2, a Participant would receive a benefit from the Plan for any reason, other than death, disability or Retirement, in respect of shares of Common Stock credited to the Participant's account pursuant to Section 4.2 as a result of the Company matching accrual of 20 percent provided for in Section 3.2 within three years after such shares were so credited, or if the Participant ceases to be an employee with respect to a matching accrual resulting from deferral of an Incentive Bonus, or a director with respect to a matching accrual resulting from deferral of Director Fees within three years after such shares are so credited, such matching accruals of shares of Common Stock and any dividends or other property or rights accumulated because of those shares of Common Stock shall be immediately forfeited.

5.3 FORFEITURE FOR CAUSE. If the Committee finds, after full consideration of the facts presented on behalf of both the Company and a former Participant, that the Participant was discharged by the Company for fraud, embezzlement, theft, commission of a felony, proven dishonesty in the course of his employment by the Company which damaged the Company, or for disclosing trade secrets of the Company, the entire amount credited to his Account, exclusive of an

amount equal to the sum of the total deferrals of the Participant, will be forfeited. The decision of the Committee as to the cause of a former Participant's discharge and the damage done to the Company will be final. No decision of the Committee will affect the finality of the discharge of the Participant by the Company in any manner.

5.4 FORFEITURE FOR COMPETITION. If at the time a distribution is being made or is to be made to a Participant or former Participant, the Committee finds after full consideration of the facts presented on behalf of the Company and the Participant or former Participant, that the Participant or former Participant at any time within two years from his termination of employment from the Company, and without written consent of the Company, directly or indirectly owns, operates, manages, controls or participates in the ownership, management, operation or control of or is employed by, or is paid as a consultant or other independent contractor by a business which competes or at any time did compete with the Company by which he was formerly employed in a trade area served by the Company at the time distributions are being made or to be made and in which the Participant or former Participant had represented the Company while employed by it; and, if the Participant or former Participant continues to be so engaged 60 days after written notice has been given to him, the Committee will forfeit all amounts otherwise due the Participant or former Participant, exclusive of an amount equal to the sum of the total deferrals of the Participant or former Participant.

5.5 FULL VESTING IN THE EVENT OF A CHANGE OF CONTROL. The forfeitures created by sections 5.2, 5.3 or 5.4 shall not apply with respect to any amounts credited to the Accounts of current or former Participants after the occurrence of a Change of Control.

ARTICLE VI  
DISTRIBUTIONS

6.1 FORM OF DISTRIBUTIONS OR WITHDRAWALS. Upon a distribution or withdrawal, at the option of Quanex, the number of shares of Common Stock credited to the Participant in the Deferred Compensation Ledger, if any, required to be distributed shall be distributed in kind or in cash, whether the distribution or withdrawal is in a lump sum or in installments. If distributed in cash, the amount per share of Common Stock which would otherwise be distributed in kind shall equal the closing quotation for the Common Stock on the NYSE (or if not traded on the NYSE, the principal market in which the Common Stock is traded) on the third business day prior to the date of distribution. If the distribution is in installments, all dividends and other property or rights accumulating on the shares still undistributed will be credited as provided in Section 4.3 and distributed with the next installment. If there are periodic installments to be made of the portion, if any, deferred as cash, income shall accumulate on that portion of the Account as described in Section 4.6 until the balance credited to the cash portion of the Participant's Account has been distributed. In that event, income accumulating on the cash portion of the Account shall be distributed with the next installment to be distributed.

6.2 DEATH. Upon the death of a Participant prior to the expiration of the Term of Deferral, the Participant's Beneficiary or Beneficiaries will receive in Common Stock or cash as required by Section 6.1, the balance then credited to the Participant's Account in the Deferred Compensation Ledger. The lump sum distribution or the first installment of the periodic distribution will be made 90 days after the Participant's death.

Each Participant, upon making his initial deferral election, will file with the Committee a designation of one or more Beneficiaries to whom distributions otherwise due the Participant will be made in the event of his death prior to the complete distribution of the amount credited to his Account in the Deferred Compensation Ledger. The designation will be effective upon receipt by the Committee of a properly executed form which the Committee has approved for that purpose. The Participant may from time to time revoke or change any designation of Beneficiary by filing another approved Beneficiary designation form with the Committee. If there is no valid designation of Beneficiary on file with the Committee at the time of the Participant's death, or if all of the Beneficiaries designated in the last Beneficiary designation have predeceased the Participant or otherwise ceased to exist, the Beneficiary will be the Participant's spouse, if the spouse survives the Participant, or otherwise the Participant's estate. A Beneficiary must survive the Participant by 60 days in order to be considered to be living on the date of the Participant's death. If any Beneficiary survives the Participant but dies or otherwise ceases to exist before receiving all amounts due the Beneficiary from the Participant's Account, the balance of the amount which would have been paid to that Beneficiary will, unless the Participant's designation provides otherwise, be distributed to the individual deceased Beneficiary's estate or to the Participant's estate in the case of a Beneficiary which is not an individual. Any Beneficiary designation which designates any person or entity other than the Participant's spouse must be consented to in writing in a form acceptable to the Committee in order to be effective.

6.3 DISABILITY. Upon the Disability of a Participant prior to the expiration of the Term of Deferral, the Participant will receive in Common Stock or cash as required by Section 6.1, the balance then credited to the Participant's Account. The lump sum distribution or the first installment of the periodic distribution will be made 90 days after the Participant becomes disabled.

6.4 EXPIRATION OF TERM OF DEFERRAL. Upon the expiration of the Term of Deferral, the Participant shall receive in Common Stock or cash as required by Section 6.1, the balance credited to the Participant's Account. The lump sum distribution or the first installment of the periodic distribution will be made 90 days after the expiration of the Term of Deferral without regard to whether the Participant is still employed by the Company or not.

6.5 HARDSHIP WITHDRAWALS. Any Participant who is in the employ of a Company and is not entitled to a distribution from the Plan may request a hardship withdrawal. No hardship withdrawal can exceed the lesser of the amount credited to the Participant's Account or the amount reasonably needed to satisfy the emergency need. Whether a hardship exists and the amount reasonably needed to satisfy the emergency need will be determined by the Committee based upon the evidence presented by the Participant and the rules established in this Section. If a hardship withdrawal is approved by the Committee it will be made in Common Stock or cash as required in Section 6.1 within ten days of the Committee's determination. A hardship for this purpose is a severe financial hardship to the Participant resulting from a sudden and unexpected illness or accident of the Participant or of a dependent (as defined in section 152(a) of the Code) of the Participant, loss of the Participant's property due to casualty, or any similar extraordinary and unforeseeable circumstance arising as a result of events beyond the control of the Participant. The circumstances that will constitute a hardship will depend upon the facts of each case, but, in any case, payment may not be made to the extent that the hardship is or may be relieved: (a) through reimbursement or compensation by insurance or otherwise, (b) by liquidation of the Participant's assets, to the extent the liquidation of such assets will not itself cause severe financial hardship, or (c) by cessation of deferrals under the Plan. Such foreseeable needs for funds as the need to send a Participant's child to college or the desire to purchase a home will not be considered to be a hardship.

#### 6.6 PAYMENT RESTRICTIONS ON ANY PORTION OF A BENEFIT

DETERMINED NOT TO BE DEDUCTIBLE. Except for hardship withdrawals under Section 6.5, if a Participant has a benefit that is due during a Plan Year and the Committee determines that section 162(m) of the Code could affect the Company's deduction on the amount paid, the distribution of his benefit will be delayed until December 1 following the end of the Plan Year. Then on December 1 if the Company's deduction is determined by the Committee not to be affected, the benefit in total will be distributed immediately; however, if the Committee determines that some portion of the benefit is affected, then only that portion of the benefit which is deductible by the Company shall be distributed on December 1st and the distribution of the remaining portion of the benefit will be delayed to the first day of the first complete month of the Plan Year or Years on which a portion or all of the remaining distribution can be made and deducted by the Company on its federal income tax return. The Committee may waive the mandatory deferral required by this Section 6.6 with respect to a Participant who is not a member of the Committee, but such waiver shall only be made on an individual basis and at the time the distribution is to be made.

#### 6.7 RESPONSIBILITY FOR DISTRIBUTIONS AND WITHHOLDING OF TAXES.

The Committee will furnish information to the Company last employing the Participant, concerning the amount and form of distribution to any Participant entitled to a distribution so that the Company may make or cause the Rabbi Trust to make the distribution required. It will also calculate the deductions from the amount of the benefit paid under the Plan for any taxes required to be withheld by federal, state or local government and will cause them to be withheld. If a Participant has deferred compensation under the Plan while in the service of more than one Company, each Company for which the Participant was working will reimburse the disbursing agent for the amount attributable to compensation deferred while the Participant was in the service of that Company if it has not already provided that funding to the disbursing agent.

## ARTICLE VII

## ADMINISTRATION

7.1 COMMITTEE APPOINTMENT. The Committee will be appointed by the Board. The initial Committee members will be Compensation Committee of the Board. Each Committee member will serve until his or her resignation or removal. The Board will have the sole discretion to remove any one or more Committee members and appoint one or more replacement or additional Committee members from time to time.

7.2 COMMITTEE ORGANIZATION AND VOTING. The Committee will select from among its members a chairman who will preside at all of its meetings and will elect a secretary without regard to whether that person is a member of the Committee. The secretary will keep all records, documents and data pertaining to the Committee's supervision and administration of the Plan. A majority of the members of the Committee will constitute a quorum for the transaction of business and the vote of a majority of the members present at any meeting will decide any question brought before the meeting. In addition, the Committee may decide any question by vote, taken without a meeting, of a majority of its members. If a member of the Committee is ever appointed who is or becomes a Participant, that Committee member will not vote or act on any matter relating solely to himself.

7.3 POWERS OF THE COMMITTEE. The Committee will have the exclusive responsibility for the general administration of the Plan according to the terms and provisions of the Plan and will have all powers necessary to accomplish those purposes, including but not by way of limitation the right, power and authority:

(a) to make rules and regulations for the administration of the Plan;



(b) to construe all terms, provisions, conditions and limitations of the Plan;

(c) to correct any defect, supply any omission or reconcile any inconsistency that may appear in the Plan in the manner and to the extent it deems expedient to carry the Plan into effect for the greatest benefit of all parties at interest;

(d) to designate the persons eligible to become Participants and to establish the maximum and minimum amounts that may be elected to be deferred;

(e) to determine all controversies relating to the administration of the Plan, including but not limited to:

(1) differences of opinion arising between the Company and a Participant except when the difference of opinion relates to the entitlement to, the amount of or the method or timing of a distribution of a benefit affected by a Change of Control, in which event it shall be decided by judicial action; and

(2) any question it deems advisable to determine in order to promote the uniform administration of the Plan for the benefit of all parties at interest; and

(f) to delegate by written notice those clerical and recordation duties of the Committee, as it deems necessary or advisable for the proper and efficient administration of the Plan.

7.4 COMMITTEE DISCRETION. The Committee in exercising any power or authority granted under the Plan or in making any determination under the Plan shall perform or refrain from performing those acts using its sole discretion and judgment. Any decision made by the Committee or any refraining to act or any act taken by the Committee in good faith shall be final and binding on all parties. The Committee's decision shall never be subject to de novo review. Notwithstanding the foregoing, the Committee's decision, refraining to act or acting is to be subject to judicial review for those incidents occurring during the Plan Year in which a Change of Control occurs and during the next three succeeding Plan Years.

7.5 ANNUAL STATEMENTS. The Committee will cause each Participant to receive an annual statement as soon as administratively possible after the conclusion of each Plan Year containing the amounts deferred, the Company match, if any, and the income accrued on the deferred and matched amounts.

7.6 REIMBURSEMENT OF EXPENSES. The Committee will serve without compensation for their services but will be reimbursed by Quanex for all expenses properly and actually incurred in the performance of their duties under the Plan.

## ARTICLE VIII

## ADOPTION BY SUBSIDIARIES

8.1 PROCEDURE FOR AND STATUS AFTER ADOPTION. Any Subsidiary may, with the approval of the Committee, adopt the Plan by appropriate action of its board. The terms of the Plan will apply separately to each Subsidiary adopting the Plan and its Participants in the same manner as is expressly provided for Quanex and its Participants except that the powers of the Board and the Committee under the Plan will be exercised by the Board alone. Quanex and each Subsidiary adopting the Plan will bear the cost of providing plan benefits for its own Participants. It is intended that the obligation of Quanex and each Subsidiary with respect to its Participants will be the sole obligation of the Company that is employing the Participant and will not bind any other Company.

8.2 TERMINATION OF PARTICIPATION BY ADOPTING SUBSIDIARY. Any Subsidiary adopting the Plan may, by appropriate action of its board of directors, terminate its participation in the Plan. The Committee may, in its discretion, also terminate a Subsidiary's participation in the Plan at any time. The termination of the participation in the Plan by a Subsidiary will not, however, affect the rights of any Participant who is working or has worked for the Subsidiary as to amounts or shares of Common Stock previously standing to his credit in his Account or reduce the income accrued on amounts deferred by him or matched by the Company and credited to his Account whether in cash or in shares of Common Stock, prior to the distribution of the benefit to the Participant without his consent.

ARTICLE IX  
AMENDMENT AND/OR TERMINATION

9.1 AMENDMENT OR TERMINATION OF THE PLAN. The Board may amend or terminate the Plan at any time by an instrument in writing without the consent of any adopting Company.

9.2 NO RETROACTIVE EFFECT ON AWARDED BENEFITS. No amendment will affect the rights of any Participant to the amounts, whether in cash or shares of Common Stock, then standing to his credit in his Account, to change the method of calculating the income already accrued or to accrue in the future on amounts already deferred by him or matched by the Company prior to the date of the amendment or to change a Participant's right under any provision relating to a Change of Control after a Change of Control has occurred, without the Participant's consent. However, the Board shall retain the right at any time to change in any manner the method of calculating the match by the Company and the income to accrue on all amounts to be deferred in the future by a Participant and/or to be matched in the future by the Company after the date of the amendment if it has been announced to the Participants.

9.3 EFFECT OF TERMINATION. If the Plan is terminated, all amounts, whether in cash or in shares of Common Stock, deferred by Participants and matched by the Company will continue to be held under the terms of the Plan until all amounts have been distributed according to the elections made by the Participants or the directives made by the Committee prior to the deferrals. The forfeiture provisions of Sections 5.2, 5.3 and 5.4 and the restriction set out in Section 6.6 would continue to apply throughout the period after the termination of the Plan but prior to the completed distribution of all benefits.

## ARTICLE X

## FUNDING

10.1 PAYMENTS UNDER THIS AGREEMENT ARE THE OBLIGATION OF THE COMPANY. The Company will distribute the benefits due the Participants under the Plan; however, should it fail to do so when a benefit is due and the funding trust contemplated by Section 10.2 exists, the benefit will be distributed by the trustee of that funding trust. In any event, if the trust fails to distribute a benefit for any reason, the Company still remains liable for all benefits provided by the Plan.

10.2 AGREEMENT MAY BE FUNDED THROUGH RABBI TRUST. It is specifically recognized by both the Company and the Participants that the Company may, but is not required to transfer any funds, shares or Common Stock or other assets that it finds desirable to a trust established to accumulate assets sufficient to fund the obligations of all of the Companies signatory to the Plan. However, under all circumstances, the Participants will have no rights to any of those assets; and likewise, under all circumstances, the rights of the Participants to the assets held in the trust will be no greater than the rights expressed in this agreement. Nothing contained in the trust agreement which creates the funding trust will constitute a guarantee by any Company that assets of the Company transferred to the trust will be sufficient to fund all benefits under the Plan or would place the Participant in a secured position ahead of general creditors should the Company become insolvent or bankrupt. Any trust agreement prepared to fund the Company's obligations under this agreement must specifically set out these principles so it is clear in that trust agreement that the Participants in the Plan are only unsecured general creditors of the Company in relation to their benefits under the Plan.

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10.3 REVERSION OF EXCESS ASSETS. Any adopting Company may, at any time, request the actuary, who last performed the annual actuarial valuation of the Quanex defined benefit Retirement plan, to determine the present Account balance, assuming the accrual rate for income not to be reduced (whether it actually is or not), as of the month end coincident with or next preceding the request, of all Participants and Beneficiaries of deceased Participants for which all Companies are or will be obligated to make benefit distributions under the Plan. If the fair market value of the assets held in the trust, as determined by the Trustee as of that same date, exceeds the total of the Account balances of all Participants and Beneficiaries by 25 percent, any Company may direct the trustee to return to each Company its proportionate part of the assets which are in excess of 125 percent of the Account balances. Each Company's share of the excess assets will be the Participants' Accounts accrued while in the employ of that Company as compared to the total of the Account balances accrued by all Participants under the Plan times the excess assets. If there has been a Change of Control, for the purpose of determining if there are excess funds, all contributions made prior to the Change of Control will be subtracted from the fair market value of the assets held in the trust as of the determination date but before the determination is made.

10.4 PARTICIPANTS MUST RELY ONLY ON GENERAL CREDIT OF THE COMPANY. It is also specifically recognized by both the Company and the Participants that the Plan is only a general corporate commitment and that each Participant must rely upon the general credit of the Company for the fulfillment of its obligations under the Plan. Under all circumstances the rights of Participants to any asset held by the Company will be no greater than the rights expressed in this agreement. Nothing contained in this agreement will constitute a guarantee by the Company that the assets of the Company will be sufficient to distribute any benefits under the Plan or would place the Participant in a secured position ahead of general creditors of the Company. Though the

Company may establish or become a signatory to a Rabbi Trust, as indicated in Section 10.1, to accumulate assets to fulfill its obligations, the Plan and any such trust will not create any lien, claim, encumbrance, right, title or other interest of any kind in any Participant in any asset held by the Company, contributed to any such trust or otherwise designated to be used in fulfillment of any of its obligations created in this agreement. No specific assets of the Company have been or will be set aside, or will in any way be transferred to the trust or will be pledged in any way for the performance of the Company's obligations under the Plan which would remove such assets from being subject to the general creditors of the Company.

ARTICLE XI  
MISCELLANEOUS

11.1 LIMITATION OF RIGHTS. Nothing in the Plan will be construed:

- (a) to give any employee of any Company any right to be designated a Participant in the Plan;
- (b) to give a Participant any right with respect to the compensation deferred, the Company match or the income accrued and credited in the Deferred Compensation Ledger except in accordance with the terms of the Plan;
- (c) to limit in any way the right of the Company to terminate a Participant's employment with the Company at any time;
- (d) to evidence any agreement or understanding, expressed or implied, that the Company will employ a Participant in any particular position or for any particular remuneration; or
- (e) to give a Participant or any other person claiming through him any interest or right under the Plan other than that of any unsecured general creditor of the Company.

11.2 DISTRIBUTIONS TO INCOMPETENTS OR MINORS. Should a Participant become incompetent or should a Participant designate a Beneficiary who is a minor or incompetent, the Committee is authorized to distribute the benefit due to the parent of the minor or to the guardian of the minor or incompetent or directly to the minor or to apply those assets for the benefit of the minor or incompetent in any manner the Committee determines in its sole discretion.

11.3 NONALIENATION OF BENEFITS. No right or benefit provided in the Plan will be transferable by the Participant except, upon his death, to a named Beneficiary as provided in the Plan. No right or benefit under the Plan will be subject to anticipation, alienation, sale, assignment, pledge, encumbrance or charge, and any attempt to anticipate, alienate, sell, assign, pledge, encumber, or charge the same will be void. No right or benefit under the Plan will in any manner



be liable for or subject to any debts, contracts, liabilities or torts of the person entitled to such benefits. If any Participant or any Beneficiary becomes bankrupt or attempts to anticipate, alienate, sell, assign, pledge, encumber or charge any right or benefit under the Plan, that right or benefit will, in the discretion of the Committee, cease. In that event, the Committee may have the Company hold or apply the right or benefit or any part of it to the benefit of the Participant or Beneficiary, his or her spouse, children or other dependents or any of them in any manner and in any proportion the Committee believes to be proper in its sole and absolute discretion, but is not required to do so.

11.4 EXPENSES INCURRED IN ENFORCING THE PLAN. The Company will, in addition, pay a Participant for all legal fees and expenses incurred by him in contesting or disputing his termination or in seeking to obtain or enforce any benefit provided by the Plan if the termination occurs in the Plan Year in which a Change of Control occurs or during the next three succeeding Plan Years following the Plan Year in which a Change of Control occurs except to the extent that the payment of those fees or expenses are restricted under Section 6.6.

11.5 RELIANCE UPON INFORMATION. The Committee will not be liable for any decision or action taken or not taken in good faith in connection with the administration of the Plan. Without limiting the generality of the foregoing, any decision or action taken or not taken by the Committee when it relies upon information supplied it by any officer of the Company, the Company's legal counsel, the Company's independent accountants or other advisors in connection with the administration of the Plan will be deemed to have been taken in good faith.

11.6 SEVERABILITY. If any term, provision, covenant or condition of the Plan is held to be invalid, void or otherwise unenforceable, the rest of the Plan will remain in full force and effect and will in no way be affected, impaired or invalidated.

11.7 NOTICE. Any notice or filing required or permitted to be given to the Committee or a Participant will be sufficient if in writing and hand-delivered or sent by U.S. mail to the principal office of the Company or to the residential mailing address of the Participant. Notice will be deemed to be given as of the date of hand-delivery or if delivery is by mail, as of the date shown on the postmark.

11.8 GENDER AND NUMBER. If the context requires it, words of one gender when used in the Plan will include the other genders, and words used in the singular or plural will include the other.

11.9 GOVERNING LAW. The Plan will be construed, administered and governed in all respects by the laws of the State of Texas.

IN WITNESS WHEREOF, the Company has executed this document on this 29th day of September, 1999.

QUANEX CORPORATION

By /s/ PAUL GIDDENS

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FIRST AMENDMENT TO  
QUANEX CORPORATION  
DEFERRED COMPENSATION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, on September 29, 1999, the Company executed the Plan known as "Quanex Corporation Deferred Compensation Plan" (the "Plan"); and

WHEREAS, the Company retained the right in Section 9.1 of the Plan to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company approved resolutions on the 7th day of December, 1999, to amend the Plan;

NOW, THEREFORE, the Company agrees that, effective as of December 7, 1999, Section 3.3 of the Plan is amended in its entirety to read as follows:

3.3 MANDATORY DEFERRAL. If (1) a Participant becomes entitled to a cash payment of part or all of an Incentive Bonus because the Participant did not elect to defer all of the Incentive Bonus, (2) the Company determines that section 162(m) of the Code may not allow the Company to take a deduction for part or all of the Incentive Bonus and, (3) effective June 1, 1999, a Change of Control has not occurred, then, the payment of the amount of the Incentive Bonus that is not deductible by the Company will be delayed and deferred under the provisions of the Plan until the 76th day following the end of the Plan Year in which the Incentive Bonus was earned, on which date the total Incentive Bonus will be paid immediately. The Committee may waive the mandatory deferral required by this Section 3.3 with respect to a Participant who is not a member of the Committee but such waiver shall only be made on an individual basis and at the time the Incentive Bonus is determined and awarded.

IN WITNESS WHEREOF, the Company has executed this Agreement this 7th day of December, 1999.

QUANEX CORPORATION

By /s/ PAUL GIDDENS

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Title Vice President  
Human Resources  
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QUANEX CORPORATION  
DEFERRED COMPENSATION PLAN

AMENDED AND RESTATED

JUNE 1, 1999

QUANEX CORPORATION  
DEFERRED COMPENSATION PLAN

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QUANEX CORPORATION  
DEFERRED COMPENSATION PLAN

WHEREAS, Quanex Corporation originally established the Quanex Deferred Compensation Plan (the "Plan") effective October 1, 1981, which provides a mechanism by which certain highly compensated management personnel may defer their compensation under the Quanex Corporation Executive Incentive Compensation Plan prior to such compensation being earned and directors may defer their director's fees prior to their being earned;

WHEREAS, Quanex Corporation amended and restated the Plan effective October 12, 1995;

WHEREAS, Quanex Corporation desires to amend and restate the Plan effective June 1, 1999;

NOW, THEREFORE, Quanex Corporation amends and restates the Plan as follows:

ARTICLE I  
DEFINITIONS

1.1 "ACCOUNT" means a Participant's account in the Deferred Compensation Ledger maintained by the Committee which reflects the benefits a Participant is entitled to under the Plan.

1.2 "BENEFICIARY" means a person or entity designated by the Participant under the terms of the Plan to receive any amounts distributed under the Plan upon the death of the Participant.

1.3 "BOARD" means the Board of Directors of Quanex Corporation.

1.4 "CHANGE OF CONTROL" means the occurrence of one or more of the following events after June 1, 1999:

(a) the acquisition by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Covered Person") of beneficial ownership (within the meaning of rule 13d-3 promulgated under the Exchange Act) of 20 percent or more of either (i) the then outstanding shares of the common stock of Quanex (the "Outstanding Quanex Common Stock"), or (ii) the combined voting power of the then outstanding voting securities of Quanex entitled to vote generally in the election of directors (the "Outstanding Quanex Voting Securities"); provided, however, that for purposes of this subsection (a) of this Section, the following acquisitions shall not constitute a Change of Control of Quanex: (i) any acquisition directly from Quanex, (ii) any acquisition by Quanex, (iii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by Quanex or any entity controlled by Quanex, or (iv) any acquisition by any corporation pursuant to a transaction which complies with clauses (i), (ii) and (iii) of subsection (c) of this Section; or

(b) individuals who, as of June 1, 1999, constitute the Board (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board; provided, however, that any individual becoming a director subsequent to June 1, 1999 whose election, or nomination for election by Quanex's stockholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board shall be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial assumption of office occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents by or on behalf of a Covered Person other than the Board; or

(c) the consummation of (xx) a reorganization, merger or consolidation or sale of Quanex or (yy) a disposition of all or substantially all of the assets of the Company (a "Business Combination"), in each case, unless, following such Business Combination, (i) all or substantially all of the individuals and entities who were the beneficial owners, respectively, of the Outstanding Quanex Common Stock and Outstanding Quanex Voting Securities immediately prior to such Business Combination beneficially own, direct or indirectly, more than 80 percent of, respectively, the then outstanding shares of common stock and the combined voting power of the then outstanding voting securities entitled to vote generally in the election of directors, as the case may be, of the corporation resulting from such Business Combination (including, without limitation, a corporation which as a result of such transaction owns Quanex or all or substantially all of Quanex's assets either directly or through one or more subsidiaries) in substantially the same proportions as their ownership immediately prior to such Business Combination of the Outstanding Quanex Common Stock and Outstanding Quanex Voting Securities, as the case may be, (ii) no Covered Person (excluding any employee benefit plan (or related trust) of Quanex or such corporation resulting from such Business Combination) beneficially owns, directly or indirectly, 20 percent or more of, respectively, the then outstanding shares of common stock of the corporation resulting from such Business Combination or the combined voting power of the then outstanding voting securities of such corporation, except to the extent that such ownership existed prior to the Business Combination, and (iii) at least a majority of the members of the board of directors of the corporation resulting from such Business Combination, were members of the Incumbent Board at the time of the execution of the initial agreement, or of the action of the Board of Directors, providing for such Business Combination; or

(d) the approval by the stockholders of Quanex of a complete liquidation or dissolution of Quanex.

1.5 "CHANGE OF CONTROL VALUE" means the amount determined in clause (i), (ii) or (iii), whichever is applicable, as follows: (i) the per share price offered to stockholders of Quanex in the merger, consolidation, reorganization, sale of assets or dissolution transaction that constitutes a Change of Control, (ii) the price per share offered to stockholders of Quanex in any tender offer or exchange offer that constitutes a Change of Control, or (iii) if a Change of Control occurs other than a Change of Control specified in clause (i) or (ii), the fair market value per share of the Common Stock on the date of the Change of Control, based on the closing quotation as described in Section 4.2, on that day. If the consideration offered to stockholders of the Company in any transaction described above consists of anything other than cash, the Committee shall determine the cash equivalent of the fair market value of the portion of the consideration offered that is other than cash.

1.6 "CODE" means the Internal Revenue Code of 1986, as amended from time to time.

1.7 "COMMITTEE" means the persons who are from time to time serving as members of the committee administering the Plan.

1.8 "COMMON STOCK" means Quanex's common stock, \$.50 par value (or such other par value as may be designated by the vote of Quanex stockholders or such other equity securities of Quanex into which such common stock may be converted, reclassified or exchanged).

1.9 "COMPANY" means Quanex and any Subsidiary adopting the Plan.

1.10 "COMPANY MATCH" means the 20 percent match which the Company makes to the amount deferred in Common Stock during a Plan Year by a Participant under the Plan for three or more Plan Years.

1.11 "DEFERRED COMPENSATION LEDGER" means the ledger maintained by the Committee for each Participant which reflects the amount of compensation deferred for the Participant under the Plan, the Company match, and the amount of income credited on each of these amounts.

1.12 "DIRECTOR" means any person serving as a member of the Board of Directors.

1.13 "DIRECTOR FEES" means any amount paid to a Director for services in such capacity.

1.14 "DISABILITY" means a mental or physical disability that in the opinion of a physician selected by the Committee, shall prevent the Participant from engaging in any substantial gainful activity, can be expected to result in death or has lasted or can be expected to last for a

continuous period of not less than twelve months, and which: (a) was not contracted, suffered or incurred while the Participant was engaged in or did not result from having engaged in, a felonious criminal enterprise; (b) did not result from alcoholism or addiction to narcotics; and (c) did not result from an injury incurred while a member of the Armed Forces of the United States for which the Participant received a military pension.

1.15 "INCENTIVE BONUS" means a bonus awarded or to be awarded to the Participant under the Quanex Corporation Executive Incentive Compensation Plan.

1.16 "NORMAL RETIREMENT DATE" means the first day of the month that coincides with or next follows the date on which the Participant or former Participant attains age 65.

1.17 "NYSE" means the New York Stock Exchange.

1.18 "PARTICIPANT" means an employee or director of a Company who is participating in the Plan.

1.19 "PLAN" means the Quanex Corporation Deferred Compensation Plan set forth in this document, as amended from time to time.

1.20 "PLAN YEAR" means a one-year period that coincides with the fiscal year of Quanex, which begins on the first day of November of each calendar year and ends on October 31 of the next ensuing calendar year.

1.21 "QUANEX" means the Quanex Corporation, a Delaware corporation, the sponsor of the Plan.

1.22 "RABBI TRUST" means the Quanex Corporation Deferred Compensation Trust, which agreement was entered into between NBD Bank and Quanex.

1.23 "RETIREMENT" means the retirement of a Participant from any Company covered by the Plan under the terms of the Retirement Plan.

1.24 "RETIREMENT PLAN" means the Quanex Corporation Salaried Employees' Pension Plan, or if the Company does not maintain that plan, the defined contribution plan maintained by the Company that is intended to satisfy the requirements of section 401(a) of the Code.

1.25 "SECURITIES ACT" means the Securities Exchange Act of 1934, as amended from time to time.

1.26 "SUBSIDIARY" means any wholly owned subsidiary of Quanex.

1.27 "TERM OF DEFERRAL" means the period of deferral chosen by the Participant under the election procedure established in Section 3.1 or by the Committee which pertains to that portion of the Incentive Bonus or Director Fees for each given Plan Year and its accumulated income accrued that has been deferred under an election made prior to the commencement of the period during which it is earned.

1.28 "VOTING SECURITIES" means any security which ordinarily possesses the power to vote in the election of the Board without the happening of any precondition or contingency.

ARTICLE II  
ELIGIBILITY

Initially, all participants in the Quanex Corporation Executive Incentive Compensation Plan and all Directors will be eligible to participate in the Plan. However, the Committee retains the right to establish such additional eligibility requirements for participation in the Plan as it may determine are appropriate or necessary from time to time and has the right to determine, in its sole discretion, that any one or more persons who meet the eligibility requirements will not be eligible to participate for one or more Plan Years beginning after the date they are notified of this decision by the Committee.

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## ARTICLE III

## DEFERRALS AND COMPANY CONTRIBUTIONS

3.1 DEFERRAL ELECTION. A Participant may elect during the election period established by the Committee prior to the beginning of any Plan Year:

(1) the percentage of his Incentive Bonus earned during the ensuing Plan Year which is to be paid as soon as conveniently possible after the Plan Year and the percentage which is to be deferred under the Plan;

(2) the percentage of his Director Fees earned during the ensuing Plan Year which is to be paid during such year and the percentage which is to be deferred under the Plan;

(3) the percentage of the amount deferred, if any, to be deferred in the form of Common Stock and the percentage, if any, to be deferred in the form of cash;

(4) the length of the period of deferral, if any amount has been elected to be deferred, whether in cash or in Common Stock, which deferral shall be for a period of years, to a date certain, to termination of employment with the Company or to his Retirement; and

(5) the form of payment of the amount that has been elected to be deferred -- a lump sum, or quarterly or annual installment payments of the principal amount plus the interest accrued after the distribution date, or last installment paid, if later, in the case of a deferral in the form of cash or of the total shares of Common Stock credited to him as of the date of distribution plus any other shares, cash or other property credited as dividends or other rights on those shares after the distribution date or last installment distributed, if later, in the case of a deferral in the form of Common Stock, over no less than three nor more than 20 years.

If a Participant elects a deferral period to Retirement, he shall also specify whether the deferral period shall end at the date of his termination of employment with the Company or at his Normal Retirement Date, in the event of termination other than as a result of death, Disability

or Retirement. If a Participant elects a deferral period of a number of years or to a date certain, the deferral period shall end upon the Participant's Retirement, if earlier.

The deferrals in the form of Common Stock elected by Participants to be allocated to their Accounts in any Plan Year must not exceed one percent of the shares of Common Stock outstanding on the first day of the Plan Year. In the event this maximum would be exceeded, each Participant who elected to defer in the form of Common Stock shall have his election reduced on a pro rata basis as compared to all Participants who elected to defer in the form of Common Stock until those deferrals in the aggregate for that Plan Year equal the maximum and the portion of his Incentive Bonus which would have been deferred in the form of Common Stock shall instead be distributed to the Participant as provided in the Quanex Corporation Executive Incentive Compensation Plan.

Once an election has been made it becomes irrevocable for that Plan Year, except that the Participant may change his election of the form of payment he previously elected under Section 3.1(5) during a 30-day period ending one year prior to the end of the deferral period. In the event a Participant originally elected a deferral period of a number of years or until a date certain and, as a result of the Participant's election to take Retirement, the Participant will retire before the end of the elected deferral period, the Participant may elect to change the form of payment during a 30- day period ending one year prior to the Retirement date chosen by the Participant by written notice to the Company. In the event a Participant changes his election, if the deferral period terminates early for any reason, which is beyond the control of the Participant, such as involuntary termination of employment, death or Disability, then the distribution or the first installment, whichever is applicable, shall not be made until one year after the election was changed; however, if the deferral period terminates early for any reason which is within the control of the Participant,

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such as Retirement or voluntary termination of employment, then the change of election will be ineffective. If for any reason the deferral period does not end one year after the end of such 30-day period because of a postponement of Retirement or otherwise, the change of election shall remain in effect and no further changes of election shall be permitted.

The election to participate in the Plan for a given Plan Year will be effective only upon receipt by the Committee of the Participant's election on such form as will be determined by the Committee from time to time. If the Participant does not exercise his right to defer, subject to Section 3.3 below, the Participant will be deemed to have elected not to defer any part of his Incentive Bonus or Director Fees for that Plan Year and all of his Incentive Bonuses and Director Fees will be paid in cash. If the percentage of the Incentive Bonus and Director Fees elected to be deferred in Common Stock results in a fractional share, it shall be reduced to the next lowest full share and the fractional share shall be paid or deferred, as the case may be, in cash.

3.2 COMPANY MATCH. The Company will credit to the Account of each Participant who has a portion of his Incentive Bonus or Director Fees deferred under the Plan in the form of Common Stock for a period of three full years or more additional shares of Common Stock equal to 20 percent of the amount which is deferred in the form of Common Stock, rounded to the next highest number of full shares.

3.3 MANDATORY DEFERRAL. If a Participant becomes entitled to a cash payment of part or all of an Incentive Bonus because the Participant did not elect to defer all of the Incentive Bonus but the Company determines that section 162(m) of the Code may not allow the Company to take a deduction for part or all of the Incentive Bonus, then, unless a Change of Control has occurred after June 1, 1999, the payment of the Incentive Bonus will be delayed until December 1st following the end of the Plan Year in which it occurred. Then on December 1st, if the Company's

deduction is determined by the Company not to be affected, the Incentive Bonus in total will be paid immediately. However, if the Company determines that some portion of the Incentive Bonus is affected, then only that portion of the Incentive Bonus which is deductible by the Company shall be paid on December 1st and the remaining portion of the Incentive Bonus will be delayed to the first day of the first complete month of the second Plan Year, at which time it will be paid. The Committee may waive the mandatory deferral required by this Section 3.3 with respect to a Participant who is not a member of the Committee but such waiver shall only be made on an individual basis and at the time the Incentive Bonus is determined and awarded.

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## ARTICLE IV

## ACCOUNT

4.1 ESTABLISHING A PARTICIPANT'S ACCOUNT. The Committee will establish an Account for each Participant in a special Deferred Compensation Ledger which will be maintained by the Company. The Account will reflect the amount of the Company's obligation to the Participant at any given time.

4.2 CREDIT OF THE PARTICIPANT'S DEFERRAL AND THE COMPANY'S MATCH. Upon completion of the Plan Year or quarter, as applicable, the Committee will determine, as soon as administratively practicable, the amount of a Participant's Incentive Bonus or Director Fees that has been deferred for that Plan Year or quarter, as applicable, and the amount of the Company Match, if any, and will credit that or those amounts to the Participant's Account as of the end of the Plan Year or quarter, as applicable, during which the Incentive Bonus or Director Fees were earned. If the Participant elected his deferral to be in the form of Common Stock, the number of shares credited to his Account as Common Stock shall be the number of full shares of Common Stock that could have been purchased with the dollar amount deferred, without taking into account any brokerage fees, taxes or other expenses which might be incurred in such a transaction, based upon the closing quotation on the NYSE, or if not traded on the NYSE, the principal market in which the Common Stock is traded on the date the amount would have been paid had it not been deferred pursuant to Article III, and any additional fractional amount shall be credited to the Participant's Account in the form of cash.

4.3 CREDITING OF DIVIDENDS, DISTRIBUTIONS AND INTEREST. When dividends are declared and paid, or other distributions, whether stock, property, cash, rights or other, are made with

respect to the Common Stock, those dividends and other distributions shall be accrued in a Participant's Account based upon the shares of Common Stock credited to his Account. The dividends or other distributions in the form of shares of Common Stock shall be credited to the Account as additional shares of Common Stock. The dividends or other distributions or rights in any other form shall be credited to the Participant's Account in the form of cash. For this purpose, all dividends and distributions not in the form of shares of Common Stock or cash shall be valued at the fair market value as determined by a resolution duly adopted by the Committee. Interest will be accrued on that portion of a Participant's Account held in the form of cash at the rate established by Section 4.4.

4.4 INTEREST RATE. Interest will be accrued on the last day of each calendar month on each portion of a Participant's Account held in the form of cash (whether resulting from a cash deferral, cash dividends or other cash distributions on Common Stock or the conversion of a Common Stock credit in his Account to cash) from the later of (a) the time it is credited to his Account or (b) the last previous calendar month end at a rate equal to (x) the rate of interest announced by Chase Manhattan Bank, N.A., or its successor, if applicable as its prime rate of interest on the last business day of the calendar quarter preceding the calendar quarter in which the month falls divided by (y) four. Interest so accrued on the last day of each calendar month shall be credited as cash to the Participant's Account and shall thereafter accrue interest. Interest will continue to be credited on the cash balance in the Participant's Account until the entire cash balance has been distributed.

4.5 COMMON STOCK CONVERSION ELECTION. At any time during a period of three years prior to the earliest time a Participant could retire under the Retirement Plan and ending on the Participant's Normal Retirement Date, the Participant may elect a Retirement date under the

Retirement Plan and may elect to have all or a portion of his shares of Common Stock in his Account converted to cash. In that event, all such shares of Common Stock shall be converted on the date notice is received by the Company based upon the closing quotation as described in Section 4.2, on that day, unless the Participant has specified no more than five different dates after the date of the notice on which the Participant desires all or a portion of the shares of Common Stock to be converted and the percentage of shares to be converted on each date. If the Participant has specified dates for and the percentage of shares to be converted, then the designated percentage of shares of Common Stock to be converted on each date shall be converted on the specified date based on the closing quotation as described in Section 4.2 on such specified dates.

At any time that is at least five years after Common Stock is credited to his Account pursuant to Section 4.2, a Participant may elect to have such Common Stock converted to cash and credited to his Account. In that event, all such shares of Common Stock specified by the Participant in a written notice to the Company which have been credited to the Participant's Account for at least five years prior to the giving of such notice shall be converted on the date notice is received by the Company based upon the closing quotation as described in Section 4.2, on that day.

#### 4.6 CONVERSION AND CASH-OUT UPON A CHANGE OF CONTROL.

Notwithstanding any other provision of the Plan, immediately upon the occurrence of a Change of Control, all shares of Common Stock credited to a current or former Participant's Account shall be converted to cash based on the Change of Control Value of such shares of Common Stock. Within five days after the date on which the Change of Control occurs, all current and former Participants shall be paid in cash lump sum payments the balances credited to their Accounts.

## ARTICLE V

## VESTING AND EVENTS CAUSING FORFEITURE

5.1 VESTING. All deferrals of the Incentive Bonus and Director Fees and all income accrued on the deferrals will be 100 percent vested except for the events of forfeiture described in Sections 5.3 and 5.4. All Company matching accruals and all income accrued on those matching accruals will be 100 percent vested except for the events of forfeiture described in Section 5.2, 5.3 and 5.4.

5.2 FORFEITURE OF COMPANY MATCH BECAUSE OF EARLY DISTRIBUTION. If, but for the provisions of this Section 5.2, a Participant would receive a benefit from the Plan for any reason, other than death, disability or Retirement, in respect of shares of Common Stock credited to the Participant's account pursuant to Section 4.2 as a result of the Company matching accrual of 20 percent provided for in Section 3.2 within three years after such shares were so credited, or if the Participant ceases to be an employee with respect to a matching accrual resulting from deferral of an Incentive Bonus, or a director with respect to a matching accrual resulting from deferral of Director Fees within three years after such shares are so credited, such matching accruals of shares of Common Stock and any dividends or other property or rights accumulated because of those shares of Common Stock shall be immediately forfeited.

5.3 FORFEITURE FOR CAUSE. If the Committee finds, after full consideration of the facts presented on behalf of both the Company and a former Participant, that the Participant was discharged by the Company for fraud, embezzlement, theft, commission of a felony, proven dishonesty in the course of his employment by the Company which damaged the Company, or for disclosing trade secrets of the Company, the entire amount credited to his Account, exclusive of an



amount equal to the sum of the total deferrals of the Participant, will be forfeited. The decision of the Committee as to the cause of a former Participant's discharge and the damage done to the Company will be final. No decision of the Committee will affect the finality of the discharge of the Participant by the Company in any manner.

5.4 FORFEITURE FOR COMPETITION. If at the time a distribution is being made or is to be made to a Participant or former Participant, the Committee finds after full consideration of the facts presented on behalf of the Company and the Participant or former Participant, that the Participant or former Participant at any time within two years from his termination of employment from the Company, and without written consent of the Company, directly or indirectly owns, operates, manages, controls or participates in the ownership, management, operation or control of or is employed by, or is paid as a consultant or other independent contractor by a business which competes or at any time did compete with the Company by which he was formerly employed in a trade area served by the Company at the time distributions are being made or to be made and in which the Participant or former Participant had represented the Company while employed by it; and, if the Participant or former Participant continues to be so engaged 60 days after written notice has been given to him, the Committee will forfeit all amounts otherwise due the Participant or former Participant, exclusive of an amount equal to the sum of the total deferrals of the Participant or former Participant.

5.5 FULL VESTING IN THE EVENT OF A CHANGE OF CONTROL. The forfeitures created by sections 5.2, 5.3 or 5.4 shall not apply with respect to any amounts credited to the Accounts of current or former Participants after the occurrence of a Change of Control.

ARTICLE VI  
DISTRIBUTIONS

6.1 FORM OF DISTRIBUTIONS OR WITHDRAWALS. Upon a distribution or withdrawal, at the option of Quanex, the number of shares of Common Stock credited to the Participant in the Deferred Compensation Ledger, if any, required to be distributed shall be distributed in kind or in cash, whether the distribution or withdrawal is in a lump sum or in installments. If distributed in cash, the amount per share of Common Stock which would otherwise be distributed in kind shall equal the closing quotation for the Common Stock on the NYSE (or if not traded on the NYSE, the principal market in which the Common Stock is traded) on the third business day prior to the date of distribution. If the distribution is in installments, all dividends and other property or rights accumulating on the shares still undistributed will be credited as provided in Section 4.3 and distributed with the next installment. If there are periodic installments to be made of the portion, if any, deferred as cash, income shall accumulate on that portion of the Account as described in Section 4.6 until the balance credited to the cash portion of the Participant's Account has been distributed. In that event, income accumulating on the cash portion of the Account shall be distributed with the next installment to be distributed.

6.2 DEATH. Upon the death of a Participant prior to the expiration of the Term of Deferral, the Participant's Beneficiary or Beneficiaries will receive in Common Stock or cash as required by Section 6.1, the balance then credited to the Participant's Account in the Deferred Compensation Ledger. The lump sum distribution or the first installment of the periodic distribution will be made 90 days after the Participant's death.

Each Participant, upon making his initial deferral election, will file with the Committee a designation of one or more Beneficiaries to whom distributions otherwise due the Participant will be made in the event of his death prior to the complete distribution of the amount credited to his Account in the Deferred Compensation Ledger. The designation will be effective upon receipt by the Committee of a properly executed form which the Committee has approved for that purpose. The Participant may from time to time revoke or change any designation of Beneficiary by filing another approved Beneficiary designation form with the Committee. If there is no valid designation of Beneficiary on file with the Committee at the time of the Participant's death, or if all of the Beneficiaries designated in the last Beneficiary designation have predeceased the Participant or otherwise ceased to exist, the Beneficiary will be the Participant's spouse, if the spouse survives the Participant, or otherwise the Participant's estate. A Beneficiary must survive the Participant by 60 days in order to be considered to be living on the date of the Participant's death. If any Beneficiary survives the Participant but dies or otherwise ceases to exist before receiving all amounts due the Beneficiary from the Participant's Account, the balance of the amount which would have been paid to that Beneficiary will, unless the Participant's designation provides otherwise, be distributed to the individual deceased Beneficiary's estate or to the Participant's estate in the case of a Beneficiary which is not an individual. Any Beneficiary designation which designates any person or entity other than the Participant's spouse must be consented to in writing in a form acceptable to the Committee in order to be effective.

6.3 DISABILITY. Upon the Disability of a Participant prior to the expiration of the Term of Deferral, the Participant will receive in Common Stock or cash as required by Section 6.1, the balance then credited to the Participant's Account. The lump sum distribution or the first installment of the periodic distribution will be made 90 days after the Participant becomes disabled.

6.4 EXPIRATION OF TERM OF DEFERRAL. Upon the expiration of the Term of Deferral, the Participant shall receive in Common Stock or cash as required by Section 6.1, the balance credited to the Participant's Account. The lump sum distribution or the first installment of the periodic distribution will be made 90 days after the expiration of the Term of Deferral without regard to whether the Participant is still employed by the Company or not.

6.5 HARDSHIP WITHDRAWALS. Any Participant who is in the employ of a Company and is not entitled to a distribution from the Plan may request a hardship withdrawal. No hardship withdrawal can exceed the lesser of the amount credited to the Participant's Account or the amount reasonably needed to satisfy the emergency need. Whether a hardship exists and the amount reasonably needed to satisfy the emergency need will be determined by the Committee based upon the evidence presented by the Participant and the rules established in this Section. If a hardship withdrawal is approved by the Committee it will be made in Common Stock or cash as required in Section 6.1 within ten days of the Committee's determination. A hardship for this purpose is a severe financial hardship to the Participant resulting from a sudden and unexpected illness or accident of the Participant or of a dependent (as defined in section 152(a) of the Code) of the Participant, loss of the Participant's property due to casualty, or any similar extraordinary and unforeseeable circumstance arising as a result of events beyond the control of the Participant. The circumstances that will constitute a hardship will depend upon the facts of each case, but, in any case, payment may not be made to the extent that the hardship is or may be relieved: (a) through reimbursement or compensation by insurance or otherwise, (b) by liquidation of the Participant's assets, to the extent the liquidation of such assets will not itself cause severe financial hardship, or (c) by cessation of deferrals under the Plan. Such foreseeable needs for funds as the need to send a Participant's child to college or the desire to purchase a home will not be considered to be a hardship.

#### 6.6 PAYMENT RESTRICTIONS ON ANY PORTION OF A BENEFIT

DETERMINED NOT TO BE DEDUCTIBLE. Except for hardship withdrawals under Section 6.5, if a Participant has a benefit that is due during a Plan Year and the Committee determines that section 162(m) of the Code could affect the Company's deduction on the amount paid, the distribution of his benefit will be delayed until December 1 following the end of the Plan Year. Then on December 1 if the Company's deduction is determined by the Committee not to be affected, the benefit in total will be distributed immediately; however, if the Committee determines that some portion of the benefit is affected, then only that portion of the benefit which is deductible by the Company shall be distributed on December 1st and the distribution of the remaining portion of the benefit will be delayed to the first day of the first complete month of the Plan Year or Years on which a portion or all of the remaining distribution can be made and deducted by the Company on its federal income tax return. The Committee may waive the mandatory deferral required by this Section 6.6 with respect to a Participant who is not a member of the Committee, but such waiver shall only be made on an individual basis and at the time the distribution is to be made.

#### 6.7 RESPONSIBILITY FOR DISTRIBUTIONS AND WITHHOLDING OF TAXES.

The Committee will furnish information to the Company last employing the Participant, concerning the amount and form of distribution to any Participant entitled to a distribution so that the Company may make or cause the Rabbi Trust to make the distribution required. It will also calculate the deductions from the amount of the benefit paid under the Plan for any taxes required to be withheld by federal, state or local government and will cause them to be withheld. If a Participant has deferred compensation under the Plan while in the service of more than one Company, each Company for which the Participant was working will reimburse the disbursing agent for the amount attributable to compensation deferred while the Participant was in the service of that Company if it has not already provided that funding to the disbursing agent.

## ARTICLE VII

## ADMINISTRATION

7.1 COMMITTEE APPOINTMENT. The Committee will be appointed by the Board. The initial Committee members will be Compensation Committee of the Board. Each Committee member will serve until his or her resignation or removal. The Board will have the sole discretion to remove any one or more Committee members and appoint one or more replacement or additional Committee members from time to time.

7.2 COMMITTEE ORGANIZATION AND VOTING. The Committee will select from among its members a chairman who will preside at all of its meetings and will elect a secretary without regard to whether that person is a member of the Committee. The secretary will keep all records, documents and data pertaining to the Committee's supervision and administration of the Plan. A majority of the members of the Committee will constitute a quorum for the transaction of business and the vote of a majority of the members present at any meeting will decide any question brought before the meeting. In addition, the Committee may decide any question by vote, taken without a meeting, of a majority of its members. If a member of the Committee is ever appointed who is or becomes a Participant, that Committee member will not vote or act on any matter relating solely to himself.

7.3 POWERS OF THE COMMITTEE. The Committee will have the exclusive responsibility for the general administration of the Plan according to the terms and provisions of the Plan and will have all powers necessary to accomplish those purposes, including but not by way of limitation the right, power and authority:

(a) to make rules and regulations for the administration of the Plan;

(b) to construe all terms, provisions, conditions and limitations of the Plan;

(c) to correct any defect, supply any omission or reconcile any inconsistency that may appear in the Plan in the manner and to the extent it deems expedient to carry the Plan into effect for the greatest benefit of all parties at interest;

(d) to designate the persons eligible to become Participants and to establish the maximum and minimum amounts that may be elected to be deferred;

(e) to determine all controversies relating to the administration of the Plan, including but not limited to:

(1) differences of opinion arising between the Company and a Participant except when the difference of opinion relates to the entitlement to, the amount of or the method or timing of a distribution of a benefit affected by a Change of Control, in which event it shall be decided by judicial action; and

(2) any question it deems advisable to determine in order to promote the uniform administration of the Plan for the benefit of all parties at interest; and

(f) to delegate by written notice those clerical and recordation duties of the Committee, as it deems necessary or advisable for the proper and efficient administration of the Plan.

7.4 COMMITTEE DISCRETION. The Committee in exercising any power or authority granted under the Plan or in making any determination under the Plan shall perform or refrain from performing those acts using its sole discretion and judgment. Any decision made by the Committee or any refraining to act or any act taken by the Committee in good faith shall be final and binding on all parties. The Committee's decision shall never be subject to de novo review. Notwithstanding the foregoing, the Committee's decision, refraining to act or acting is to be subject to judicial review for those incidents occurring during the Plan Year in which a Change of Control occurs and during the next three succeeding Plan Years.

7.5 ANNUAL STATEMENTS. The Committee will cause each Participant to receive an annual statement as soon as administratively possible after the conclusion of each Plan Year containing the amounts deferred, the Company match, if any, and the income accrued on the deferred and matched amounts.

7.6 REIMBURSEMENT OF EXPENSES. The Committee will serve without compensation for their services but will be reimbursed by Quanex for all expenses properly and actually incurred in the performance of their duties under the Plan.



## ARTICLE VIII

## ADOPTION BY SUBSIDIARIES

8.1 PROCEDURE FOR AND STATUS AFTER ADOPTION. Any Subsidiary may, with the approval of the Committee, adopt the Plan by appropriate action of its board. The terms of the Plan will apply separately to each Subsidiary adopting the Plan and its Participants in the same manner as is expressly provided for Quanex and its Participants except that the powers of the Board and the Committee under the Plan will be exercised by the Board alone. Quanex and each Subsidiary adopting the Plan will bear the cost of providing plan benefits for its own Participants. It is intended that the obligation of Quanex and each Subsidiary with respect to its Participants will be the sole obligation of the Company that is employing the Participant and will not bind any other Company.

8.2 TERMINATION OF PARTICIPATION BY ADOPTING SUBSIDIARY. Any Subsidiary adopting the Plan may, by appropriate action of its board of directors, terminate its participation in the Plan. The Committee may, in its discretion, also terminate a Subsidiary's participation in the Plan at any time. The termination of the participation in the Plan by a Subsidiary will not, however, affect the rights of any Participant who is working or has worked for the Subsidiary as to amounts or shares of Common Stock previously standing to his credit in his Account or reduce the income accrued on amounts deferred by him or matched by the Company and credited to his Account whether in cash or in shares of Common Stock, prior to the distribution of the benefit to the Participant without his consent.

ARTICLE IX  
AMENDMENT AND/OR TERMINATION

9.1 AMENDMENT OR TERMINATION OF THE PLAN. The Board may amend or terminate the Plan at any time by an instrument in writing without the consent of any adopting Company.

9.2 NO RETROACTIVE EFFECT ON AWARDED BENEFITS. No amendment will affect the rights of any Participant to the amounts, whether in cash or shares of Common Stock, then standing to his credit in his Account, to change the method of calculating the income already accrued or to accrue in the future on amounts already deferred by him or matched by the Company prior to the date of the amendment or to change a Participant's right under any provision relating to a Change of Control after a Change of Control has occurred, without the Participant's consent. However, the Board shall retain the right at any time to change in any manner the method of calculating the match by the Company and the income to accrue on all amounts to be deferred in the future by a Participant and/or to be matched in the future by the Company after the date of the amendment if it has been announced to the Participants.

9.3 EFFECT OF TERMINATION. If the Plan is terminated, all amounts, whether in cash or in shares of Common Stock, deferred by Participants and matched by the Company will continue to be held under the terms of the Plan until all amounts have been distributed according to the elections made by the Participants or the directives made by the Committee prior to the deferrals. The forfeiture provisions of Sections 5.2, 5.3 and 5.4 and the restriction set out in Section 6.6 would continue to apply throughout the period after the termination of the Plan but prior to the completed distribution of all benefits.

## ARTICLE X

## FUNDING

10.1 PAYMENTS UNDER THIS AGREEMENT ARE THE OBLIGATION OF THE COMPANY. The Company will distribute the benefits due the Participants under the Plan; however, should it fail to do so when a benefit is due and the funding trust contemplated by Section 10.2 exists, the benefit will be distributed by the trustee of that funding trust. In any event, if the trust fails to distribute a benefit for any reason, the Company still remains liable for all benefits provided by the Plan.

10.2 AGREEMENT MAY BE FUNDED THROUGH RABBI TRUST. It is specifically recognized by both the Company and the Participants that the Company may, but is not required to transfer any funds, shares or Common Stock or other assets that it finds desirable to a trust established to accumulate assets sufficient to fund the obligations of all of the Companies signatory to the Plan. However, under all circumstances, the Participants will have no rights to any of those assets; and likewise, under all circumstances, the rights of the Participants to the assets held in the trust will be no greater than the rights expressed in this agreement. Nothing contained in the trust agreement which creates the funding trust will constitute a guarantee by any Company that assets of the Company transferred to the trust will be sufficient to fund all benefits under the Plan or would place the Participant in a secured position ahead of general creditors should the Company become insolvent or bankrupt. Any trust agreement prepared to fund the Company's obligations under this agreement must specifically set out these principles so it is clear in that trust agreement that the Participants in the Plan are only unsecured general creditors of the Company in relation to their benefits under the Plan.

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10.3 REVERSION OF EXCESS ASSETS. Any adopting Company may, at any time, request the actuary, who last performed the annual actuarial valuation of the Quanex defined benefit Retirement plan, to determine the present Account balance, assuming the accrual rate for income not to be reduced (whether it actually is or not), as of the month end coincident with or next preceding the request, of all Participants and Beneficiaries of deceased Participants for which all Companies are or will be obligated to make benefit distributions under the Plan. If the fair market value of the assets held in the trust, as determined by the Trustee as of that same date, exceeds the total of the Account balances of all Participants and Beneficiaries by 25 percent, any Company may direct the trustee to return to each Company its proportionate part of the assets which are in excess of 125 percent of the Account balances. Each Company's share of the excess assets will be the Participants' Accounts accrued while in the employ of that Company as compared to the total of the Account balances accrued by all Participants under the Plan times the excess assets. If there has been a Change of Control, for the purpose of determining if there are excess funds, all contributions made prior to the Change of Control will be subtracted from the fair market value of the assets held in the trust as of the determination date but before the determination is made.

10.4 PARTICIPANTS MUST RELY ONLY ON GENERAL CREDIT OF THE COMPANY. It is also specifically recognized by both the Company and the Participants that the Plan is only a general corporate commitment and that each Participant must rely upon the general credit of the Company for the fulfillment of its obligations under the Plan. Under all circumstances the rights of Participants to any asset held by the Company will be no greater than the rights expressed in this agreement. Nothing contained in this agreement will constitute a guarantee by the Company that the assets of the Company will be sufficient to distribute any benefits under the Plan or would place the Participant in a secured position ahead of general creditors of the Company. Though the

Company may establish or become a signatory to a Rabbi Trust, as indicated in Section 10.1, to accumulate assets to fulfill its obligations, the Plan and any such trust will not create any lien, claim, encumbrance, right, title or other interest of any kind in any Participant in any asset held by the Company, contributed to any such trust or otherwise designated to be used in fulfillment of any of its obligations created in this agreement. No specific assets of the Company have been or will be set aside, or will in any way be transferred to the trust or will be pledged in any way for the performance of the Company's obligations under the Plan which would remove such assets from being subject to the general creditors of the Company.

ARTICLE XI  
MISCELLANEOUS

11.1 LIMITATION OF RIGHTS. Nothing in the Plan will be construed:

- (a) to give any employee of any Company any right to be designated a Participant in the Plan;
- (b) to give a Participant any right with respect to the compensation deferred, the Company match or the income accrued and credited in the Deferred Compensation Ledger except in accordance with the terms of the Plan;
- (c) to limit in any way the right of the Company to terminate a Participant's employment with the Company at any time;
- (d) to evidence any agreement or understanding, expressed or implied, that the Company will employ a Participant in any particular position or for any particular remuneration; or
- (e) to give a Participant or any other person claiming through him any interest or right under the Plan other than that of any unsecured general creditor of the Company.

11.2 DISTRIBUTIONS TO INCOMPETENTS OR MINORS. Should a Participant become incompetent or should a Participant designate a Beneficiary who is a minor or incompetent, the Committee is authorized to distribute the benefit due to the parent of the minor or to the guardian of the minor or incompetent or directly to the minor or to apply those assets for the benefit of the minor or incompetent in any manner the Committee determines in its sole discretion.

11.3 NONALIENATION OF BENEFITS. No right or benefit provided in the Plan will be transferable by the Participant except, upon his death, to a named Beneficiary as provided in the Plan. No right or benefit under the Plan will be subject to anticipation, alienation, sale, assignment, pledge, encumbrance or charge, and any attempt to anticipate, alienate, sell, assign, pledge, encumber, or charge the same will be void. No right or benefit under the Plan will in any manner

be liable for or subject to any debts, contracts, liabilities or torts of the person entitled to such benefits. If any Participant or any Beneficiary becomes bankrupt or attempts to anticipate, alienate, sell, assign, pledge, encumber or charge any right or benefit under the Plan, that right or benefit will, in the discretion of the Committee, cease. In that event, the Committee may have the Company hold or apply the right or benefit or any part of it to the benefit of the Participant or Beneficiary, his or her spouse, children or other dependents or any of them in any manner and in any proportion the Committee believes to be proper in its sole and absolute discretion, but is not required to do so.

11.4 EXPENSES INCURRED IN ENFORCING THE PLAN. The Company will, in addition, pay a Participant for all legal fees and expenses incurred by him in contesting or disputing his termination or in seeking to obtain or enforce any benefit provided by the Plan if the termination occurs in the Plan Year in which a Change of Control occurs or during the next three succeeding Plan Years following the Plan Year in which a Change of Control occurs except to the extent that the payment of those fees or expenses are restricted under Section 6.6.

11.5 RELIANCE UPON INFORMATION. The Committee will not be liable for any decision or action taken or not taken in good faith in connection with the administration of the Plan. Without limiting the generality of the foregoing, any decision or action taken or not taken by the Committee when it relies upon information supplied it by any officer of the Company, the Company's legal counsel, the Company's independent accountants or other advisors in connection with the administration of the Plan will be deemed to have been taken in good faith.

11.6 SEVERABILITY. If any term, provision, covenant or condition of the Plan is held to be invalid, void or otherwise unenforceable, the rest of the Plan will remain in full force and effect and will in no way be affected, impaired or invalidated.

11.7 NOTICE. Any notice or filing required or permitted to be given to the Committee or a Participant will be sufficient if in writing and hand-delivered or sent by U.S. mail to the principal office of the Company or to the residential mailing address of the Participant. Notice will be deemed to be given as of the date of hand-delivery or if delivery is by mail, as of the date shown on the postmark.

11.8 GENDER AND NUMBER. If the context requires it, words of one gender when used in the Plan will include the other genders, and words used in the singular or plural will include the other.

11.9 GOVERNING LAW. The Plan will be construed, administered and governed in all respects by the laws of the State of Texas.



IN WITNESS WHEREOF, the Company has executed this document on  
this 29th day of September, 1999.

QUANEX CORPORATION

By /s/ PAUL GIDDENS

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QUANEX CORPORATION  
EXECUTIVE INCENTIVE COMPENSATION PLAN

AMENDED AND RESTATED  
EFFECTIVE OCTOBER 12, 1995

ARTICLE I  
ESTABLISHMENT AND PURPOSE

Establishment of the Plan. Quanex Corporation herewith establishes an incentive compensation plan for executives as herein set forth, which shall be known as the Quanex Corporation Executive Incentive Compensation Plan that shall become effective as of November 1, 1981.

1.1 Purpose. The purpose of the Plan is to provide executives of the Company with competitive levels of total compensation and incentive earning opportunities commensurate with results achieved and individual performance.

ARTICLE II  
DEFINITIONS

Company. "Company" means Quanex Corporation and any successor. In addition, the term "Company" shall include any other corporation in which Quanex Corporation owns more than 50% of the outstanding voting stock and adopts this Plan.

2.1 Committee. "Committee" means those directors appointed by the Board of Directors to administer this Plan.

2.2 Consolidated Financial Statements. "Consolidated Financial Statements" means for each year, the consolidated balance sheet, statement of earnings, and shareholders' equity prepared by the independent certified public accountants engaged by the Company's Board of Directors to audit the financial statements of the Company, as set forth and certified in the annual report to stockholders of the Company.

2.3 Corporate Performance Goal. "Corporate Performance Goal" means the level of EBITDA/Sales, Group EBITDA/Sales, Group Return on Controllable Investment, Return on Equity and Return on Investment for the Plan Year, approved annually by the Committee. The Committee, in its discretion, may select other Corporate Performance Goals provided such goals are

set forth in writing and approved no later than 60 days after the beginning of the Plan Year for which such goals are to apply.

2.4 EBITDA/Sales. "EBITDA/Sales" for any Plan Year means the Company's annual operating income plus depreciation and amortization divided by net sales for such year.

2.5 Group EBITDA/Sales. "Group EBITDA/Sales" for any Plan Year for a business group of the Company selected by the Committee means the annual operating income of such business group plus depreciation and amortization for such group divided by net sales for such group for such year.

2.6 Group Return on Controllable Investment. "Group Return on Controllable Investment" for a business group of the Company selected by the Committee for any Plan Year means Group annual operating income plus depreciation and amortization less the capital use charge on working capital imposed by the Company on the group, less taxes thereon at the effective tax rate for such Group for such Plan Year, divided by equity and non-current liabilities attributable to such group.

2.7 Incentive Award. "Incentive Award" means the amount due a Participant in accordance with Article IV of this Plan.

2.8 Individual Incentive Target. "Individual Incentive Target" means the anticipated Incentive Award to be paid to a Participant in the event the Corporate Performance Goals assigned to such Participant are met and the individual performance of the Participant is fully proficient and satisfactory. Individual Incentive Targets shall be a percentage of Salary as determined by the Committee and the Committee may assign such weight to each of a Participant's Corporate Performance Goals for purposes of determining whether an Individual Incentive Target is met as the Committee, in its sole discretion, shall determine.

2.9 Participant. "Participant" means an employee of the Company selected by the Committee to be considered for an Incentive Award under this Plan. The mere selection as a Participant shall not convey any rights as to the eventual receipt of an award.

2.10 Plan. "Plan" means the Quanex Corporation Executive Incentive Compensation Plan.

2.11 Plan Year. "Plan Year" means the period from November 1 to October 31 each year.

2.12 Return on Equity. "Return on Equity" for any Plan Year means the annual net income of the Company less preferred dividends divided by average common shareholders' equity. For purposes hereof average common shareholders' equity shall be the sum of common

equity as of the beginning of each fiscal quarter of the Plan Year and as of the end of the Plan Year divided by five.

2.13 Return on Investment. "Return on Investment" for any Plan Year means the annual net income of the Company plus interest expense (net of the income tax benefit thereof at the effective tax rate of the Company for such Plan Year) divided by total investment. For purposes hereof total investment shall be the sum of shareholders' equity plus long term debt as of the beginning of each fiscal quarter of the Plan Year and as of the end of the Plan Year divided by five.

2.14 Salary. "Salary" means the amounts paid by the Company to a Participant during the Plan Year as regular compensation for services, exclusive of bonuses, awards, reimbursement of expenses and all indirect payments or other additional amounts paid or credited to or on behalf of the Participant by the Company.

In determining any Corporate Performance Goal, the Committee, in its sole discretion, may exclude from long-term debt that part of the debt which the Committee considers not available for production of earnings and may adjust annual operating income and expenses for those items the Committee deems extraordinary, unusual or infrequent and for changes in accounting standards. In addition, the Committee, in its discretion, may determine that portions of long-term debt and additional equity arising from a public offering of the capital stock of the Company are to be phased into the debt and equity accounts over a period of time, not exceeding 36 months, as the Committee shall determine appropriate, giving consideration to the fact that the debt and equity may not be available, or may be only partially available for production of earnings.

### ARTICLE III ELIGIBILITY AND PARTICIPATION

Eligibility and Participation. Eligibility for participation in the Plan will be limited to those key executive personnel who, by the nature and scope of their position, regularly and directly make or influence policy decisions which significantly impact the overall results or success of the Company.

3.1 Participation. Participants will be selected by the Committee not later than the beginning of each Plan Year. Each person selected to be a Participant will be notified in writing. The notice shall inform the Participant of his selection and of the Corporate Performance Goals established for the Plan Year and the Individual Incentive Targets for the Participant.

3.2 Cessation of Participants. The Committee may withdraw its approval of an executive's participation at any time during the Plan Year.

ARTICLE IV  
AWARD DETERMINATION

Assignment of Individual Incentive Targets. Each year the Committee will assign an Individual Incentive Target for each Participant. This Individual Incentive Target will be expressed as a percentage of the Participant's Salary. The Committee shall have the power to adjust Individual Incentive Targets at any time during the Plan Year.

4.1 Corporate Performance Goals. Prior to the beginning of each Plan Year the Committee will establish Corporate Performance Goals for each Participant that, if no adjustment were made for individual Participant's performance, would result in 100% of the Individual Incentive Target being earned. In addition, the Committee will establish for each Plan Year levels of Corporate Performance Goals for each Participant that, if no adjustment were made for individual Participant's performance, would result in amounts greater or lesser than the Individual Incentive Target being earned.

To establish the Corporate Performance Goals for each Participant for each Plan Year, the Committee will use any information it considers relevant regarding the likely performance of the Company. The Corporate Performance Goals, together with related schedules, will be communicated to Participants as soon as practicable following its determination by the Committee.

4.2 Award Determination. As soon as possible after the end of the Plan Year, the Committee shall determine the Incentive Award payable to each Participant on the basis of the Corporate Performance Goals achieved based on the Consolidated Financial Statements for the Plan Year. The Incentive Award so determined shall be subject to adjustment to reflect individual performance in accordance with Section 4.4.

4.3 Individual Performance Adjustments. The Committee shall have the power to adjust awards as determined under Section 4.3, to reflect the individual performance of the Participant or to better relate the Incentive Award to the performance of the Company or to one of the business groups. In making adjustments to reflect excellent or superior individual performance the Committee is only limited by the maximum Incentive Award that can be earned by the Participant.

4.4 Participation in Other Incentive Plans. Notwithstanding the preceding, for each Participant who is also a Participant under another incentive compensation plan of the Company, the Committee may specify that incentive compensation shall be based on the compensation payable under the other plan to the maximum amount payable under that plan and additional incentive compensation shall be payable to the Participant under the provisions of this

Plan only to the extent that compensation under this Plan would exceed compensation under the other plan.

4.5 Maximum Individual Awards. The Committee shall determine for each Participant a maximum Incentive Award that can be earned for each Plan Year, expressed as a percentage of the Participant's Salary. The maximum Incentive Award cannot be exceeded regardless of the level of corporate and individual performance achieved.

ARTICLE V  
FORM AND TIMING OF AWARDS

Payment of Individual Awards. Except as provided in Section 5.2, Incentive Awards to be paid to Participants in accordance with the provisions of Article IV shall be paid in cash as soon as practicable following the release of the Company's Consolidated Financial Statements for the Plan Year.

5.1 Participant Election to Defer Payments. For each Plan Year, a Participant may elect to defer all or any part of the Incentive Award which may be earned under this Plan, and otherwise become payable to the Participant. That election to defer shall be made in accordance with the Quanex Corporation Deferred Compensation Plan. If the Participant fails to make an election to defer a part or all of his Incentive Award and the payment of a part or all of the Incentive Award would cause the Company to lose a part or all of its deduction because of Section 162(m) of the Code, the payment of the Incentive Award will be delayed under the Quanex Corporation Deferred Compensation Plan. Under this circumstance, the provisions of the Quanex Corporation Deferred Compensation Plan shall then become controlling as to the terms of payment of the Incentive Award.

ARTICLE VI  
TERMINATION OF EMPLOYMENT

In the event the employment of a Participant is terminated for cause, the right of the Participant to receive any Incentive Award under the Plan with respect to the Plan Year during which the termination occurred shall be forfeited. In the event the employment of a Participant is terminated for any reason other than for cause, the Participant or his or her other beneficiaries shall be entitled to receive a prorated Incentive Award for the portion of the Plan Year prior to his termination of employment.

ARTICLE VII  
DESIGNATION OF BENEFICIARIES

A Participant shall designate a Beneficiary or Beneficiaries who are to receive upon his death the distributions that otherwise would have been paid to the Participant. All designations shall be in writing and shall be effective only if and when delivered to the Committee during the

lifetime of the Participant. If a Participant designates a Beneficiary without providing in the designation that the Beneficiary must be living at the time of each distribution, the designation shall vest in the Beneficiary all of the distributions whether payable before or after the Beneficiary's death, and any distributions remaining upon the Beneficiary's death shall be made to the Beneficiary's estate. A Participant may, from time to time, during his lifetime, change his Beneficiary or Beneficiaries by a written instrument delivered to the Committee. In the event a Participant does not designate a Beneficiary or Beneficiaries, or if for any reason the designation is ineffective, in whole or in part, the distribution that otherwise would have been paid to the Participant shall be paid to his estate and in that event the term "Beneficiary" shall include his estate.

Once an Incentive Award is held under the terms of the Quanex Corporation Deferred Compensation, the designation of Beneficiaries shall become controlled by its terms and any designation of a Beneficiary under this Plan will become ineffective.

#### ARTICLE VIII ADMINISTRATION

**Committee Appointment.** The Committee will be appointed by the Board of Directors from their members who are not salaried officers of the Company and are not eligible to participate in the Plan. Each Committee member will serve until his or her resignation or removal. The Board of Directors will have the sole discretion to remove any one or more Committee members and appoint one or more replacement or additional Committee members from time to time.

**8.1 Committee Organization and Voting.** The Committee will select from among its members a chairman who will preside at all of its meetings and will elect a secretary without regard to whether that person is a member of the Committee. The secretary will keep all records, documents and data pertaining to the Committee's supervision and administration of the Plan. A majority of the members of the Committee will constitute a quorum for the transaction of business and the vote of a majority of the members present at any meeting will decide any question brought before the meeting. In addition, the Committee may decide any question by vote, taken without a meeting, of a majority of its members.

**8.2 Powers of the Committee.** The Committee will have the exclusive responsibility for the general administration of the Plan according to the terms and provisions of the Plan and will have all powers necessary to accomplish those purposes, including but not by way of limitation the right, power and authority:

- (a) to make rules and regulations for the administration of the Plan;

(b) to construe all terms, provisions, conditions and limitations of the Plan;

(c) to correct any defect, supply any omission or reconcile any inconsistency that may appear in the Plan;

(d) to designate the persons eligible to become Participants and to establish the Corporate Performance Goal, and the Individual Incentive Target for each Participant, a maximum for each Incentive Award, and all other matters necessary to make this Plan operative;

(e) to determine all controversies relating to the administration of the Plan, including but not limited to:

(1) differences of opinion arising between the Company and a Participant; and

(2) any question it deems advisable to determine in order to administer the Plan; and

(f) to delegate by written notice those clerical and recordation duties of the Committee, as it deems necessary or advisable for the proper and efficient administration of the Plan.

8.3 Committee Discretion. The Committee in exercising any power or authority granted under this Plan or in making any determination under this Plan shall perform or refrain from performing those acts using its sole discretion and judgment. Any decision made by the Committee or any refraining to act or any act taken by the Committee in good faith shall be final and binding on all parties. The Committee's decision shall never be subject to de novo review.

8.4 Reimbursement of Expenses. The Committee will serve without compensation for their services but will be reimbursed by the Company for all expenses properly and actually incurred in the performance of their duties under the Plan.

#### ARTICLE IX ADOPTION BY SUBSIDIARIES

Procedure for and Status After Adoption. Any subsidiary corporation in which Quanex Corporation owns more than 50% of the outstanding voting stock may, with the approval of the Committee, adopt this Plan by appropriate action of its board of directors. The terms of the



Plan will apply separately to each Company adopting the Plan and its Participants in the same manner as is expressly provided for Quanex Corporation and its Participants except that the powers of the Board of Directors and the Committee under the Plan will be exercised by the Board of Directors of Quanex Corporation alone. Each Company will bear the cost of providing Plan benefits for its own Participants. It is intended that the obligation of each Company with respect to its Participants will be the sole obligation of the Company that is employing the Participant and will not bind any other Company.

9.1 Termination of Participation By Adopting Company. Any Company adopting the Plan may, by appropriate action of its board of directors, terminate its participation in the Plan. The Committee may, in its discretion, also terminate a Company's participation in the Plan at any time.

ARTICLE X  
AMENDMENT AND/OR TERMINATION

Amendment and/or Termination. The Committee, in its sole discretion, without notice, at any time and from time to time, may modify or amend, in whole or in part, any or all of the provisions of this Plan, or suspend or terminate it entirely.

10.1 No Retroactive Effect. No modification, amendment, suspension, or termination, may without the consent of a Participant (or his Beneficiary in the case of the death of the Participant) reduce the right of a Participant (or his Beneficiary as the case may be) to a payment or distribution under this Plan to which he is entitled in accordance with the provisions contained in Article IV of this Plan.

ARTICLE XI  
MERGER, CONSOLIDATION, AND SALE OF ASSETS

Notwithstanding anything in this Plan to the contrary, in the event that the Company consolidates with, merges into, or transfers all or substantially all of its assets to another corporation, the obligations of the Company under this Plan shall be binding on that corporation or other entity.

ARTICLE XII  
MISCELLANEOUS

Limitation of Rights. Nothing in this Plan will be construed:

(a) to give any employee of any Company any right to be designated a Participant in the Plan;

(b) to give a Participant any right with respect to the Incentive Award except in accordance with the terms of this Plan;

(c) to limit in any way the right of the Company to terminate a Participant's employment with the Company at any time;

(d) to evidence any agreement or understanding, expressed or implied, that the Company will employ a Participant in any particular position or for any particular remuneration; or

(e) to give a Participant or any other person claiming through him any interest or right under this Plan other than that of any unsecured general creditor of the Company.

12.1 Distributions to Incompetents or Minors. Should a Participant become incompetent or should a Participant designate a Beneficiary who is a minor or incompetent, the Committee is authorized to pay the funds due to the parent of the minor or to the guardian of the minor or incompetent or directly to the minor or to apply those funds for the benefit of the minor or incompetent in any manner the Committee determines in its sole discretion.

Nonalienation of Benefits. No right or benefit provided in this Plan will be transferable by the Participant except, upon his death, to a named Beneficiary as provided in this Plan. No right or benefit under this Plan will be subject to anticipation, alienation, sale, assignment, pledge, encumbrance or charge, and any attempt to anticipate, alienate, sell, assign, pledge, encumber, or charge the same will be void. No right or benefit under this Plan will in any manner be liable for or subject to any debts, contracts, liabilities or torts of the person entitled to such benefits. If any Participant or any Beneficiary becomes bankrupt or attempts to anticipate, alienate, sell, assign, pledge, encumber or charge any right or benefit under this Plan, that right or benefit will, in the discretion of the Committee, cease. In that event, the Committee may have the Company hold or apply the right or benefit or any part of it to the benefit of the Participant or Beneficiary, his or her spouse, children or other dependents or any of them in any manner and in any proportion the Committee believes to be proper in its sole and absolute discretion, but is not required to do so.

12.3 Reliance Upon Information. The Committee will not be liable for any decision or action taken or not taken in good faith in connection with the administration of this Plan. Without limiting the generality of the foregoing, any decision or action taken or not taken by the Committee when it relies upon information supplied it by any officer of the Company, the Company's legal counsel, the Company's independent accountants or other advisors in connection with the administration of this Plan will be deemed to have been taken in good faith.

12.4 Severability. If any term, provision, covenant or condition of the Plan is held to be invalid, void or otherwise unenforceable, the rest of the Plan will remain in full force and effect and will in no way be affected, impaired or invalidated.

12.5 Notice. Any notice or filing required or permitted to be given to the Committee or a Participant will be sufficient if in writing and hand delivered or sent by U.S. mail to the principal office of the Company or to the residential mailing address of the Participant. Notice will be deemed to be given as of the date of hand delivery or if delivery is by mail, as of the date shown on the postmark.

12.6 Gender and Number. If the context requires it, words of one gender when used in this Plan will include the other genders, and words used in the singular or plural will include the other.

12.7 Governing Law. The Plan will be construed, administered and governed in all respects by the laws of the State of Texas.

12.8 Effective Date. This amendment and restatement of the Plan will be operative and effective on October 12, 1995.

IN WITNESS WHEREOF, the Committee has executed this document on this 9th day of November, 1995, as authorized by Section 9.1 of the Plan prior to this Amendment and Restatement.

THE COMMITTEE FOR THE  
QUANEX CORPORATION INCENTIVE  
COMPENSATION PLAN

By \_\_\_\_\_ /s/ DONALD J. MORFEE  
-----  
Chairman

QUANEX CORPORATION  
SUPPLEMENTAL BENEFIT PLAN

AMENDED AND RESTATED  
EFFECTIVE JUNE 1, 1999

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## ARTICLE I

## NAME AND PURPOSE

This plan, as adopted effective February 28, 1980 and amended and restated October 22, 1981, November 1, 1988 and June 1, 1999, shall be known as the Quanex Corporation Supplemental Benefit Plan (the "Plan").

The Plan provides retirement benefits for certain designated management employees in addition to those provided under the benefit plans for salaried employees of Quanex Corporation, as in effect from time to time.

The purpose of the Plan is to supplement those benefits that a Participant may be entitled to receive as a salaried employee of Quanex Corporation. Except as may be otherwise provided herein, the terms used in the Plan shall have the meanings specified in the Quanex Corporation Salaried Employees' Pension Plan.

## ARTICLE II

## DEFINITIONS AND DESIGNATIONS

2.01 "ACTUARIAL EQUIVALENT" means a benefit of equivalent value computed on the basis of the UP-84 mortality tables and an eight percent rate of interest for purposes of determining lump sum benefits and the value of Trust assets.

2.02 "BOARD" means the Board of Directors of the Company.

2.03 "CHANGE OF CONTROL" means the occurrence of one or more of the following events after June 1, 1999.

(a) the acquisition by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Covered Person") of beneficial ownership (within the meaning of rule 13d-3 promulgated under the Exchange Act) of 20 percent or more of either (i) the then outstanding shares of the common stock of (the "Outstanding Company Common Stock"), or (ii) the combined voting power of the then outstanding voting securities of the Company entitled to vote generally in the election of directors (the "Outstanding Company Voting Securities"); provided, however, that for purposes of this subsection (a) of this Section, the following acquisitions shall not constitute a Change of Control of the Company: (i) any acquisition directly from the Company, (ii) any acquisition by the Company, (iii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any entity controlled by the Company, or (iv) any acquisition by any corporation pursuant to a transaction which complies with clauses (i), (ii) and (iii) of subsection (c) of this Section; or

(b) individuals who, as of June 1, 1999, constitute the Board (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board; provided, however, that any individual becoming a director subsequent to June 1, 1999 whose election, or nomination for election by the Company's stockholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board shall be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial assumption of office occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents by or on behalf of a Covered Person other than the Company; or

(c) the consummation of (xx) a reorganization, merger or consolidation or sale of the Company or (yy) a disposition of all or substantially all of the assets of the Company (a "Business Combination"), in each case, unless, following such Business Combination, (i) all or substantially all of the individuals and entities who were the beneficial owners, respectively, of the Outstanding



Company Common Stock and Outstanding Company Voting Securities immediately prior to such Business Combination beneficially own, direct or indirectly, more than 80 percent of, respectively, the then outstanding shares of common stock and the combined voting power of the then outstanding voting securities entitled to vote generally in the election of directors, as the case may be, of the corporation resulting from such Business Combination (including, without limitation, a corporation which as a result of such transaction owns the Company or all or substantially all of the Company's assets either directly or through one or more subsidiaries) in substantially the same proportions as their ownership immediately prior to such Business Combination of the Outstanding Company Common Stock and Outstanding Company Voting Securities, as the case may be, (ii) no Covered Person (excluding any employee benefit plan (or related trust) of the Company or such corporation resulting from such Business Combination) beneficially owns, directly or indirectly, 20 percent or more of, respectively, the then outstanding shares of common stock of the corporation resulting from such Business Combination or the combined voting power of the then outstanding voting securities of such corporation, except to the extent that such ownership existed prior to the Business Combination, and (iii) at least a majority of the members of the board of directors of the corporation resulting from such Business Combination, were members of the Incumbent Board at the time of the execution of the initial agreement, or of the action of the Board, providing for such Business Combination; or

(d) the approval by the stockholders of Quanex of a complete liquidation or dissolution of Quanex.

2.04 "CODE" means the Internal Revenue Code of 1986, as amended from time to time.

2.05 "COMMITTEE" means the Committee established under Article IX to administer the Plan.

2.06 "COMPANY" means Quanex Corporation, a Delaware corporation.

2.07 "DISABILITY" means physical or mental condition which, during the first 24 months of the existence of the condition totally prevents the Participant from performing each and every duty of his own job. Subsequently, the disabling physical or mental condition must totally and permanently prevent the Participant from engaging for remuneration or profit in any equivalent occupation for which he is reasonably qualified by education, training, or experience. Proof of total and permanent disability must be based upon a medical examination or other evidence submitted in a statement by a licensed physician or clinic. Notwithstanding any other provision, the Participant will not qualify for disability benefits as defined herein if the disability results from chronic

alcoholism, self-addiction to narcotics or other drugs, a willfully self-inflicted injury, an injury as the result of engaging in a felonious or criminal act or enterprise; injury or disease sustained during and arising out of employment by anyone other than the Company, or service in the Armed Forces of the United States which entitles the Participant to a veteran's disability pension.

2.08 "EARLY RETIREMENT DATE" means the first day of any month after a Participant's attainment of age 55 and the completion of five years of Service.

2.09 "EARNINGS" means all wages as defined in section 3401 of the Code (for purposes of income tax withholding) for services rendered in the course of employment with the Company; modified by excluding reimbursements or other expense allowances, fringe benefits (cash and noncash), moving expenses, deferred compensation, welfare benefits, BeneFlex dollars under the Quanex Corporation Medical Reimbursement Plan, Incentive Bonuses and restricted stock awards and stock options; and modified further by including elective contributions under a cafeteria plan maintained by the Company that is governed by section 125 of the Code and elective contributions to any plan maintained by the Company that contains a qualified cash or deferred arrangement under section 401(k) of the Code.

2.10 "EMPLOYEE" means any person hired by the Company who is receiving remuneration in the form of a salary for personal services rendered to the Company.

2.11 "FINAL AVERAGE EARNINGS" means the highest monthly average of a Participant's Earnings which is produced by averaging his Earnings and Incentive Bonuses over any 36 consecutive month period during the 60 consecutive month period immediately preceding the date of the Participant's termination of employment with the Company. However, for the purposes of this

definition, no than three Incentive Bonuses shall be taken into account in calculating a Participant's earnings over any 36 consecutive month period.

2.12 "FORFEITING ACT" means the Participant's fraud, dishonesty, willful destruction of Company property, committing of a felony, revealing Company trade secrets, acts of competition against the Company or acts in aid of a competitor of the Company.

2.13 "INCENTIVE BONUS" or "INCENTIVE BONUSES" means compensation earned under the Quanex Corporation Executive Incentive Plan, whether or not deferred under the Quanex Corporation Deferred Compensation Plan.

2.14 "NORMAL RETIREMENT DATE" means the first day of the month coincident with or next following a Participant's 65th birthday.

2.15 "PARTICIPANT" means an Employee designated by the Board as eligible for participation in the Plan, and who meets the requirements of Article III.

2.16 "PLAN" means the Quanex Corporation Supplemental Benefit Plan.

2.17 "PLAN YEAR" means the period commencing on November 1 and ending on October 31.

2.18 "QUALIFIED PLAN" means the Quanex Corporation Salaried Employees' Pension Plan maintained by the Company.

2.19 "QUALIFIED PLAN BENEFIT" means the aggregate of all benefits which would be payable to the Participant from the Qualified Plan payable on or after his Normal Retirement Date. In calculating the amount of the Qualified Plan Benefit, for the purposes of the Plan the following shall apply:

(a) If the normal form of benefit of the Qualified Plan is other than a straight life annuity, the benefit shall be expressed in the form of a straight life annuity by using the actuarial assumptions contained in the Qualified Plan.

(b) If benefits under the Qualified Plan are paid or are payable to the Participant prior to the date his benefits commence under the Plan, the Actuarial Equivalent of such benefits as of his Normal Retirement Date (as defined in the Qualified Plan) shall be used.

(c) The amount of a Participant's Qualified Plan Benefit shall be determined based on the provisions of the Qualified Plan as in effect on the date his benefits under the Plan are determined.

(d) The amount of a Participant's Qualified Plan Benefit shall be determined by disregarding any offset for benefits payable under a terminated retirement plan that was previously maintained by the Company as one of its affiliates.

2.20 "SERVICE" means service for purposes of the Qualified Plan. In determining a Participant's Service, all Years of Service after the Participant's date of hire shall be taken into effect.

2.21 "SOCIAL SECURITY BENEFIT" means, for all purposes other than determining the Disability benefit, the monthly amount payable commencing on the later of the Participant's 65th birthday or the date of his termination of employment with the Company under the provisions of Title II of the Social Security Act. Such benefit shall be determined based on (1) the Participant's average monthly wage or indexed earnings (as defined in the Social Security Act, as amended) on the date of his termination of employment with the Company, computed under the Social Security Act as in effect on the January 1 of the calendar year in which benefits are determined and using the Participant's annual total wages from the Company for the prior calendar year, as defined in Section 3121(b), assuming his wages increased prior thereto at the rate of increase in the average per worker total wages reported by the Social Security Administration, and assuming continuation of such wages without increase thereafter until his termination of employment with the Company (with no wages thereafter); and (2) the Table of Primary Social Security Benefits under the Social Security Act as in effect on the January 1 of the calendar year in which his termination of employment with the Company actually occurs. "Social Security Benefit" means, for purposes of determining a Disability benefit, any actual disability benefit for which the Participant is eligible under Title II of the Social Security Act.

ARTICLE III  
PARTICIPATION

3.01 ELIGIBILITY TO PARTICIPATE. An Employee shall become eligible to become a Participant in the Plan by designation of the Board. The Committee shall notify each Participant of his eligibility. Each designated Employee shall furnish such information and perform such acts as the Committee may require prior to becoming a Participant.

3.02 REEMPLOYMENT. Any person who terminates employment with the Company shall not be eligible to participate in the Plan upon his reemployment by the Company unless the Board so determines. In such event, the Board shall specify whether and under what conditions the person shall receive credit for all or any of his Service completed prior to reemployment.

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## ARTICLE IV

## RETIREMENT BENEFITS

4.01 NORMAL RETIREMENT BENEFIT. Subject to Article VIII, if a Participant terminates employment with the Company on or after his Normal Retirement Date, he will be entitled to the lump-sum Actuarial Equivalent of a monthly benefit payable to the Participant for life only in an amount equal to:

(a) 2.75 percent of his Final Average Earnings multiplied by his years of Service (not in excess of 29.09 years), less

(b) the sum of:

- (1) the Participant's Qualified Plan Benefit, and
- (2) the Participant's Social Security Benefit.

4.02 DEFERRED RETIREMENT BENEFIT. If a Participant terminates employment with the Company on or after his Normal Retirement Date, he will be entitled to the lump-sum Actuarial Equivalent of a monthly benefit payable to the Participant for life only determined in accordance with the provisions of Section 4.01. The benefit will not be actuarially increased to reflect the later benefit payment date or his shorter life expectancy. In determining a Participant's deferred retirement benefit, his Service subsequent to his Normal Retirement Date and the computation of his Final Average Earnings shall take into account his Service after his Normal Retirement Date.

4.03 EARLY RETIREMENT BENEFIT. If a Participant terminates employment with the Company on or after his Early Retirement Date but before age 65, he shall be entitled to the lump-sum Actuarial Equivalent of a monthly benefit payable to the Participant for life only determined in accordance with the provisions of Section 4.01 based upon his years of Service and Final Average Earnings on the date of his termination of employment with the Company. The monthly amount

shall be reduced by a fraction, the numerator of which is the Participant's actual years of Service as of the date of his termination of employment with the Company and the denominator of which is the number of years of Service the Participant would have if he continued to be employed by the Company until the date of his 65th birthday.

4.04 DISABILITY BENEFIT. If a Participant who has completed six months of Service terminates employment with the Company prior to his Early Retirement Date due to his Disability, he shall receive a monthly Disability benefit, for so long as he has a Disability but no longer than his Normal Retirement Date (on which date the Participant shall be treated as a retiree entitled to benefits under Section 4.01), in an amount equal to:

(a) 50 percent of the sum of his monthly Earnings in effect at the date of his Disability and the monthly equivalent of the average of his Incentive Bonuses for the prior three Plan Years, less

(b) the sum of:

(1) the Participant's Qualified Plan Benefit;

(2) the Participant's Social Security Benefit;

(3) the Participant's benefit under the Company's group long-term disability insurance plan;

(4) the Participant's benefit under an individual disability policy provided by the Company, and;

(5) the Participant's benefit under the Company's wage continuation policy plan.

Upon the occurrence of the Normal Retirement Date of a former Participant with a Disability, he will be entitled to the lump sum Actuarial Equivalent of a monthly benefit payable to him for life only determined in accordance with the provisions of Section 4.01. In determining his benefit payable upon the occurrence of his Normal Retirement Date, his Final Average Earnings and his years of Service shall be determined as of the date of his Disability.

4.05 DEFERRED VESTED BENEFIT. If a Participant terminates employment with the Company prior to his Early Retirement Date but has five or more years of Service, he will upon attaining age 55 be entitled to the lump-sum Actuarial Equivalent of a monthly benefit payable to the Participant for life only determined in accordance with the provisions of Section 4.01 based upon his years of Service and Final Average Earnings at his termination of employment. The benefit calculated under Section 4.01 however, shall be actuarially reduced, using the factors described in Section 2.01 for the definition of Actuarial Equivalent, because of the younger age and earlier commencement for all Participants entering the Plan on or after June 1, 1988, and shall be reduced because of the younger age and earlier commencement for all Participants who were in the Plan on May 31, 1988 by a fraction, the numerator of which is the Participant's years of Service he would have had had he continued to work until his Early Retirement Date and the denominator of which is the number of years of Service the Participant would have had had he continued to work until his Normal Retirement Date. If the Participant has fewer than five years of Service when he terminates employment prior to his Early Retirement Date, he shall not be entitled to any benefits under the Plan.

4.06 CHANGE OF CONTROL BENEFIT. Notwithstanding any other provisions of the Plan, if a Participant's termination of employment with the Company occurs after a Change of Control, he will be entitled to the lump-sum Actuarial Equivalent of a monthly benefit payable to the Participant for life only determined in accordance with the provisions of section 4.01 based upon his years of Service and Final Average Earnings at his termination of employment. The benefit calculated under section 4.01 shall not be actuarially reduced because of the Participant's age or early payment of his benefit under the Plan. Any benefit paid pursuant to this Section 4.06 shall be in lieu of any other benefit otherwise payable to the Participant under the Plan.



4.07 TIME OF PAYMENT OF BENEFIT. The lump sum payments provided for Normal Retirement, Deferred Retirement, and Early Retirement, shall be paid on the 90th day after the Participant's termination of employment with the Company. The monthly Disability benefit shall commence being paid on the first day of the month coincident with or next following the Participant's termination of employment with the Company due to Disability and shall cease with the last payment prior to his recovery or attainment of his Normal Retirement Date. If a former Participant who terminated employment with the Company due to Disability continues to have a Disability until his Normal Retirement Date, the lump sum payment then due shall be paid on his Normal Retirement Date. A Participant's deferred vested benefit or Change of Control benefit shall be payable on the 90th day after his attainment of age 55.

## ARTICLE V

## DEATH BENEFITS

5.01 IN GENERAL. The benefits under the Plan payable subsequent to a Participant's or former Participant's death shall be limited to those contained in this Article, and shall in any case be subject to Article VIII.

5.02 DEATH DURING EMPLOYMENT. If a Participant's death occurs while he is in the employ of the Company, an Actuarially Equivalent lump sum benefit shall be payable as hereinafter provided in this Section. The designated beneficiary of a Participant shall be entitled to receive a lump-sum benefit that is Actuarially Equivalent to 50 percent of the sum of the Participant's monthly Earnings in effect at the date of his death and the monthly equivalent of the average of his Incentive Bonuses for the prior three Plan Years, payable monthly until the later of completion of 120 monthly payments or the date the Participant would have attained his Normal Retirement Date. The lump-sum payment shall be made on the 90th day after the death of the Participant. The designated beneficiary of a Participant shall be determined under Article VI.

## 5.03 DEATH AFTER TERMINATION OF EMPLOYMENT.

(a) In General. Except as provided in this Section, no benefits shall be payable to or on behalf of a Participant or former Participant whose death occurs subsequent to his termination of employment.

(b) Before Benefit is Paid. If a former Participant dies before his benefit is paid but after his termination of employment with the Company on or after his Normal Retirement Date, his Early Retirement Date or a Change of Control, his designated beneficiary, if any, shall be entitled to receive a lump-sum benefit equal to the benefit which he would have received had he lived to the date his benefit would have been paid out. If a former Participant dies before his benefit is paid and he was eligible for a Disability benefit or he terminated employment with the Company prior to a Change of Control and he was entitled to a deferred vested benefit under Section 4.05, his designated beneficiary, if any, shall be entitled to receive a lump-sum benefit which is Actuarially Equivalent to a survivor annuity equal to the survivor portion of a qualified joint and 50 percent survivor annuity as if the former Participant had been entitled to elect and had elected such survivor annuity

on the day before his death. The survivor lump-sum death benefit shall be payable on the 90th day following the date of the Former Participant's death. In calculating the survivor portion for the survivor lump-sum benefit, the benefit shall be reduced in the same manner it is reduced under Section 4.03, 4.04 or 4.05, whichever is applicable, for payment earlier than Normal Retirement Date. In the event of a Participant's termination of employment with the company after a Change of Control, the death benefits payable under this Section 5.03 on his behalf will not be reduced for payment before the Participant's Normal Retirement Date.

(c) After Disability Benefits Commence. If a former Participant who is receiving a Disability benefit dies prior to reaching his Normal Retirement Date but while he still has a Disability, his designated beneficiary shall receive a lump-sum benefit which is Actuarially Equivalent to the survivor portion of a qualified joint and 50 percent survivor annuity as if the former Participant had been entitled to elect and had elected such survivor annuity on the day before his death. Such benefit shall be payable on the 90th day after his death.

ARTICLE VI  
BENEFICIARIES

6.01 DESIGNATION OF BENEFICIARY. Each Participant or former Participant shall designate as his beneficiary the person or persons who shall, upon his death, receive the death benefits, if any, payable pursuant to Article V. The designation shall be in such form as the Committee requires and may include contingent beneficiaries. A beneficiary designation shall be effective when filed with the Committee during the Participant's or former Participant's life, and shall cancel and revoke all prior designations.

6.02 PAYMENT OF BENEFITS UPON DEATH. If a Participant's or former Participant's death occurs prior to payment of his benefit, the benefit payable upon his death, if any, shall be paid to the persons or persons designated as his primary beneficiary, but if the primary beneficiary does not survive him, then to the person or persons designated as the contingent beneficiary. If no primary or contingent beneficiary survives him or if no beneficiary designation is in effect upon his death, then the benefit under Article V shall be paid to his spouse. If his spouse does not survive him, then the benefit shall be paid to his descendants who survive him by right of representation, and if no descendants of the Participant or former Participant survive him, then to his estate.

6.03 MINORS AND PERSONS UNDER LEGAL DISABILITY. Payments to a minor or a person under a legal disability shall be made by the Company at the direction of the Committee as follows:

(a) to the natural or adoptive parents or legal guardian or conservator of such person, or to any other person in loco parent is;

(b) to a custodian for such person under the Uniform Gifts to Minors Act or Gifts of securities to Minors Act; or

(c) by expending amounts directly for the education and support of such person.

## ARTICLE VII

## FORFEITURE FOR CAUSE

Except with respect to persons whose terminations of employment with the Company occur after a Change of Control, notwithstanding any other provision of the Plan to the contrary, in all cases where a written document is executed by the Company expressly making acts of competition against the Company or acts in aid of a competitor of the Company by the Participant or former Participant a Forfeiting Act, if the Participant commits one or more Forfeiting Acts during his employment with the Company or following his termination of employment, any and all unpaid benefits due the Participant or his designated beneficiary shall be forfeited. This provision shall apply regardless of the date the Company first learns of the occurrence of a Forfeiting Act.

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## ARTICLE VIII

## AGREEMENT FUNDED THROUGH RABBI TRUST

The Company shall pay the benefits due the Participants and former Participants under the Plan; however, should it fail to do so when a benefit is due, such benefit shall be paid by the Trustee of that certain Trust Agreement entered into contemporaneously with this Amendment, by and between the Company and Norstar Trust Company, a New York banking corporation (the "Trust"). In any event, if the Trust fails to pay for any reason, the Company still remains liable for the payment of all benefits provided by the Plan. The Company may contribute at any time and from time to time such assets to the Trust as it, in its sole discretion, shall determine and shall have the right at any time and from time to time to borrow from the Trust the fair market value of assets held in the Trust which are in excess of the net present value of the largest benefit all Participants and former Participants are entitled to under the Plan as of the beginning of the Plan Year during which the loan is made (exclusive of any Disability or death benefit). Any such loan shall be evidenced by an instrument in writing, shall bear interest at such rate as the Company would be required to pay to its prime lender under the same terms (except for the security), shall provide a repayment schedule which would repay but only to the extent of the funds so borrowed, such amount as is necessary to maintain at the beginning of each Plan Year during the existence of the loan, non-borrowed funds in the Trust at a level at least equal to the net present value of all benefits calculated under the preceding sentence and shall provide for prepayment at the Company's election, without penalty. The above calculations shall use the same actuarial factors set out in the definition of Actuarial Equivalent under Section 2.01. All assets contributed shall be held in and administered according to the terms of the Trust which are incorporated by reference in the Plan for all purposes. However,

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in no event shall the rights of Participants and former Participants in the assets held by the Trust be greater than the rights of unsecured creditors of the Company. Nothing contained in the Plan or the Trust constitutes a secured promise by the Company that the assets of the Company will be sufficient to pay any benefit to any person.

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## ARTICLE IX

## PLAN COMMITTEE

9.01 COMMITTEE. The Plan shall be administered by the Committee, which shall have three members designated in writing by the Company. Any person may resign from the Committee upon 30 days' prior notice to the Company and to any other member of the Committee. The Company may remove any member of the Committee by written notice to him and to any other member of the Plan Committee. The Company shall fill any vacancy and shall give written notice thereof to the other members of the Committee. In the interim, the other member(s) of the Committee shall have full authority to act. If, at any time, there are no members of the Committee, then the Board shall serve as the Committee.

9.02 GENERAL RIGHTS, POWERS AND DUTIES OF PLAN COMMITTEE. The Committee shall be responsible for the management, operation and administration of the Plan. In addition to any powers, rights and duties set forth elsewhere in the Plan, it shall have the following powers and duties:

(a) to adopt such rules and regulations consistent with the provisions of the Plan as it deems necessary for the proper and efficient administration of the Plan;

(b) to enforce the Plan in accordance with its terms and any rules and regulations it establishes;

(c) to maintain records concerning the Plan sufficient to prepare reports, returns and other information required by the Plan or by law;

(d) to construe and interpret the Plan and to resolve all questions arising under the Plan;

(e) to direct the Company to pay benefits under the Plan, and to give such other directions and instructions as may be necessary for the proper administration of the Plan;

(f) to employ or retain agents, attorneys, actuaries, accounts or other persons, who may also be employed by or represent the Company, and



(g) to be responsible for the preparation, filing and disclosure on behalf of the Plan of such documents and reports as are required by any applicable Federal or State law.

The Committee shall have no power to add to, subtract from or modify any of the terms of the Plan, or to change or add to any benefits provided by the Plan, or to waive or fail to apply any requirements of eligibility for benefits under the Plan.

9.03 RULES AND DECISIONS. The Committee may adopt such rules and actuarial tables as it deems necessary, desirable or appropriate. All rules and decisions of the Committee shall be uniformly and consistently applied to all Participants in similar circumstances. When making a determination or calculation, the Committee shall be entitled to rely upon information furnished to it by a Participant or beneficiary, the Company, and the legal counsel, actuary and accountant for the Company.

9.04 COMMITTEE PROCEDURES. The Committee may act at a meeting or in writing without a meeting. The Committee shall elect one of its members as chairman and appoint a secretary, who may or may not be a Committee member. The Secretary shall keep a record of all meetings and forward all necessary communications to the Company. The Committee may adopt such bylaws and regulations as it deems desirable for the conduct of its affairs. All decisions of the Committee shall be made by the vote of the majority, including actions in writing taken without a meeting. A dissenting Committee member who, within a reasonable time after he has knowledge of any action or failure to act by the majority, registers his dissent in writing delivered to the other Committee members and the Company, shall not, to the extent permitted by law, be responsible for any such action or failure to act.

9.05 AUTHORIZATION OF BENEFIT PAYMENTS. The Committee shall issue directions to the Company concerning all benefits which are to be paid pursuant to the provisions of the Plan. The Company shall furnish the Committee such data and information as it may require. The records of the Company shall be determinative of each Participant's period of employment, termination of employment and the reason therefor, leave of absence, reemployment, years of Service, Earnings, and Final Average Earnings. Participants and their beneficiaries shall furnish to the Committee such evidence, data, or information, and execute such documents, as the Committee requests.

9.06 APPLICATION AND FORMS OF BENEFITS. The Committee may require a Participant or former Participant to complete and file with the Committee an application for retirement benefits and all other forms approved by the Committee, and to furnish all pertinent information requested by the Committee. The Committee may rely upon all such information so furnished it, including the Participant's or former Participant's current mailing address.

9.07 FACILITY OF PAYMENT. Whenever, in the Committee's opinion, a person entitled to receive any payment of a benefit or installment thereof hereunder is under a legal disability or is incapacitated in any way so as to be unable to manage his financial affairs, the Committee may direct the Company to make payments to such person or to his legal representative or to a relative or friend of such person for his benefit, or the Committee may direct the Company to apply the payment for the benefit of such person in such manner as the Committee considers advisable. Any payment of a benefit or installment thereof in accordance with the provisions of this Section shall be a complete discharge of any liabilities for the making of such payment under the provisions of the Plan.

9.08 CLAIMS PROCEDURE. The Committee shall make all determinations as to the right of any person to receive benefits under the Plan. Any denial by the Committee of a claim for benefits under the Plan by a Participant, former Participant beneficiary of a former Participant (collectively referred to herein as "Claimant") shall be stated in writing by the Committee and delivered or mailed to the Claimant on the 90th day after receipt of the claim, unless special circumstances require an extension of time for processing the claim. If such an extension of time is required, written notice of the extension shall be furnished to the Claimant on the 90th day after receipt of the claim and the claim shall thereafter be paid on the 180th day after the date of receipt of the initial claim. Such notice shall set forth the specific reasons for the denial, specific reference to pertinent provisions of the Plan upon which the denial is based, a description of any additional material or information necessary for the Claimant to perfect his claim with an explanation of why such material or information is necessary, and an explanation of claim review procedures under the Plan written to the best of the Committee's ability in a manner that may be understood without legal or actuarial counsel. A Claimant whose claim for benefits has been wholly or partially denied by the Committee may, within 90 days following the date of such denial, request a review of such denial in a writing addressed to the Committee. The Claimant shall be entitled to submit such issues or comments, in writing or otherwise, as he shall consider relevant to a determination of his claim, and may include in his request a request for a hearing in person before the Committee. Prior to submitting his request, the Claimant shall be entitled to review such documents as the Committee shall agree are pertinent to his claim. The Claimant may, at all stages of review, be represented by counsel, legal or otherwise, of his choice, provided that the fees and expenses of such counsel shall be borne by the Claimant. All requests for review shall be promptly resolved. The Committee's decisions with respect to any

such review shall be set forth in writing and shall be mailed to the Claimant on the 60th day following receipt by the Committee of the Claimant's request unless special circumstances, such as the need to hold a hearing, require an extension of time for processing, in which case the Committee's decision shall be so mailed on the 120th day after receipt of such request.

9.09 RESPONSIBILITY. No member of the Committee or of the Board shall be liable to any person for any action taken or omitted in connection with the administration of the Plan unless attributable to his own fraud or willful misconduct; nor shall the Company be liable to any person for any such action unless attributable to fraud or willful misconduct on the part of a director, officer or employee of the Company.

## ARTICLE X

## AMENDMENT AND TERMINATION

10.01 AMENDMENT. The Plan may be amended in whole or in part by the Company at any time. Notice of any such amendment shall be given in writing to the Committee and to each Participant, former Participant, and beneficiary of a deceased former Participant. No such amendment however shall have the effect of reducing that portion of the benefit the Participant or former Participant ultimately becomes entitled to below that amount he would have received for Service to the date of the amendment under the formula set out in the Plan prior to the amendment.

10.02 RIGHT TO TERMINATE PLAN. The Company reserves the right to terminate the accrual or vesting of additional benefits under the Plan by any or all Participants at any time by written notice to the Committee. The Committee shall notify any Participant affected by such termination of such action and its effective date within 30 days after it receives notice from the Company. A Participant whose accrual of additional benefits is terminated shall not lose any previously earned and vested benefits, and, subject to Article VIII, any such vested benefits shall be payable at the time and in the manner provided hereunder.

## ARTICLE XI

## MISCELLANEOUS

11.01 INALIENABILITY OF BENEFITS. The right of any Participant, former Participant or beneficiary to any benefit or payment under the Plan shall not be subject to voluntary or involuntary transfer, alienation, pledge, assignment, garnishment, sequestration or other legal or equitable process. Any attempt to transfer, alienate, pledge, assign or otherwise dispose of such right or any attempt to subject such right to attachment, execution, garnishment, sequestration or other legal or equitable process shall be null and void.

11.02 NO IMPLIED RIGHTS. Neither the establishment of the Plan nor any modification thereof shall be construed as giving any Participant, former Participant beneficiary or other person any legal or equitable right unless such right shall be specifically provided for in the Plan or conferred by affirmative action of the Company in accordance with the terms and provisions of the Plan.

11.03 ACTIONS BY COMPANY. All actions by the Company under the Plan shall be taken by the Board or by a person or persons designated by the Board.

11.04 BINDING EFFECT. The provisions of the Plan shall be binding on the Company, the Committee, and all persons entitled to benefits under the Plan, together with their respective heirs, legal representatives and successors in interest.

11.05 NUMBER AND GENDER. Wherever appropriate, the singular shall include the plural, the plural shall include the singular, and the masculine shall include the feminine or neuter.

11.06 GOVERNING LAW. The Plan shall be construed and administered according to the laws of the State of Texas.

IN WITNESS WHEREOF, effective June 1, 1999, the Company has adopted this amendment and restatement of the Plan on the 18th day of June, 1999.

QUANEX CORPORATION

By:                   /s/ PAUL GIDDENS  
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Title: Vice President - Human Resources  
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## CHANGE IN CONTROL AGREEMENT

THIS AGREEMENT between Quanex Corporation, a Delaware corporation (the "Company"), and \_\_\_\_\_ (the "Executive") is effective as of \_\_\_\_\_ (the "Effective Date"). Certain capitalized terms used herein are defined in Section 21.

## W I T N E S S E T H:

WHEREAS, the Company considers it to be in the best interests of its stockholders to encourage the continued employment of certain key employees of the Company notwithstanding the possibility, threat or occurrence of a Change in Control of the Company (as that phrase is defined in Section 2); and

WHEREAS, the Executive is a key employee of the Company; and

WHEREAS, the Company believes that the possibility of the occurrence of a Change in Control of the Company may result in the termination by the Executive of the Executive's employment by the Company or in the distraction of the Executive from the performance of his duties to the Company, in either case to the detriment of the Company and its stockholders; and

WHEREAS, the Company recognizes that the Executive could suffer adverse financial and professional consequences if a Change in Control of the Company were to occur; and

WHEREAS, the Company wishes to enter into this Agreement to protect the Executive if a Change in Control of the Company occurs, thereby encouraging the Executive to remain in the employ of the Company and not to be distracted from the performance of his duties to the Company by the possibility of a Change in Control of the Company;

NOW, THEREFORE, the parties agree as follows:

Section 1. Other Employment Arrangements.

(a) This Agreement does not affect the Executive's existing or future employment arrangements with the Company unless a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement. The Executive's employment with the Company shall continue to be governed by the Executive's existing or future employment agreements with the Company, if any, or, in the absence of any employment agreement, shall continue to be at the will of the Board of Directors or, if the Executive is not an officer of the Company at the time of the termination of the Executive's employment with the Company, the will of the Chief Executive Officer of the Company, except that if (i) a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement, and (ii) the Executive's employment with the Company is terminated (whether by the Executive or the Company or automatically as provided in Section 3) after the occurrence of that Change in Control of the Company, then the Executive shall be entitled to receive certain benefits as provided in this Agreement.



(b) Notwithstanding anything contained in this Agreement to the contrary, if following the commencement of any discussion with a third person that ultimately results in a Change in Control of the Company, (i) the Executive's employment with the Company is terminated, (ii) the Executive is removed from any material duties or position with the Company, (iii) the Executive's Base Salary is reduced, or (iv) the Executive's annual bonus is reduced to an amount less than the Benchmark Bonus, then for all purposes of this Agreement, such Change in Control of the Company shall be deemed to have occurred on the date immediately prior to the date of such termination, removal, or reduction.

(c) Nothing in this Agreement shall prevent or limit the Executive's continuing or future participation in any plan, program, policy or practice of or provided by the Company or any of its Affiliates and for which the Executive may qualify, nor shall anything herein limit or otherwise affect such rights as the Executive may have under any contract or agreement with the Company or any of its Affiliates. Amounts which are vested benefits or which the Executive is otherwise entitled to receive under any plan, program, policy or practice of or provided by, or any contract or agreement with, the Company or any of its Affiliates at or subsequent to the date of termination of the Executive's employment with the Company shall be payable or otherwise provided in accordance with such plan, program, policy or practice or contract or agreement except as explicitly modified by this Agreement.

Section 2. Change in Control of the Company. For purposes of this Agreement, a "Change in Control of the Company" shall mean the occurrence of any of the following after the Effective Date:

(a) The acquisition by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Exchange Act) (a "Covered Person") of beneficial ownership (within the meaning of rule 13d-3 promulgated under the Exchange Act) of 20 percent or more of either (i) the then outstanding shares of the common stock of the Company (the "Outstanding Company Common Stock"), or (ii) the combined voting power of the then outstanding voting securities of the Company entitled to vote generally in the election of directors (the "Outstanding Company Voting Securities"); provided, however, that for purposes of this subsection (a) of this Section 2, the following acquisitions shall not constitute a Change in Control of the Company: (i) any acquisition directly from the Company, (ii) any acquisition by the Company, (iii) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any entity controlled by the Company, or (iv) any acquisition by any corporation pursuant to a transaction which complies with clauses (i), (ii) and (iii) of subsection (c) of this Section 2; or

(b) Individuals who, as of the Effective Date, constitute the Board of Directors (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board of Directors; provided, however, that any individual becoming a director subsequent to the Effective Date whose election, or nomination for election by the Company's stockholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board shall be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial assumption of office occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents by or on behalf of a Covered Person other than the Board; or

(c) Consummation of (xx) a reorganization, merger or consolidation or sale of the Company, or (yy) a disposition of all or substantially all of the assets of the Company (a "Business Combination"), in each case, unless, following such Business Combination, (i) all or substantially all of the individuals and entities who were the beneficial owners, respectively, of the Outstanding Company Common Stock and Outstanding Company Voting Securities immediately prior to such Business Combination beneficially own, direct or indirectly, more than 80 percent of, respectively, the then outstanding shares of common stock and

the combined voting power of the then outstanding voting securities entitled to vote generally in the election of directors, as the case may be, of the corporation resulting from such Business Combination (including, without limitation, a corporation which as a result of such transaction owns the Company or all or substantially all of the Company's assets either directly or through one or more subsidiaries) in substantially the same proportions as their ownership immediately prior to such Business Combination of the Outstanding Company Common Stock and Outstanding Company Voting Securities, as the case may be, (ii) no Covered Person (excluding any employee benefit plan (or related trust) of the Company or such corporation resulting from such Business Combination) beneficially owns, directly or indirectly, 20 percent or more of, respectively, the then outstanding shares of common stock of the corporation resulting from such Business Combination or the combined voting power of the then outstanding voting securities of such corporation, except to the extent that such ownership existed prior to the Business Combination, and (iii) at least a majority of the members of the board of directors of the corporation resulting from such Business Combination, were members of the Incumbent Board at the time of the execution of the initial agreement, or of the action of the Board of Directors, providing for such Business Combination; or

(d) Approval by the stockholders of the Company of a complete liquidation or dissolution of the Company.

Section 3 . Term of This Agreement. The term of this Agreement shall begin on the Effective Date and, unless automatically extended pursuant to the second sentence of this Section 3, shall expire on the first to occur of:

(i) the Executive's death or the Executive's Disability, which events shall also be deemed automatically to terminate Executive's employment by the Company;

(ii) the termination by the Executive or the Company of the Executive's employment by the Company; or

(iii) the end of the last day (the "Expiration Date") of:

(x) the three-year period beginning on the Effective Date (or any period for which the term of this Agreement shall have been automatically extended pursuant to the second sentence of this Section 3) if no Change in Control of the Company shall have occurred during that three-year period (or any period for which the term of this Agreement shall have been automatically extended pursuant to the second sentence of this Section 3); or

(y) if one or more Changes in Control of the Company shall have occurred during the three-year period beginning on the Effective Date (or any period for which the term of this Agreement shall have been automatically extended pursuant to the second sentence of this Section 3), the three-year period beginning on the date on which the last Change in Control of the Company occurred.

If (i) the term of this Agreement shall not have expired as a result of the occurrence of one of the events described in clause (i) or (ii) of the immediately preceding sentence, and (ii) the Company shall not have given notice to the Executive at least ninety (90) days before the Expiration Date that the term of this Agreement will expire on the Expiration Date, then the term of this Agreement shall be automatically

extended for successive one-year periods (the first such period to begin on the day immediately following the Expiration Date) unless the Company shall have given notice to the Executive at least ninety (90) days before the end of any one-year period for which the term of this Agreement shall have been automatically extended that such term will expire at the end of that one-year period. The expiration of the term of this Agreement shall not terminate this Agreement itself or affect the right of the Executive or the Executive's legal representatives to enforce the payment of any amount or other benefit to which the Executive was entitled before the expiration of the term of this Agreement or to which the Executive became entitled as a result of the event (including the termination, whether by the Executive or the Company or automatically as provided in this Section 3, of the Executive's employment by the Company) that caused the term of this Agreement to expire.

Section 4. Event of Termination for Cause. An "Event of Termination for Cause" shall have occurred if, after a Change in Control of the Company, the Executive shall have committed:

- (i) gross negligence or willful misconduct in connection with his duties or in the course of his employment with the Company;
- (ii) an act of fraud, embezzlement or theft in connection with his duties or in the course of his employment with the Company;
- (iii) intentional wrongful damage to property of the Company;
- (iv) intentional wrongful disclosure of secret processes or confidential information of the Company; or
- (v) an act leading to a conviction of a felony or a misdemeanor involving moral turpitude.

For purposes of this Agreement, no act, or failure to act, on the part of the Executive shall be deemed "intentional" if it was due primarily to an error in judgment or negligence, but shall be deemed "intentional" only if done, or omitted to be done, by the Executive not in good faith and without reasonable belief that his action or omission was in the best interest of the Company. Notwithstanding the foregoing, the Executive shall not be deemed to have been terminated as a result of an "Event of Termination for Cause" hereunder unless and until there shall have been delivered to the Executive a copy of a resolution duly adopted by the affirmative vote of not less than three-quarters of the Board of Directors then in office at a meeting of the Board of Directors called and held for such purpose (after reasonable notice to the Executive and an opportunity for the Executive, together with his counsel, to be heard before the Board of Directors), finding that, in the good faith opinion of the Board of Directors, the Executive had committed an act set forth above in this Section 4 and specifying the particulars thereof in detail. Nothing herein shall limit the right of the Executive or his legal representatives to contest the validity or propriety of any such determination.

Section 5. An Event of Termination for Good Reason. An "Event of Termination for Good Reason" shall have occurred if, after a Change in Control of the Company, the Company shall:

- (i) assign to the Executive any duties inconsistent with the Executive's position (including offices, titles and reporting requirements), authority, duties or responsibilities with the Company in effect immediately before the occurrence of the first Change in Control of the Company or otherwise make any change in any such position, authority, duties or responsibilities;

(ii) remove the Executive from, or fail to re-elect or appoint the Executive to, any duties or position with the Company or any of its Affiliates that were assigned or held by the Executive immediately before the occurrence of the first Change in Control of the Company, except that a nominal change in the Executive's title that is merely descriptive and does not affect rank or status shall not constitute such an event;

(iii) take any other action that results in a material diminution in such position, authority, duties or responsibilities or otherwise take any action that materially interferes therewith;

(iv) reduce the Executive's annual base salary as in effect immediately before the occurrence of the first Change in Control of the Company or as the Executive's annual base salary may be increased from time to time after that occurrence (the "Base Salary");

(v) reduce the Executive's annual bonus (x) to an amount less than \$\_\_\_\_\_ at any time on or prior to the third anniversary of the Effective Date, or (y) to an amount less than the average of the two annual bonuses earned by such Executive with respect to the two preceding years at any time after the third anniversary of the Effective Date (the amount determined pursuant to clause (x) or (y), as applicable, is referred to herein as the "Benchmark Bonus");

(vi) relocate the Executive's principal office outside of the portion of the metropolitan area of the City of Houston, Texas that is located within the highway known as "Beltway 8";

(vii) fail to (x) continue in effect any bonus, incentive, profit sharing, performance, savings, retirement or pension policy, plan, program or arrangement (such policies, plans, programs and arrangements collectively being referred to herein as "Basic Benefit Plans"), including, but not limited to, any deferred compensation, supplemental executive retirement or other retirement income, stock option, stock purchase, stock appreciation, or similar policy, plan, program or arrangement of the Company, in which the Executive was a participant immediately before the occurrence of the first Change in Control of the Company, or any substitute plan adopted by the Board of Directors and in which the Executive was a participant immediately before the occurrence of the last Change in Control of the Company, unless an equitable and reasonably comparable arrangement (embodied in a substitute or alternative benefit or plan) shall have been made with respect to such Basic Benefit Plan promptly following the occurrence of the last Change in Control of the Company, or (y) continue the Executive's participation in any Basic Benefit Plan (or any substitute or alternative plan) on substantially the same basis, both in terms of the amount of benefits provided to the Executive (which are in any event always subject to the terms of any applicable Basic Benefit Plan) and the level of the Executive's participation relative to other participants, as existed immediately before the occurrence of the first Change in Control of the Company;

(viii) fail to continue to provide the Executive with benefits substantially similar to those enjoyed by the Executive under any of the Company's other Executive benefit plans, policies, programs and arrangements, including, but not limited to, life insurance, medical, dental, health, hospital, accident or disability plans, in which the Executive was a

participant immediately before the occurrence of the first Change in Control of the Company;

(ix) take any action that would directly or indirectly materially reduce any other non-contractual benefits that were provided to the Executive by the Company immediately before the occurrence of the first Change in Control of the Company or deprive the Executive of any material fringe benefit enjoyed by the Executive immediately before the occurrence of the first Change in Control of the Company;

(x) fail to provide the Executive with the number of paid vacation days to which the Executive was entitled in accordance with the Company's vacation policy in effect immediately before the occurrence of the first Change in Control of the Company;

(xi) fail to continue to provide Executive with office space, related facilities and support personnel (including, but not limited to, administrative and secretarial assistance) (y) that are both commensurate with Executive's responsibilities to and position with the Company immediately before the occurrence of the first Change in Control of the Company and not materially dissimilar to the office space, related facilities and support personnel provided to other Executives of the Company having comparable responsibility to the Executive, or (z) that are physically located at the Company's principal executive offices;

(xii) require the Executive to perform a majority of his duties outside the Company's principal executive offices for a period of more than 21 consecutive days or for more than 90 days in any calendar year;

(xiii) fail to honor any provision of any employment agreement Executive has or may in the future have with the Company or fail to honor any provision of this Agreement;

(xiv) give effective notice of an election to terminate at the end of the term or extended the term of any employment agreement Executive has or may in the future have with the Company in accordance with the terms of any such agreement; or

(xv) purport to terminate the Executive's employment by the Company unless notice of that termination shall have been given to the Executive pursuant to, and that notice shall meet the requirements of, Section 6.

Section 6. Notice of Termination. If a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement, any subsequent termination by the Executive or the Company of the Executive's employment by the Company, or any determination of the Executive's Disability, shall be communicated by notice to the other party that shall indicate the specific paragraph of Section 7 pursuant to which the Executive is to receive benefits as a result of the termination. If the notice states that the Executive's employment by the Company has been automatically terminated as a result of the Executive's Disability, the notice shall (i) specifically describe the basis for the determination of the Executive's Disability, and (ii) state the date of the determination of the Executive's Disability, which date shall be not more than ten (10) days before the date such notice is given. If the notice is from the Company and states that the Executive's employment by the Company is terminated by the Company as a result of the occurrence of an Event of Termination for Cause, the notice shall specifically describe the action or inaction of the Executive that the Company believes constitutes an Event of Termination for Cause and shall be accompanied by a copy of the resolution satisfying Section 4. If the notice is from the Executive and states

that the Executive's employment by the Company is terminated by the Executive as a result of the occurrence of an Event of Termination for Good Reason, the notice shall specifically describe the action or inaction of the Company that the Executive believes constitutes an Event of Termination for Good Reason. Each notice given pursuant to this Section 6 (other than a notice stating that the Executive's employment by the Company has been automatically terminated as a result of the Executive's Disability) shall state a date, which shall be not fewer than thirty (30) days nor more than sixty (60) days after the date such notice is given, on which the termination of the Executive's employment by the Company is effective. The date so stated in accordance with this Section 6 shall be the "Termination Date". If a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement, any subsequent purported termination by the Company of the Executive's employment by the Company, or any subsequent purported determination by the Company of the Executive's Disability, shall be ineffective unless that termination or determination shall have been communicated by the Company to the Executive by notice that meets the requirements of the foregoing provisions of this Section 6 and the provisions of Section 9.

Section 7. Benefits Payable on Change in Control and Termination. (a) If (x) a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement, and (y) the Executive's employment by the Company is terminated (whether by the Executive or the Company or automatically as provided in Section 3) after the occurrence of that Change in Control of the Company, the Executive shall be entitled to the following benefits:

(i) If the Executive's employment by the Company is terminated (x) by the Company as a result of the occurrence of an Event of Termination for Cause, or (y) by the Executive before the occurrence of an Event of Termination for Good Reason, then the Company shall pay to the Executive the Base Salary accrued through the Termination Date but not previously paid to the Executive, and the Executive shall be entitled to any other amounts or benefits provided under any plan, policy, practice, program, contract or arrangement of or with the Company, including, but not limited to, the Basic Benefit Plans and the Other Benefit Plans, which shall be governed by the terms thereof (except as explicitly modified by this Agreement).

(ii) If the Executive's employment by the Company is automatically terminated as a result of the Executive's death or the Executive's Disability, then (x) the Company shall pay to the Executive the Base Salary accrued through the date of the occurrence of that event but not previously paid to the Executive, and (y) the Executive shall be entitled to any other amounts or benefits provided under any plan, policy, practice, program, contract or arrangement of or with the Company, including, but not limited to, the Basic Benefit Plans and the Other Benefit Plans, which shall be governed by the terms thereof (except as explicitly modified by this Agreement).

(iii) If the Executive's employment by the Company is terminated (x) by the Company otherwise than as a result of the occurrence of an Event of Termination for Cause, or (y) by the Executive after the occurrence of an Event of Termination for Good Reason, then the Executive shall be entitled to the following:

(1) the Company shall pay to the Executive the Base Salary and compensation for earned but unused vacation time accrued through the Termination Date but not previously paid to the Executive;

(2) the Company shall pay to the Executive an amount equal to the product of (A) the greater of (I) the Executive's target performance bonus for the Fiscal Year in which the Termination Date occurs and (II) the Executive's performance bonus for the Fiscal Year preceding the Fiscal Year in which the Termination Date occurs (including any deferred portion thereof) (the greater of the amounts described in clauses (I) and (II) of this Section 7(a)(iii)(2)(A) being referred to herein as the "Highest Bonus"), and (B) a fraction, the numerator of which is the number of days in the current Fiscal Year through the Termination Date and the denominator of which is 365;

(3) the Company shall pay to the Executive, as a lump sum, an amount (the "Severance Payment") equal to three (3) times the sum of:

(A) the amount (including any deferred portion thereof) of the Base Salary that would have been paid to the Executive during the Fiscal Year in which the Termination Date occurs based on the assumption that the Executive's employment by the Company had continued throughout that Fiscal Year at the Base Salary rate in effect in the Fiscal Year in which the Termination Date occurs, or in the immediately preceding Fiscal Year, whichever is higher;

(B) the amount of the Highest Bonus;

(4) the Company (at its sole expense) shall take the following actions:

(A) throughout the Relevant Period, the Company shall maintain in effect, and not materially reduce the benefits provided by, each of the Other Benefit Plans in which the Executive was a participant immediately before the Termination Date; and

(B) the Company shall arrange for the Executive's uninterrupted participation throughout the Relevant Period in each of such Other Benefit Plans,

provided that if the Executive's participation after the Termination Date in any such Other Benefit Plan is not permitted by the terms of that Other Benefit Plan, then throughout the Relevant Period, the Company (at its sole expense) shall provide the Executive with substantially the same benefits that were provided to the Executive by that Other Benefit Plan immediately before the Termination Date; and

(5) the Executive shall be entitled to any other amounts or benefits provided under any plan, policy, practice, program, contract or arrangement of or with the Company, including, but not limited to, the

Basic Benefit Plans and the Other Benefit Plans, which shall be governed by the terms thereof (except as explicitly modified by this Agreement).

(b) Each payment required to be made to the Executive pursuant to the foregoing provisions of this Section 7(a) above (i) shall be made by check drawn on an account of the Company at a bank located in the United States of America, and (ii) shall be paid (x) if the Executive's employment by the Company was terminated as a result of the Executive's death or the Executive's Disability, not more than thirty (30) days immediately following the date of the occurrence of that event, and (y) if the Executive's employment by the Company was terminated for any other reason, not more than ten (10) days immediately following the Termination Date.

(c) The following shall occur immediately upon the occurrence of a Change in Control of the Company:

(i) all options to acquire Voting Stock and all stock appreciation rights pertaining to Voting Stock held by the Executive immediately prior to a Change in Control of the Company shall become fully exercisable, regardless of whether or not the vesting conditions set forth in the relevant stock option agreements have been satisfied in full; and

(ii) all restrictions on any restricted Voting Stock granted to the Executive prior to a Change in Control of the Company shall be removed and the stock shall be freely transferable, regardless of whether the conditions set forth in the relevant restricted stock agreements have been satisfied in full.

Section 8. Successors. If a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement,

(i) the Company shall not, directly or indirectly, consolidate with, merge into or sell or otherwise transfer its assets as an entirety or substantially as an entirety to, any person, or permit any person to consolidate with or merge into the Company, unless immediately after such consolidation, merger, sale or transfer, the Successor shall have assumed in writing the Company's obligations under this Agreement; and

(ii) not fewer than ten (10) days before the consummation of any consolidation of the Company with, merger by the Company into, or sale or other transfer by the Company of its assets as an entirety or substantially as an entirety to, any person, the Company shall give the Executive notice of that proposed transaction.

Section 9. Notice. Notices required or permitted to be given by either party pursuant to this Agreement shall be in writing and shall be deemed to have been given when delivered personally to the other party or when deposited with the United States Postal Service as certified or registered mail with postage prepaid and addressed:

(i) if to the Executive, at the Executive's address last shown on the Company's records, and



(ii) if to the Company, at 1900 West Loop West, Suite 1500, Houston, Texas 77027, directed to the attention of the Chief Financial Officer.

or, in either case, to such other address as the party to whom or which such notice is to be given shall have specified by notice given to the other party.

Section 10. Withholding Taxes. The Company may withhold from all payments to be paid to the Executive pursuant to this Agreement all taxes that, by applicable federal or state law, the Company is required to so withhold.

Section 11. Certain Additional Payments by the Company.

(a) Anything in this Agreement to the contrary notwithstanding, in the event it shall be determined that any payment or distribution by, or benefit from, the Company or any of its Affiliates to or for the benefit of the Executive, whether paid or payable or distributed or distributable pursuant to the terms of this Agreement or otherwise (any such payments, distributions or benefits being individually referred to herein as a "Payment," and any two or more of such payments, distributions or benefits being referred to herein as "Payments"), would be subject to the excise tax imposed by Section 4999 of the Code (such excise tax, together with any interest thereon, any penalties, additions to tax, or additional amounts with respect to such excise tax, and any interest in respect of such penalties, additions to tax or additional amounts, being collectively referred to herein as the "Excise Tax"), then the Executive shall be entitled to receive an additional payment or payments (individually referred to herein as a "Gross-Up Payment" and any two or more of such additional payments being referred to herein as "Gross-Up Payments") in an amount such that after payment by the Executive of all taxes (as defined in Section 11(k)) imposed upon the Gross-Up Payment, the Executive retains an amount of such Gross-Up Payment equal to the Excise Tax imposed upon the Payments.

(b) Subject to the provisions of Section 11(c) through (i), any determination (individually, a "Determination") required to be made under this Section 11(b), including whether a Gross-Up Payment is required and the amount of such Gross-Up Payment, shall initially be made, at the Company's expense, by nationally recognized tax counsel mutually acceptable to the Company and the Executive ("Tax Counsel"). Tax Counsel shall provide detailed supporting legal authorities, calculations, and documentation both to the Company and the Executive within 15 business days of the termination of the Executive's employment, if applicable, or such other time or times as is reasonably requested by the Company or the Executive. If Tax Counsel makes the initial Determination that no Excise Tax is payable by the Executive with respect to a Payment or Payments, it shall furnish the Executive with an opinion reasonably acceptable to the Executive that no Excise Tax will be imposed with respect to any such Payment or Payments. The Executive shall have the right to dispute any Determination (a "Dispute") within 15 business days after delivery of Tax Counsel's opinion with respect to such Determination. The Gross-Up Payment, if any, as determined pursuant to such Determination shall, at the Company's expense, be paid by the Company to the Executive within five business days of the Executive's receipt of such Determination. The existence of a Dispute shall not in any way affect the Executive's right to receive the Gross-Up Payment in accordance with such Determination. If there is no Dispute, such Determination shall be binding, final and conclusive upon the Company and the Executive, subject in all respects, however, to the provisions of Section 11(c) through (i) below. As a result of the uncertainty in the application of Sections 4999 and 280G of the Code, it is possible that Gross-Up Payments (or portions thereof) which will not have been made by the Company should have been made ("Underpayment"), and if upon any reasonable written request from the Executive or the Company to Tax Counsel, or upon Tax Counsel's own initiative, Tax Counsel, at the Company's expense, thereafter determines that the Executive is required to make a payment of any Excise Tax or any additional Excise Tax,

as the case may be, Tax Counsel shall, at the Company's expense, determine the amount of the Underpayment that has occurred and any such Underpayment shall be promptly paid by the Company to the Executive.

(c) The Company shall defend, hold harmless, and indemnify the Executive on a fully grossed-up after tax basis from and against any and all claims, losses, liabilities, obligations, damages, impositions, assessments, demands, judgements, settlements, costs and expenses (including reasonable attorneys', accountants', and experts' fees and expenses) with respect to any tax liability of the Executive resulting from any Final Determination (as defined in Section 11(j)) that any Payment is subject to the Excise Tax.

(d) If a party hereto receives any written or oral communication with respect to any question, adjustment, assessment or pending or threatened audit, examination, investigation or administrative, court or other proceeding which, if pursued successfully, could result in or give rise to a claim by the Executive against the Company under this Section 11 ("Claim"), including, but not limited to, a claim for indemnification of the Executive by the Company under Section 11(c), then such party shall promptly notify the other party hereto in writing of such Claim ("Tax Claim Notice").

(e) If a Claim is asserted against the Executive ("Executive Claim"), the Executive shall take or cause to be taken such action in connection with contesting such Executive Claim as the Company shall reasonably request in writing from time to time, including the retention of counsel and experts as are reasonably designated by the Company (it being understood and agreed by the parties hereto that the terms of any such retention shall expressly provide that the Company shall be solely responsible for the payment of any and all fees and disbursements of such counsel and any experts) and the execution of powers of attorney, provided that:

(i) within 30 calendar days after the Company receives or delivers, as the case may be, the Tax Claim Notice relating to such Executive Claim (or such earlier date that any payment of the taxes claimed is due from the Executive, but in no event sooner than five calendar days after the Company receives or delivers such Tax Claim Notice), the Company shall have notified the Executive in writing ("Election Notice") that the Company does not dispute its obligations (including, but not limited to, its indemnity obligations) under this Agreement and that the Company elects to contest, and to control the defense or prosecution of, such Executive Claim at the Company's sole risk and sole cost and expense; and

(ii) the Company shall have advanced to the Executive on an interest-free basis, the total amount of the tax claimed in order for the Executive, at the Company's request, to pay or cause to be paid the tax claimed, file a claim for refund of such tax and, subject to the provisions of the last sentence of Section 11(g), sue for a refund of such tax if such claim for refund is disallowed by the appropriate taxing authority (it being understood and agreed by the parties hereto that the Company shall only be entitled to sue for a refund and the Company shall not be entitled to initiate any proceeding in, for example, United States Tax Court) and shall indemnify and hold the Executive harmless, on a fully grossed-up after tax basis, from any tax imposed with respect to such advance or with respect to any imputed income with respect to such advance; and

(iii) the Company shall reimburse the Executive for any and all costs and expenses resulting from any such request by the Company and shall indemnify and hold the Executive harmless, on fully grossed-up after-tax basis, from any tax imposed as a result of such reimbursement.

(f) Subject to the provisions of Section 11(e) hereof, the Company shall have the right to defend or prosecute, at the sole cost, expense and risk of the Company, such Executive Claim by all appropriate proceedings, which proceedings shall be defended or prosecuted diligently by the Company to a Final Determination; provided, however, that (i) the Company shall not, without the Executive's prior written consent, enter into any compromise or settlement of such Executive Claim that would adversely affect the Executive, (ii) any request from the Company to the Executive regarding any extension of the statute of limitations relating to assessment, payment, or collection of taxes for the taxable year of the Executive with respect to which the contested issues involved in, and amount of, the Executive Claim relate is limited solely to such contested issues and amount, and (iii) the Company's control of any contest or proceeding shall be limited to issues with respect to the Executive Claim and the Executive shall be entitled to settle or contest, in his sole and absolute discretion, any other issue raised by the Internal Revenue Service or any other taxing authority. So long as the Company is diligently defending or prosecuting such Executive Claim, the Executive shall provide or cause to be provided to the Company any information reasonably requested by the Company that relates to such Executive Claim, and shall otherwise cooperate with the Company and its representatives in good faith in order to contest effectively such Executive Claim. The Company shall keep the Executive informed of all developments and events relating to any such Executive Claim (including, without limitation, providing to the Executive copies of all written materials pertaining to any such Executive Claim), and the Executive or his authorized representatives shall be entitled, at the Executive's expense, to participate in all conferences, meetings and proceedings relating to any such Executive Claim.

(g) If, after actual receipt by the Executive of an amount of a tax claimed (pursuant to an Executive Claim) that has been advanced by the Company pursuant to Section 11(e)(ii) hereof, the extent of the liability of the Company hereunder with respect to such tax claimed has been established by a Final Determination, the Executive shall promptly pay or cause to be paid to the Company any refund actually received by, or actually credited to, the Executive with respect to such tax (together with any interest paid or credited thereon by the taxing authority and any recovery of legal fees from such taxing authority related thereto), except to the extent that any amounts are then due and payable by the Company to the Executive, whether under the provisions of this Agreement or otherwise. If, after the receipt by the Executive of an amount advanced by the Company pursuant to Section 11(e)(ii), a determination is made by the Internal Revenue Service or other appropriate taxing authority that the Executive shall not be entitled to any refund with respect to such tax claimed and the Company does not notify the Executive in writing of its intent to contest such denial of refund prior to the expiration of 30 days after such determination, then such advance shall be forgiven and shall not be required to be repaid and the amount of such advance shall offset, to the extent thereof, the amount of any Gross-Up Payments and other payments required to be paid hereunder.

(h) With respect to any Executive Claim, if the Company fails to deliver an Election Notice to the Executive within the period provided in Section 11(e)(i) hereof or, after delivery of such Election Notice, the Company fails to comply with the provisions of Section 11(e)(ii) and (iii) and (f) hereof, then the Executive shall at any time thereafter have the right (but not the obligation), at his election and in his sole and absolute discretion, to defend or prosecute, at the sole cost, expense and risk of the Company, such Executive Claim. The Executive shall have full control of such defense or prosecution and such proceedings, including any settlement or compromise thereof. If requested by the Executive, the Company shall cooperate, and shall cause its Affiliates to cooperate, in good faith with the Executive and his authorized representatives in order to contest effectively such Executive Claim. The Company may attend, but not participate in or control, any

defense, prosecution, settlement or compromise of any Executive Claim controlled by the Executive pursuant to this Section 11(h) and shall bear its own costs and expenses with respect thereto. In the case of any Executive Claim that is defended or prosecuted by the Executive, the Executive shall, from time to time, be entitled to current payment, on a fully grossed-up after tax basis, from the Company with respect to costs and expenses incurred by the Executive in connection with such defense or prosecution.

(i) In the case of any Executive Claim that is defended or prosecuted to a Final Determination pursuant to the terms of this Section 11(i), the Company shall pay, on a fully grossed-up after tax basis, to the Executive in immediately available funds the full amount of any taxes arising or resulting from or incurred in connection with such Executive Claim that have not theretofore been paid by the Company to the Executive, together with the costs and expenses, on a fully grossed-up after tax basis, incurred in connection therewith that have not theretofore been paid by the Company to the Executive, within ten calendar days after such Final Determination. In the case of any Executive Claim not covered by the preceding sentence, the Company shall pay, on a fully grossed-up after tax basis, to the Executive in immediately available funds the full amount of any taxes arising or resulting from or incurred in connection with such Executive Claim at least ten calendar days before the date payment of such taxes is due from the Executive, except where payment of such taxes is sooner required under the provisions of this Section 11(i), in which case payment of such taxes (and payment, on a fully grossed-up after tax basis, of any costs and expenses required to be paid under this Section 11(i) shall be made within the time and in the manner otherwise provided in this Section 11(i).

(j) For purposes of this Agreement, the term "Final Determination" shall mean (A) a decision, judgment, decree or other order by a court or other tribunal with appropriate jurisdiction, which has become final and non-appealable; (B) a final and binding settlement or compromise with an administrative agency with appropriate jurisdiction, including, but not limited to, a closing agreement under Section 7121 of the Code; (C) any disallowance of a claim for refund or credit in respect to an overpayment of tax unless a suit is filed on a timely basis; or (D) any final disposition by reason of the expiration of all applicable statutes of limitations.

(k) For purposes of this Agreement, the terms "tax" and "taxes" mean any and all taxes of any kind whatsoever (including, but not limited to, any and all Excise Taxes, income taxes, and employment taxes), together with any interest thereon, any penalties, additions to tax, or additional amounts with respect to such taxes and any interest in respect of such penalties, additions to tax, or additional amounts.

Section 12. Expenses of Enforcement. If a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement, then, upon demand by the Executive made to the Company, the Company shall reimburse the Executive for the reasonable expenses (including attorneys' fees and expenses) incurred by the Executive in enforcing or seeking to enforce the payment of any amount or other benefit to which the Executive shall have become entitled pursuant to this Agreement, including those incurred in connection with any arbitration initiated pursuant to Section 20. To the extent that any such reimbursement would be subject to the Excise Tax, then the Executive shall be entitled to receive Gross-Up Payments in an amount such that after payment by the Executive of all taxes imposed on such Gross-Up Payments, the Executive retains an amount equal to the Excise Tax imposed upon the reimbursement, and the other provisions of Section 11 hereof shall also apply to such circumstance unless the context thereof otherwise indicates.

Section 13. Employment by Wholly Owned Entities. If, at or after the Effective Date, the Executive is or becomes an Executive of one or more corporations, partnerships, limited liability companies or other entities that are, directly or indirectly, wholly owned by the Company ("Wholly Owned Entities"), references in this Agreement to the Executive's employment by the Company shall include the Executive's employment by any such Wholly Owned Entity.

Section 14. No Obligation to Mitigate; No Rights of Offset.

(a) The Executive shall not be required to mitigate the amount of any payment or other benefit required to be paid to the Executive pursuant to this Agreement, whether by seeking other employment or otherwise, nor shall the amount of any such payment or other benefit be reduced on account of any compensation earned by the Executive as a result of employment by another person.

(b) The Company's obligation to make the payments provided for in this Agreement and otherwise to perform its obligations hereunder shall not be affected by any set-off, counterclaim, recoupment, defense or other claim, right or action which the Company may have against the Executive or others.

Section 15. Amendment and Waiver. No provision of this Agreement may be amended or waived (whether by act or course of conduct or omission or otherwise) unless that amendment or waiver is by written instrument signed by the parties hereto. No waiver by either party of any breach of this Agreement shall be deemed a waiver of any other or subsequent breach.

Section 16. Governing Law. The validity, interpretation, construction and enforceability of this Agreement shall be governed by the laws of the State of Texas.

Section 17. Validity. The invalidity or unenforceability of any provision of this Agreement shall not affect the validity or enforceability of any other provision of this Agreement, which shall remain in full force and effect.

Section 18. Counterparts. This Agreement may be executed in counterparts, each of which shall be deemed an original but all of which together will constitute the same instrument.

Section 19. Assignment. This Agreement shall inure to the benefit of and be enforceable by the Executive's legal representative. The Company may not assign any of its obligations under this Agreement unless (i) such assignment is to a Successor and (ii) the requirements of Section 8 are fulfilled.

Section 20. Arbitration. Except as otherwise explicitly provided in Section 11, any dispute between the parties arising out of this Agreement, whether as to this Agreement's construction, interpretation or enforceability or as to any party's breach or alleged breach of any provision of this Agreement, shall be submitted to arbitration in accordance with the following procedures:

(i) Either party may demand such arbitration by giving notice of that demand to the other party. The notice shall state (x) the matter in controversy, and (y) the name of the arbitrator selected by the party giving the notice.

(ii) Not more than 15 days after such notice is given, the other party shall give notice to the party who demanded arbitration of the name of the arbitrator selected by the other party. If the other party shall fail to timely give such notice, the arbitrator that the other party was entitled to select shall be named by the Arbitration Committee of the

American Arbitration Association. Not more than 15 days after the second arbitrator is so named, the two arbitrators shall select a third arbitrator. If the two arbitrators shall fail to timely select a third arbitrator, the third arbitrator shall be named by the Arbitration Committee of the American Arbitration Association.

(iii) The dispute shall be arbitrated at a hearing that shall be concluded within ten days immediately following the date the dispute is submitted to arbitration unless a majority of the arbitrators shall elect to extend the period of arbitration. Any award made by a majority of the arbitrators (x) shall be made within ten days following the conclusion of the arbitration hearing, (y) shall be conclusive and binding on the parties, and (z) may be made the subject of a judgment of any court having jurisdiction.

(iv) All expenses of the arbitration shall be borne by the Company.

The agreement of the parties contained in the foregoing provisions of this Section 20 shall be a complete defense to any action, suit or other proceeding instituted in any court or before any administrative tribunal with respect to any dispute between the parties arising out of this Agreement.

#### Section 21. Interpretation.

(a) As used in this Agreement, the following terms and phrases have the indicated meanings:

(i) "Affiliate" and "Affiliates" mean, when used with respect to any entity, individual, or other person, any other entity, individual, or other person which, directly or indirectly, through one or more intermediaries controls, or is controlled by, or is under common control with such entity, individual or person.

(ii) "Base Salary" has the meaning assigned to that term in Section 5.

(iii) "Basic Benefit Plans" has the meaning assigned to that term in Section 5.

(iv) "Benchmark Bonus" has the meaning assigned to that term in Section 5.

(v) "Board of Directors" means the Board of Directors of the Company.

(vi) "Business Combination" has the meaning assigned to that term in Section 2.

(vii) "Change in Control of the Company" has the meaning assigned to that phrase in Section 2.

(viii) "Claim" has the meaning assigned to such term in Section 11.

(ix) "Code" means the Internal Revenue Code of 1986, as amended from time to time.

(x) "Commission" means the United States Securities and Exchange Commission or any successor agency.

(xi) "Company" has the meaning assigned to that term in the preamble to this Agreement. The term "Company" shall also include any Successor, whether the liability of such Successor under this Agreement is established by contract or occurs by operation of law.

(xii) "Covered Person" has the meaning assigned to that term in Section 2.

(xiii) "Determination" has the meaning assigned to that term in Section 11.

(xiv) "Dispute" has the meaning assigned to that term in Section 11.

(xv) "Effective Date" has the meaning assigned to that term in the preamble to this Agreement.

(xvi) "Election Notice" has the meaning assigned to such term in Section 11.

(xvii) "Executive" has the meaning assigned to such term in the preamble to this Agreement.

(xviii) "Executive Claim" has the meaning assigned to such term in Section 11.

(xix) "Executive's Disability" means:

(A) if no Change in Control of the Company shall have occurred before the date of determination, the physical or mental disability of the Executive determined in accordance with the disability policy of the Company at the time in effect and generally applicable to its salaried Executives; and

(B) if a Change in Control of the Company shall have occurred at that date, the physical or mental disability of the Executive determined in accordance with the disability policy of the Company in effect immediately before the occurrence of the first Change in Control of the Company and generally applicable to its salaried Executives.

The Executive's Disability, and the automatic termination of the Executive's employment by the Company by reason of the Executive's Disability, shall be deemed to have occurred on the date of determination, provided that if (1) a Change in Control of the Company shall have occurred before the expiration of the term of this Agreement, (2) the Company shall have subsequently given notice pursuant to Section 6 of the Company's determination of the Executive's Disability, and (3) the Executive shall have given notice to the Company that the Executive disagrees with that determination, then (A) whether the Executive's Disability shall have occurred shall be submitted to arbitration pursuant to Section 20, and (B) if a majority of the arbitrators decide that the Executive's Disability had not occurred, at the date of determination by the Company, then (I) the Executive's Disability, and the automatic termination of the Executive's employment by the Company by reason of the Executive's Disability, shall be deemed not to have occurred, and (II) on demand by the Executive made to the Company, the Company shall reimburse the Executive for the reasonable expenses (including attorneys' fees and expenses) incurred by the Executive in obtaining that decision.

(xx) "Event of Termination for Good Reason" has the meaning assigned to that phrase in Section 5.

(xxi) "Event of Termination for Cause" has the meaning assigned to that phrase in Section 4.

(xxii) "Exchange Act" means the Securities Exchange Act of 1934, as amended from time to time.

(xxiii) "Excise Tax" has the meaning assigned to that term in Section 11.

(xxiv) "Expiration Date" has the meaning assigned to that term in Section 3.

(xxv) "Final Determination" has the meaning assigned to such term in Section 11.

(xxvi) "Fiscal Year" means the fiscal year of the Company.

(xxvii) "Gross-Up Payment" has the meaning assigned to that term in Section 11.

(xxviii) "Other Benefit Plan" means any employee welfare benefit plan (within the meaning of section 3(1) of the Employee Retirement Income Security Act of 1974, as amended) maintained by the Company.

(xxix) "Outstanding Company Common Stock" has the meaning assigned to that term in Section 2.

(xxx) "Outstanding Company Voting Securities" has the meaning assigned to that term in Section 2.

(xxxi) "Payment" has the meaning assigned to that term in Section 11.

(xxxii) "person" means any individual, corporation, partnership, joint venture, association, joint-stock company, limited partnership, limited liability company, trust, unincorporated organization, government, or agency or political subdivision of any government.

(xxxiii) "Relevant Period" means a period beginning on the Termination Date and ending on the first to occur of (x) the third anniversary of the Termination Date, or (y) the date on which the Executive becomes employed on a full-time basis by another person.

(xxxiv) "Severance Payment" has the meaning assigned to that term in Section 7.

(xxxv) "Successor" means a person with or into which the Company shall have been merged or consolidated or to which the Company shall have transferred its assets as an entirety or substantially as an entirety.

(xxxvi) "Tax" has the meaning assigned to that term in Section 11.



(xxxvii) "Tax Claim Notice" has the meaning assigned to that term in Section 11.

(xxxviii) "Tax Counsel" has the meaning assigned to that term in Section 11.

(xxxix) "Termination Date" has the meaning assigned to that term in Section 6.

(xl) "This Agreement" means this Change in Control Agreement as it may be amended from time to time in accordance with Section 15.

(xli) "Underpayment" has the meaning assigned to that term in Section 11.

(xlii) "Wholly Owned Entities" has the meaning assigned to that term in Section 13.

(b) In the event of the enactment of any successor provision to any statute or rule cited in this Agreement, references in this Agreement to such statute or rule shall be to such successor provision.

(c) The headings of Sections of this Agreement shall not control the meaning or interpretation of this Agreement.

(d) References in this Agreement to any Section are to the corresponding Section of this Agreement unless the context otherwise indicates.

IN WITNESS WHEREOF, the Company and the Executive have executed this Agreement as of the Effective Date.

COMPANY:

QUANEX CORPORATION

By: \_\_\_\_\_  
Name: \_\_\_\_\_  
Title: \_\_\_\_\_

EXECUTIVE:

\_\_\_\_\_  
Name: \_\_\_\_\_

AMENDMENT TO THE  
QUANEX CORPORATION 1987 NON-EMPLOYEE  
DIRECTOR STOCK OPTION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1987 Non-Employee Director Stock Option Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, the Board of Directors of the Company agrees that Section 8 of the Plan is completely amended to provide as follows:

8. TRANSFERABILITY OF OPTIONS. Except as expressly provided otherwise in an Optionee's Agreement, an Option shall not be transferable by the Optionee otherwise than by will or under the laws of descent and distribution, and shall be exercisable, during the Optionee's lifetime, only by him.

AMENDMENT TO  
THE QUANEX CORPORATION  
1987 NON-EMPLOYEE DIRECTOR STOCK OPTION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1987 Non-Employee Director Stock Option Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right in Paragraph 13 of the Plan to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, effective January 1, 2000, the Board of Directors of the Company agrees that Paragraph 9 of the Plan is hereby amended, effective with respect to all Options issued in the future under this Plan, as follows:

9. TERMINATION OR DEATH OF OPTIONEE. Except as may be otherwise expressly provided herein all Options shall terminate on the earlier of the date of the expiration of the Option or the date that is three months after the optionee ceases to be a member of the Company's Board of Directors, for any reason other than the death, permanent disability or, retirement of the optionee, during which period the optionee shall be entitled to exercise the Option in respect of the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Option on the date the optionee ceased to be a member of the Company's Board of Directors.

In the event the optionee ceases to be a member of the Company's Board of Directors because of his death, permanent disability or retirement from the Board of Directors of the Company, before the date of expiration of his Option, such Option shall continue fully in effect, including provisions providing for subsequent vesting of such Option, for a period of not longer than three years commencing on the date of his retirement, and shall terminate on the earlier of the date of the expiration of

such three-year period or the date of expiration of the Option notwithstanding any provision to the contrary in the optionee's Option Agreement. After the death of the optionee, his executors, administrators or any person or persons to whom his Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of the Option to exercise the Option, in respect to the number of shares that the optionee would have been entitled to exercise if he were still alive.

In any event, an Option shall terminate on the tenth anniversary of the date of grant of such Option.

For purposes of this Paragraph 9, an Optionee will be treated as having retired from the Company's Board of Directors if the Optionee shall, at the time the Optionee ceases to be a member of the Board of Directors of the Company, have served at least two full three-year terms of office as a director of the Company or six years of service as a director of the Company.

Dated: December 9, 1999.

AMENDMENT TO THE  
QUANEX CORPORATION 1989 NON-EMPLOYEE  
DIRECTOR STOCK OPTION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1989 Non-Employee Director Stock Option Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, the Board of Directors of the Company agrees that Section 8 of the Plan is completely amended to provide as follows:

8. TRANSFERABILITY OF OPTIONS. Except as expressly provided otherwise in an Optionee's Option Agreement, an Option shall not be transferable by the Optionee otherwise than by will or under the laws of descent and distribution, and shall be exercisable, during the Optionee's lifetime, only by him.

AMENDMENT TO  
THE QUANEX CORPORATION  
1989 NON-EMPLOYEE DIRECTOR STOCK OPTION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1989 Non-Employee Director Stock Option Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right in Section 13 of the Plan to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, effective January 1, 2000, the Board of Directors of the Company agrees that Paragraph 9 of the Plan is hereby amended, effective with respect to all Options issued in the future under this Plan, as follows:

9. TERMINATION OR DEATH OF OPTIONEE. Except as may be otherwise expressly provided herein all Options shall terminate on the earlier of the date of the expiration of the Option or the date that is three months after the optionee ceases to be a member of the Company's Board of Directors, for any reason other than the death, permanent disability or, retirement of the optionee, during which period the optionee shall be entitled to exercise the Option in respect of the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Option on the date the optionee ceased to be a member of the Company's Board of Directors.

In the event the optionee ceases to be a member of the Company's Board of Directors because of his death, permanent disability or retirement from the Board of Directors of the Company, before the date of expiration of his Option, such Option shall continue fully in effect, including provisions providing for subsequent vesting of such Option, for a period of not longer than three years after the date of his death, permanent disability or retirement from the Board of Directors of the Company and

shall terminate on the earlier of the date of the expiration of such three-year period or the date of the expiration of the Option notwithstanding any provision to the contrary in the optionee's Option Agreement. After the death of the optionee, his executors, administrators or any person or persons to whom his Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of the Option to exercise the Option, in respect to the number of shares that the optionee would have been entitled to exercise if he were still alive.

In any event, an Option shall terminate on the tenth anniversary of the date of grant of such Option.

For purposes of this Paragraph 9, an Optionee will be treated as having retired from the Company's Board of Directors if the Optionee shall, at the time the Optionee ceases to be a member of the Board of Directors of the Company, have served at least two full three-year terms of office as a director of the Company or six years of service as a director of the Company.

Dated: December 9, 1999.

AMENDMENT TO THE  
QUANEX CORPORATION EMPLOYEE  
STOCK OPTION AND RESTRICTED STOCK PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation Employee Stock Option and Restricted Stock Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, the Board of Directors of the Company agrees that paragraph G of Section 7 of the Plan is completely amended to provide as follows:

G. TRANSFERABILITY OF OPTIONS. Except as expressly provided otherwise in an Optionee's Agreement with respect to a Non-Incentive Stock Option, an Option shall not be transferable by the Optionee otherwise than by will or under the laws of descent and distribution, and shall be exercisable, during the Optionee's lifetime, only by him.



AMENDMENT TO  
THE QUANEX CORPORATION  
EMPLOYEE STOCK OPTION AND RESTRICTED STOCK PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation Employee Stock Option and Restricted Stock Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right in Section 12 of the Plan to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, effective January 1, 2000, the Board of Directors of the Company agrees that Paragraph H. of Section 7 of the Plan is hereby amended, effective with respect to all Options issued in the future under this Plan, as follows:

H. TERMINATION OF EMPLOYMENT OR DEATH OF OPTIONEE. Except as may be otherwise expressly provided herein with respect to an Option that is a Non-Incentive Stock Option, all Options shall terminate on the earlier of the date of the expiration of the Option or one day less than three months after the date of severance, upon severance of the employment relationship between the Company and the optionee, whether with or without cause, for any reason other than the death, Disability or, in the case of Non-Incentive Stock Options only, Retirement of the optionee, during which period the optionee shall be entitled to exercise the Option in respect of the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Option on the date of such severance of employment. Whether authorized leave of absence, or absence on military or government service, shall constitute severance of the employment relationship between the Company and the optionee shall be determined by the Committee at the time thereof. In the event of severance because of the Disability of the holder of any Incentive Stock Option while in the employ of the Company and before the date of expiration of such Incentive Stock Option, such Incentive Stock Option shall terminate on the earlier

of such date of expiration or one year following the date of such severance because of Disability, during which period the optionee shall be entitled to exercise the Incentive Stock Option in respect to the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Incentive Stock Option on the date of such severance because of Disability. In the event of the death of the holder of any Incentive Stock Option while in the employ of the Company and before the date of expiration of such Incentive Stock Option, such Incentive Stock Option shall terminate on the earlier of such date of expiration or one year following the date of death. After the death of the optionee, his executors, administrators or any person or persons to whom his Incentive Stock Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of an Incentive Stock Option to exercise the Incentive Stock Option, in respect to the number of shares that the optionee would have been entitled to exercise if he had exercised the Incentive Stock Option on the date of his death while in employment. For purposes of Incentive Stock Options issued under this Plan, an employment relationship between the Company and the optionee shall be deemed to exist during any period in which the optionee is employed by the Company, a corporation issuing or assuming an option in a transaction to which Section 424(a) of the Code applies, or a parent or subsidiary corporation of such corporation issuing or assuming an option. For this purpose, the phrase "corporation issuing or assuming an option" shall be substituted for the word "Company" in the definitions of parent and subsidiary corporations in Section 5 and the parent-subsidiary relationship shall be determined at the time of the corporate action described in Section 424(a) of the Code.

In the event of the death, Disability or Retirement of a holder of a Non-Incentive Stock Option, before the date of expiration of such Non-Incentive Stock Option, such Non-Incentive Stock Option shall continue fully in effect, including provisions providing for subsequent vesting of such Option, for a period of not more than three years commencing on the date of the optionee's death, Disability or Retirement and shall terminate on the earlier of the date of the expiration of such three-year period or the date of expiration of the Non-Incentive Stock Option. After the death of the optionee, his executors, administrators or any person or persons to whom his Non-Incentive Stock Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of the Non-Incentive Stock Option to exercise the Non-Incentive Stock Option, in respect to the number of shares that the optionee would have been entitled to exercise if he were still alive. Notwithstanding the foregoing provisions of this Section, in the case of a Non-Incentive Stock Option the Committee may provide for a different option termination date in the Option Agreement with respect to such Option.

Dated: December 9, 1999.

AMENDMENT TO THE  
QUANEX CORPORATION 1996 EMPLOYEE  
STOCK OPTION AND RESTRICTED STOCK PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, the Board of Directors of the Company agrees that paragraph G of Section 7 of the Plan is completely amended to provide as follows:

G. TRANSFERABILITY OF OPTIONS. Except as expressly provided otherwise in an Optionee's Agreement with respect to a Non-Incentive Stock Option, an Option shall not be transferable by the Optionee otherwise than by will or under the laws of descent and distribution, and shall be exercisable, during the Optionee's lifetime, only by him.

AMENDMENT TO  
THE QUANEX CORPORATION  
1996 EMPLOYEE STOCK OPTION AND RESTRICTED STOCK PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1996 Employee Stock Option and Restricted Stock Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right in Section 12 of the Plan to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, effective January 1, 2000, the Board of Directors of the Company agrees that Paragraph H. of Section 7 of the Plan is hereby amended, effective with respect to all Options issued in the future under this Plan, as follows:

H. TERMINATION OF EMPLOYMENT OR DEATH OF OPTIONEE. Except as may be otherwise expressly provided herein with respect to an Option that is a Non-Incentive Stock Option, all Options shall terminate on the earlier of the date of the expiration of the Option or one day less than three months after the date of severance, upon severance of the employment relationship between the Company and the optionee, whether with or without cause, for any reason other than the death, Disability or, in the case of Non-Incentive Stock Options only, Retirement of the optionee, during which period the optionee shall be entitled to exercise the Option in respect of the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Option on the date of such severance of employment. Whether authorized leave of absence, or absence on military or government service, shall constitute severance of the employment relationship between the Company and the optionee shall be determined by the Committee at the time thereof. In the event of severance because of the Disability of the holder of any Incentive Stock Option while in the employ of the Company and before the date of expiration of such Incentive Stock Option, such Incentive Stock Option shall terminate on the earlier

of such date of expiration or one year following the date of such severance because of Disability, during which period the optionee shall be entitled to exercise the Incentive Stock Option in respect to the number of shares that the optionee would have been entitled to purchase had the optionee exercised the Incentive Stock Option on the date of such severance because of Disability. In the event of the death of the holder of any Incentive Stock Option while in the employ of the Company and before the date of expiration of such Incentive Stock Option, such Incentive Stock Option shall terminate on the earlier of such date of expiration or one year following the date of death. After the death of the optionee, his executors, administrators or any person or persons to whom his Incentive Stock Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of an Incentive Stock Option to exercise the Incentive Stock Option, in respect to the number of shares that the optionee would have been entitled to exercise if he had exercised the Incentive Stock Option on the date of his death while in employment. For purposes of Incentive Stock Options issued under this Plan, an employment relationship between the Company and the optionee shall be deemed to exist during any period in which the optionee is employed by the Company, a corporation issuing or assuming an option in a transaction to which Section 424(a) of the Code applies, or a parent or subsidiary corporation of such corporation issuing or assuming an option. For this purpose, the phrase "corporation issuing or assuming an option" shall be substituted for the word "Company" in the definitions of parent and subsidiary corporations in Section 5 and the parent-subsidiary relationship shall be determined at the time of the corporate action described in Section 424(a) of the Code.

In the event of the death, Disability or Retirement of a holder of a Non-Incentive Stock Option, before the date of expiration of such Non-Incentive Stock Option, such Non-Incentive Stock Option shall continue fully in effect, including provisions providing for subsequent vesting of such Option, for a period of not more than three years commencing on the date of the optionee's death, Disability or Retirement and shall terminate on the earlier of the date of the expiration of such three-year period or the date of expiration of the Non-Incentive Stock Option. After the death of the optionee, his executors, administrators or any person or persons to whom his Non-Incentive Stock Option may be transferred by will or by the laws of descent and distribution, shall have the right, at any time prior to the termination of the Non-Incentive Stock Option to exercise the Non-Incentive Stock Option, in respect to the number of shares that the optionee would have been entitled to exercise if he were still alive. Notwithstanding the foregoing provisions of this Section, in the case of a Non-Incentive Stock Option the Committee may provide for a different option termination date in the Option Agreement with respect to such Option.

Dated: December 9, 1999.

APPOINTMENT OF THE TRUSTEE OF THE  
QUANEX CORPORATION DEFERRED COMPENSATION TRUST  
AND THE AMENDMENT OF THE QUANEX CORPORATION  
DEFERRED COMPENSATION TRUST

RESOLVED, that pursuant to the power retained by Quanex Corporation (the "Company") in Section 11 of that certain Trust Agreement dated August 1, 1996, by the Company, entitled "Quanex Corporation Deferred Compensation Trust," the Company hereby appoints Fleet Bank N.A. as successor Trustee of the Trust, and the proper officers of the Company are hereby authorized and directed to execute such documents as are necessary to make such appointment effective as of the end of business on December 9, 1999; and

RESOLVED FURTHER, that the Trust Agreement be amended, effective as of the effective date of the appointment of successor Trustee, as follows:

1. The words "NBD Bank" shall be deleted in the Trust Agreement, and the words "Fleet Bank N.A." shall be substituted in their stead.
2. Section 13.(c) of the Trust Agreement shall be amended in its entirety as follows:

(c) This Trust Agreement shall be governed by and construed in accordance with the laws of the State of New York.

AMENDMENT TO  
THE QUANEX CORPORATION  
1997 NON-EMPLOYEE DIRECTOR STOCK OPTION PLAN

THIS AGREEMENT by Quanex Corporation (the "Company"),

W I T N E S S E T H:

WHEREAS, the Board of Directors of the Company previously adopted the plan agreement known as the "Quanex Corporation 1997 Non-Employee Director Stock Option Plan" (the "Plan"); and

WHEREAS, the Board of Directors of the Company retained the right in Article IV of the Plan to amend the Plan from time to time; and

WHEREAS, the Board of Directors of the Company has approved the following amendment to the Plan;

NOW, THEREFORE, effective January 1, 2000, the Board of Directors of the Company agrees that Section 3.6 the Plan is hereby amended, effective with respect to all Options issued in the future under this Plan, as follows:

3.6 DURATION OF OPTIONS.

Each Option awarded, to the extent it shall not previously have been exercised, shall terminate on the earlier of the following dates:

(i) on the last day within the three month period commencing on the date on which the Optionee ceases to be a director of the Company, for any reason other than death, Retirement or Disability; or

(ii) ten years after the date of grant of such Option.

If the Optionee ceases to be a director of the Company due to his death, Disability or Retirement, his Option shall continue to vest after such cessation of service as a director for a period of not longer than three years commencing on the

date of the Optionee's death, disability or Retirement until the Option expires upon the earlier of date of the expiration of such three-year period or ten years after the grant of the Option.

Dated: December 9, 1999.



## SUBSIDIARIES OF QUANEX CORPORATION

## JURISDICTION OF INCORPORATION

Piper Impact, Inc.	Delaware
Quanex Bar, Inc.	Delaware
Quanex Steel, Inc.	Delaware
Quanex Health Management Company, Inc.	Delaware
Quanex Manufacturing, Inc.	Delaware
Quanex Solutions, Inc.	Delaware
Quanex Technologies, Inc.	Delaware
Quanex Foreign Sales Corporation	U.S. Virgin Islands
Piper Impact Europe B.V.	The Netherlands
Nichols Aluminum-Alabama, Inc.	Delaware
Quanex Windows, Inc.	Delaware
Quanex Two, Inc.	Delaware
Quanex Three, Inc.	Delaware
Quanex Four, Inc.	Delaware
Quanex Five, Inc.	Delaware
Quanex Six, Inc.	Delaware

## INDEPENDENT AUDITORS' CONSENT

We consent to the incorporation by reference in Registration Statements No. 33-23474, No. 33-29585, No. 33-22550, No. 33-35128, No. 33-38702, No. 33-46824, No. 33-57235, No. 33-54081, No. 33-54085, No. 33-54087, No. 333-18267, No. 333-22977, No. 333-36635, No. 333-89853 and No. 333-66777 of Quanex Corporation of our report dated November 19, 1999 appearing in this Annual Report on Form 10-K of Quanex Corporation for the year ended October 31, 1999.

/s/ Deloitte & Touche LLP

Houston, Texas  
January 7, 2000

THIS SCHEDULE CONTAINS SUMMARY FINANCIAL INFORMATION EXTRACTED FROM THE BALANCE SHEET AS OF OCTOBER 31, 1999 AND THE INCOME STATEMENT FOR THE YEAR ENDED OCTOBER 31, 1999 AND IS QUALIFIED IN ITS ENTIRETY BY REFERENCE TO SUCH FINANCIAL STATEMENTS.

1,000

YEAR	
	OCT-31-1999
	NOV-01-1998
	OCT-31-1999
	25,874
	0
	87,204
	12,154
	78,463
	212,387
	753,811
	346,970
	690,446
136,140	
	179,121
0	
	0
	7,135
690,446	293,926
	810,094
	810,094
	738,337
	738,337
	0
	921
14,402	
	60,349
	21,048
39,301	
	0
	415
	0
	39,716
	2.790
	2.590