

LAWSON PRODUCTS INC/NEW/DE/

Form 10-Q

April 30, 2009

**Table of Contents**

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

**(Mark One)**

**Quarterly Report under Section 13 OR 15(d) of the Securities Exchange Act of 1934  
For quarterly period ended March 31, 2009**

**or**

**Transition Report under Section 13 OR 15(d) of the Securities Exchange Act of 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file Number: 0-10546**

**LAWSON PRODUCTS, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**

**36-2229304**

(State or other jurisdiction of  
incorporation or organization)

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

**1666 East Touhy Avenue, Des Plaines, Illinois**

**60018**

(Address of principal executive offices)

(Zip Code)

**(847) 827-9666**

(Registrant's telephone number, including area code)

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

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

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

The number of shares outstanding of the registrant's common stock, \$1 par value, as of April 17, 2009 was 8,522,001.

**Table of Contents**

**Safe Harbor Statement under the Securities Litigation Reform Act of 1995:**

This Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that involve risks and uncertainties. The terms may, should, could, anticipate, believe, continues, estimate, expect, intend, objective, plan, potential, project and similar are intended to identify forward-looking statements. These statements are not guarantees of future performance and involve risks, uncertainties and assumptions that are difficult to predict. These statements are based on management's current expectations, intentions or beliefs and are subject to a number of factors, assumptions and uncertainties that could cause actual results to differ materially from those described in the forward-looking statements. Factors that could cause or contribute to such differences or that might otherwise impact the business include any breach of the terms and conditions of the Deferred Prosecution Agreement with U.S. Attorney's Office for the Northern District of Illinois; excess and obsolete inventory; disruptions of the Company's information systems; risks of rescheduled or cancelled orders; increases in commodity prices; the influence of controlling stockholders; competition and competitive pricing pressures; the effect of general economic conditions and market conditions in the markets and industries the Company serves; the risks of war, terrorism, and similar hostilities; and, all of the factors discussed in the Company's Risk Factors set forth in its Annual Report on Form 10-K for the year ended December 31, 2008 and in this Quarterly Report on Form 10-Q.

The Company undertakes no obligation to update any such factor or to publicly announce the results of any revisions to any forward-looking statements contained herein whether as a result of new information, future events or otherwise.

**TABLE OF CONTENTS**

|   | Page # |
|---|--------|
| <b><u>PART I FINANCIAL INFORMATION</u></b>  |        |
| <u>Item 1 Condensed Consolidated Financial Statements</u>   | 4      |
| <u>Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 12     |
| <u>Item 3 Quantitative and Qualitative Disclosures about Market Risk</u>                            | 14     |
| <u>Item 4 Controls and Procedures</u>   | 14     |
| <b><u>PART II OTHER INFORMATION</u></b>   |        |
| <u>Item 6 Exhibits</u>  | 14     |
| <b><u>SIGNATURES</u></b>  |        |
| <u>Exhibit 15</u>   |        |
| <u>Exhibit 31.1</u>   |        |
| <u>Exhibit 31.2</u>   |        |
| <u>Exhibit 32</u>   |        |

**Table of Contents**

**PART I FINANCIAL INFORMATION**  
**ITEM 1 CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**Lawson Products, Inc. and Subsidiaries**  
**Condensed Consolidated Balance Sheets**

| (Amounts in thousands, except share data)                                     | March 31,<br>2009<br>(Unaudited) | December 31,<br>2008 |
|---|----------------------------------|----------------------|
| <b>ASSETS</b>   |                                  |                      |
| <b>Current assets:</b>  |                                  |                      |
| Cash and cash equivalents   | \$ 8,255                         | \$ 4,300             |
| Accounts receivable, less allowance for doubtful accounts                     | 43,423                           | 48,634               |
| Inventories   | 82,389                           | 86,435               |
| Miscellaneous receivables and prepaid expenses                                | 13,383                           | 11,812               |
| Deferred income taxes   | 6,454                            | 6,127                |
| Property held for sale  | 1,799                            |                      |
| Discontinued assets   | 329                              | 296                  |
| <b>Total current assets</b>   | <b>156,032</b>                   | <b>157,604</b>       |
| Property, plant and equipment, less accumulated depreciation and amortization | 44,812                           | 47,783               |
| Cash value of life insurance  | 16,840                           | 17,970               |
| Deferred income taxes   | 18,154                           | 18,159               |
| Goodwill  | 26,876                           | 25,748               |
| Other assets  | 3,831                            | 3,732                |
| <b>Total assets</b>   | <b>\$ 266,545</b>                | <b>\$ 270,996</b>    |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>                                    |                                  |                      |
| <b>Current liabilities:</b>   |                                  |                      |
| Accounts payable  | \$ 18,988                        | \$ 16,334            |
| Settlement payable - current  | 10,000                           | 10,000               |
| Accrued expenses and other liabilities  | 33,418                           | 41,205               |
| Discontinued current liabilities  | 59                               | 53                   |
| <b>Total current liabilities</b>  | <b>62,465</b>                    | <b>67,592</b>        |
| Revolving line of credit  | 13,050                           | 7,700                |
| Security bonus plan   | 25,832                           | 26,218               |
| Deferred compensation   | 11,837                           | 11,301               |
| Settlement payable - noncurrent   | 10,000                           | 10,000               |
| Other   | 10,332                           | 9,441                |

|  |                   |                   |
|--|-------------------|-------------------|
|  | 71,051            | 64,660            |
| <b>Stockholders equity:</b>                          |                   |                   |
| Preferred stock, \$1 par value:                      |                   |                   |
| Authorized 500,000 shares, Issued and outstanding    | None              |                   |
| Common stock, \$1 par value:                         |                   |                   |
| Authorized 35,000,000 shares, Issued and outstanding | 8,522,001 shares  |                   |
| Capital in excess of par value                       | 8,522             | 8,522             |
|  | 4,774             | 4,774             |
| Retained earnings                                    | 119,954           | 126,158           |
| Accumulated other comprehensive loss                 | (221)             | (710)             |
| <b>Stockholders equity:</b>                          | <b>133,029</b>    | <b>138,744</b>    |
| <b>Total liabilities and stockholders equity</b>     | <b>\$ 266,545</b> | <b>\$ 270,996</b> |

See notes to condensed consolidated financial statements.

**Table of Contents**

**Lawson Products, Inc. and Subsidiaries**  
**Condensed Consolidated Statements of Operations**  
**(Unaudited)**

| (Amounts in thousands, except per share data)                | Three Months Ended March 31, |                 |
|--|------------------------------|-----------------|
|  | 2009                         | 2008            |
| Net sales  | \$ 99,381                    | \$ 125,870      |
| Cost of goods sold   | 45,214                       | 51,742          |
| <b>Gross profit</b>  | <b>54,167</b>                | <b>74,128</b>   |
| <b>Operating expenses:</b>                                   |                              |                 |
| Selling, general and administrative expenses                 | 56,632                       | 64,828          |
| Severance and other charges                                  | 6,452                        | 602             |
| Settlement related costs                                     | 49                           | 751             |
| <b>Operating (loss) income</b>                               | <b>(8,966)</b>               | <b>7,947</b>    |
| Other income   | 725                          | 108             |
| Interest expense   | (74)                         | (229)           |
| (Loss) income from continuing operations before income taxes | (8,315)                      | 7,826           |
| Income tax (benefit) provision                               | (2,396)                      | 3,302           |
| <b>(Loss) income from continuing operations</b>              | <b>(5,919)</b>               | <b>4,524</b>    |
| Loss from discontinued operations, net of income taxes       | (29)                         | (155)           |
| <b>Net (loss) income</b>                                     | <b>\$ (5,948)</b>            | <b>\$ 4,369</b> |
| <b>Basic (loss) income per share of common stock:</b>        |                              |                 |
| Continuing operations  | \$ (0.70)                    | \$ 0.53         |
| Discontinued operations                                      |                              | (0.02)          |
|  | \$ (0.70)                    | \$ 0.51         |
| <b>Diluted (loss) income per share of common stock:</b>      |                              |                 |
| Continuing operations  | \$ (0.70)                    | \$ 0.53         |
| Discontinued operations                                      |                              | (0.02)          |
|  | \$ (0.70)                    | \$ 0.51         |

|   |    |       |    |       |
|---|----|-------|----|-------|
| Cash dividends declared per share of common stock | \$ | 0.03  | \$ | 0.20  |
| Weighted average shares outstanding:              |    |       |    |       |
| Basic   |    | 8,522 |    | 8,522 |
| Diluted   |    | 8,522 |    | 8,523 |

See notes to condensed consolidated financial statements.



**Table of Contents**

**Lawson Products, Inc. and Subsidiaries**  
**Condensed Consolidated Statements of Cash Flows**  
**(Unaudited)**

| (Amounts in thousands)   | Three Months Ended March 31, |                 |
|--|------------------------------|-----------------|
|  | 2009                         | 2008            |
| <b>Operating activities:</b>   |                              |                 |
| Net (loss) income  | \$ (5,948)                   | \$ 4,369        |
| Adjustments to reconcile net (loss) income to net cash provided by operating activities: |                              |                 |
| Depreciation and amortization  | 1,864                        | 2,142           |
| Loss from write-down of property, plant and equipment                                    | 411                          |                 |
| Changes in operating assets and liabilities  | 6,944                        | (5,006)         |
| Other  | (1,612)                      | (2,234)         |
| <b>Net cash provided by (used for) operating activities</b>                              | <b>1,659</b>                 | <b>(729)</b>    |
| <b>Investing activities:</b>   |                              |                 |
| Additions to property, plant and equipment   | (1,150)                      | (1,206)         |
| <b>Net cash used for investing activities</b>  | <b>(1,150)</b>               | <b>(1,206)</b>  |
| <b>Financing activities:</b>   |                              |                 |
| Net proceeds from revolving line of credit   | 5,350                        | 4,500           |
| Dividends paid   | (1,704)                      | (1,704)         |
| Other  | (178)                        |                 |
| <b>Net cash provided by financing activities</b>   | <b>3,468</b>                 | <b>2,796</b>    |
| <b>Increase in cash and cash equivalents</b>   | <b>3,977</b>                 | <b>861</b>      |
| Cash and cash equivalents at beginning of period   | 4,581                        | 2,473           |
| Cash and cash equivalents at end of period   | 8,558                        | 3,334           |
| Cash held by discontinued operations   | (303)                        | (785)           |
| <b>Cash and cash equivalents held by continuing operations at end of period</b>          | <b>\$ 8,255</b>              | <b>\$ 2,549</b> |

See notes to condensed consolidated financial statements.



**Table of Contents**

**Lawson Products, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**  
(Dollars in Thousands, except per share data)

**Note A Basis of Presentation and Summary of Significant Accounting Policies**

The accompanying condensed consolidated financial statements of Lawson Products, Inc. (the Company) have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information, the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not contain all disclosures required by U.S. generally accepted accounting principles. Reference should be made to the Company's Annual Report on Form 10-K for the year ended December 31, 2008. The Condensed Consolidated Balance Sheet as of March 31, 2009, the Condensed Consolidated Statements of Operations for the three-month periods ended March 31, 2009 and 2008 and the Condensed Consolidated Statements of Cash Flows for the three-month periods ended March 31, 2009 and 2008 are unaudited. In the opinion of the Company, all normal recurring adjustments have been made, that are necessary to present fairly the results of operations for the interim periods. Operating results for the three-month period ended March 31, 2009 are not necessarily indicative of the results that may be expected for the year ending December 31, 2009.

There have been no material changes in our significant accounting policies during the three months ended March 31, 2009 as compared to the significant accounting policies described in our Annual Report on Form 10-K for the year ended December 31, 2008.

**Note B Fair Value Measurements**

The Company adopted FASB Statement of Financial Accounting Standards No. 157 (SFAS No. 157), *Fair Value Measurements*, effective January 1, 2009 for our financial assets and liabilities. Adoption of SFAS No. 157 did not have a material effect on our financial position, results of operations or cash flows. SFAS No. 157 requires the categorization of financial assets and liabilities, based on the inputs to the valuation technique, into a three-level fair value hierarchy. The fair value hierarchy gives the highest priority to the quoted prices in active markets for identical assets and liabilities and lowest priority to unobservable inputs. The various levels of the SFAS No. 157 fair value hierarchy are described as follows:

- Level 1 Financial assets and liabilities valued based on unadjusted quoted market prices for identical assets and liabilities in an active market that the company has the ability to access.
- Level 2 Financial assets and liabilities valued based on quoted prices in markets that are not active or model inputs that are observable for substantially the full term of the asset or liability.
- Level 3 Financial assets and liabilities valued based on prices or valuation techniques that require inputs that are both unobservable and significant to the overall fair value measurement.

The following table presents the fair value hierarchy for those assets and liabilities measured at fair value on a recurring basis as of March 31, 2009:

|                              | Level 1   | Level 2 | Level 3 | Total     |
|------------------------------|-----------|---------|---------|-----------|
| <b>Assets:</b>               |           |         |         |           |
| Cash value of life insurance | \$ 16,840 | \$      | \$      | \$ 16,840 |
| <b>Liabilities:</b>          |           |         |         |           |
| Deferred compensation        | \$ 11,837 | \$      | \$      | \$ 11,837 |

**Table of Contents**

**Lawson Products, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**  
(Dollars in Thousands, except per share data)

**Note C Inventories**

Components of inventories were as follows:

| (Amounts in thousands)                    | March 31,<br>2009 | December 31,<br>2008 |
|---|-------------------|----------------------|
| Finished goods                            | \$ 90,216         | \$ 92,565            |
| Work in progress                          | 2,024             | 1,791                |
| Raw materials                             | 2,082             | 2,146                |
| <br>Total                                 | <br>94,322        | <br>96,502           |
| Reserve for obsolete and excess inventory | (11,933)          | (10,067)             |
|   | \$ 82,389         | \$ 86,435            |

**Note D Property Held for Sale**

During the first quarter of 2009, the Company closed and began to actively market its Charlotte, North Carolina distribution center. The net book value of \$1,799 has been reclassified to Property held for sale in the Condensed Consolidated Balance Sheets. The property is valued at the lower of carrying amount or estimated net realizable value (proceeds less cost to sell), and will not be depreciated after being classified as held for sale.

**Note E Reserve for Severance and Restructuring**

During the first quarter of 2009 the Company committed to implementing certain cost reduction measures in response to current economic conditions. These cost reduction measures include a reduction in force of approximately 11%, or approximately 150 employees, across the organization and the closure of its Dallas, Texas and Charlotte, North Carolina distribution centers. The reduction in force and closure of the distribution centers are expected to be substantially complete by the end of the second quarter. As a result of these measures, the Company incurred a charge of \$6,452 in the first quarter of 2009, primarily related to the Maintenance, Repair and Operations ( MRO ) segment. Of this amount, \$5,989 related to future cash payments related to terminated employees, \$411 related to a non-cash charge for disposal of property, plant and equipment and other expenses of \$52.

The table below shows the changes in the Company's reserves for severance and related payments, included in accrued expenses and other liabilities on the balance sheet as of March 31, 2009 and 2008:

| (Amounts in thousands)       | Three Months Ended March 31, |              |
|------------------------------|------------------------------|--------------|
|                              | 2009                         | 2008         |
| Balance at beginning of year | \$ 6,111                     | \$ 7,058     |
| Charged to earnings          | 5,989                        | 602          |
| Cash paid                    | (1,849)                      | (1,315)      |
| Adjustment to reserve        |                              | (42)         |
| <br>Balance at end of year   | <br>\$ 10,251                | <br>\$ 6,303 |

**Table of Contents**

**Lawson Products, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**  
(Dollars in Thousands, except per share data)

**Note F Comprehensive (Loss) Income**

Components of comprehensive (loss) income for the three months ended March 31, 2009 and 2008 are as follows:

| (Amounts in thousands)                  | Three Months Ended March 31, |          |
|---|------------------------------|----------|
|   | 2009                         | 2008     |
| Net (loss) income                       | \$ (5,948)                   | \$ 4,369 |
| Foreign currency translation adjustment | 489                          | (191)    |
| Comprehensive (loss) income             | \$ (5,459)                   | \$ 4,178 |

**Note G Stock Performance Rights**

During the first quarter of 2009, 5,000 SPRs were granted with an exercise price of \$19.62. A compensation benefit of \$734 and \$1,202 was recorded for outstanding SPRs in selling, general and administrative expenses in the first quarters of 2009 and 2008, respectively. The fair value of outstanding SPRs was remeasured on March 31, 2009 using the Black-Scholes valuation model. This model requires the input of the following subjective assumptions that may have a significant impact on the fair value estimate:

|                          |                 |
|--------------------------|-----------------|
| Expected volatility      | 52.7% to 101.7% |
| Risk-free interest rate  | 0.6% to 1.8%    |
| Expected term (in years) | 0.9 to 5.9      |
| Expected annual dividend | \$0.12          |

**Note H Earnings Per Share**

The calculations of dilutive weighted average shares outstanding for the three months ended March 31, 2009 and 2008 were as follows:

| (Amounts in thousands)                       | Three Months Ended March 31, |          |
|--|------------------------------|----------|
|  | 2009                         | 2008     |
| Basic weighted average shares outstanding    | \$ 8,522                     | \$ 8,522 |
| Dilutive impact of stock options outstanding |                              | 1        |
| Dilutive weighted average shares outstanding | \$ 8,522                     | \$ 8,523 |

Stock options outstanding for the three months ended March 31, 2009, would have been anti-dilutive and therefore were excluded from the computation of diluted earnings per share.

**Table of Contents**

**Lawson Products, Inc. and Subsidiaries**  
**Notes to Condensed Consolidated Financial Statements**  
(Dollars in Thousands, except per share data)

**Note I Segment Reporting**

The Company conducts business in two reportable segments: MRO and Original Equipment Marketplace ( OEM ). The Company's MRO segment is a distributor and marketer of systems, services and products to the industrial, commercial, institutional, and governmental maintenance repair and operations marketplace. The Company's OEM segment manufactures, sells and distributes production and specialized component parts to the original equipment marketplace. The Company's two reportable segments are distinguished by the nature of products distributed and sold, types of customers and manner of servicing them. The Company evaluates performance and allocates resources to reportable segments primarily based on operating income.

The following table presents summary financial information for the Company's reportable segments:

| (Amounts in thousands)                                       | Three Months Ended March 31, |            |
|--|------------------------------|------------|
|  | 2009                         | 2008       |
| Net sales  |                              |            |
| MRO  | \$ 82,819                    | \$ 105,404 |
| OEM  | 16,562                       | 20,466     |
| Consolidated total   | \$ 99,381                    | \$ 125,870 |
| Operating (loss) income                                      |                              |            |
| MRO  | \$ (953)                     | \$ 8,847   |
| OEM  | (1,512)                      | 453        |
| Severance and other charges                                  | (6,452)                      | (602)      |
| Settlement related costs                                     | (49)                         | (751)      |
| Consolidated total   | (8,966)                      | 7,947      |
| Other income   | 725                          | 108        |
| Interest expense   | (74)                         | (229)      |
| (Loss) income from continuing operations before income taxes | \$ (8,315)                   | \$ 7,826   |

**Note J Income Tax (Benefit) Expense**

Income tax as a percentage of pre-tax (loss) income for the three months ended March 31, 2009 was 28.8% compared to 42.2% for the three months ended March 31, 2008. The primary reason for the change in the tax rates is the effect of non-deductible expenses, including the decrease in the cash surrender value of executive life insurance, which increases the rate of tax expenses resulting from income while reducing the rate of tax benefits from losses. Additionally, earnings in jurisdictions with higher tax rates decreased the net income tax benefit in relation to the overall pre-tax loss.

At March 31, 2009, the Company had \$3,040 in unrecognized tax benefits, the recognition of which would have a favorable effect on the effective tax rate. Due to the uncertainty of both timing and resolution of income tax examinations, the Company is unable to determine whether any amounts included in the March 31, 2009 balance of unrecognized tax benefits represent tax positions that could significantly change during the next twelve months.

The Company recognizes interest and penalties related to unrecognized tax benefits in income tax (benefit) expense. The Company had \$1,877 accrued for interest and penalties at March 31, 2009.

The Company and its subsidiaries are subject to U.S. Federal income tax as well as income tax of multiple state and international jurisdictions. As of March 31, 2009, the Company is subject to U.S. Federal and non-U.S. income tax examinations for the years 2000 through 2007.

**Table of Contents**

**Report of Independent Registered Public Accounting Firm**

Board of Directors and Stockholders

Lawson Products, Inc.

We have reviewed the condensed consolidated balance sheet of Lawson Products, Inc. and subsidiaries as of March 31, 2009 and the related condensed consolidated statements of operations for the three month periods ended March 31, 2009 and 2008 and the related condensed consolidated statements of cash flows for the three month periods ended March 31, 2009 and 2008. These financial statements are the responsibility of the Company's management.

We conducted our review in accordance with standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with U.S. generally accepted accounting principles.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Lawson Products, Inc. and subsidiaries as of December 31, 2008, and the related consolidated statements of operations, changes in stockholders' equity and cash flows for the year then ended, not presented herein, and in our report dated March 11, 2009, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2008, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

ERNST & YOUNG LLP

Chicago, Illinois

April 28, 2009



**Table of Contents****ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following table presents a summary of the Company's financial performance for the first quarter of 2009 and 2008:

|   | 2009       |                   | 2008       |                   |
|---|------------|-------------------|------------|-------------------|
|   | Amount     | % of<br>Net Sales | Amount     | % of<br>Net Sales |
| Net sales   |            |                   |            |                   |
| MRO   | \$ 82,819  | 83.3%             | \$ 105,404 | 83.7%             |
| OEM   | 16,562     | 16.7              | 20,466     | 16.3              |
| Consolidated total  | \$ 99,381  | 100.0             | \$ 125,870 | 100.0             |
| Gross profit  |            |                   |            |                   |
| MRO   | \$ 51,565  | 62.3%             | \$ 69,719  | 66.1%             |
| OEM   | 2,602      | 15.7              | 4,409      | 21.5              |
| Consolidated total  | 54,167     | 54.5              | 74,128     | 58.9              |
| Operating expenses:   |            |                   |            |                   |
| Selling, general and administrative expenses                          | 56,632     | 57.0              | 64,828     | 51.5              |
| Severance and other charges   | 6,452      | 6.5               | 602        | 0.5               |
| Settlement related costs  | 49         |                   | 751        | 0.6               |
| Operating (loss) income   | (8,966)    | (9.0)             | 7,947      | 6.3               |
| Other, net  | 651        | 0.6               | (121)      | (0.1)             |
| (Loss) income from continuing operations before<br>income tax expense | (8,315)    | (8.4)             | 7,826      | 6.2               |
| Income tax (benefit) expense  | (2,396)    | (2.4)             | 3,302      | 2.6               |
| Loss (income) from continuing operations                              | \$ (5,919) | (6.0)%            | \$ 4,524   | 3.6%              |

*Net Sales*

Net sales for the three-month period ended March 31, 2009 decreased 21.0% to \$99.4 million, from \$125.9 million in the same period of 2008 as the global economic recession and contraction in the credit markets led to decreased customer demand throughout our industry. The duration of the recession is uncertain and industry demand may continue to decline and create downward pressure on sales volume throughout 2009.

The sales decline was reflected in both the MRO and the OEM segments. MRO net sales decreased \$22.6 million or 21.4% in the first quarter of 2009, to \$82.8 million from \$105.4 million in the prior year period. OEM net sales decreased \$3.9 million or 19.1% in the first quarter of 2009, to \$16.6 million from \$20.5 million in the prior year period.

*Gross Profit*

Gross profit decreased \$19.9 million in the first quarter of 2009, to \$54.2 million from \$74.1 million in the prior year period. The gross profit margin for the first quarter of 2009 was 54.5%, 4.4 percentage points lower than the 58.9% achieved in the first quarter of 2008. MRO gross profit decreased \$18.1 million in the first quarter of 2009, to \$51.6 million from \$69.7 million in the prior year period. MRO gross profit as a percent of net sales decreased to 62.3% for the first quarter of 2009 from 66.1% in the first quarter of 2008. OEM gross profit decreased \$1.8 million in the first quarter of 2009, to \$2.6 million from \$4.4 million in the prior year period. Gross profit as a percent of net sales decreased to 15.7% for the first quarter of 2009 from 21.5% in the first quarter of 2008. The decreases recorded in both segments were primarily due to an increasingly competitive pricing environment, a change in the sales mix to lower margin products and an increase in inventory reserves.

**Table of Contents**

*Selling, General and Administrative Expenses ( SG&A )*

SG&A expenses were \$56.6 million or 57.0% of net sales and \$64.8million or 51.5% of net sales for the quarters ended March 31, 2009 and 2008, respectively. The \$8.2 million reduction in the first quarter of 2009 primarily reflects lower compensation expenses including sales commission. SG&A as a percent of net sales increased 5.5 percentage points in the first quarter of 2009 compared to the first quarter of 2008 as fixed costs were not reduced in proportion to the overall decrease in net sales.

*Severance and Other Charges*

During the first quarter of 2009 the Company committed to implementing certain cost reduction measures in response to current economic conditions. These cost reduction measures include a reduction in force of approximately 11%, or approximately 150 employees, across the organization and the closure of its Dallas, Texas and Charlotte, North Carolina distribution centers. The reduction in force and closure of the distribution centers are expected to be substantially complete by the end of the second quarter. As a result of these measures, the Company incurred a charge of \$6.4 million in the first quarter of 2009. Of this amount, \$6.0 million related to payments of terminated employees and \$0.4 million related to a non-cash charge for disposal of property, plant and equipment. These cost reduction measures are expected to result in future annualized cost savings of between \$10.0 million and \$12.0 million.

*Income Tax Expense*

For the three months ended March 31, 2009, the Company recorded \$2.4 million of income tax benefit, based on a pre-tax loss from continuing operations of \$8.3 million, resulting in an effective tax rate of 28.8%. For the three months ended March 31, 2008, income tax expense of \$3.3 million was recorded based on pre-tax income of \$7.8 million, resulting in an effective tax rate of 42.2%. The primary reason for the change in the tax rates is the effect of non-deductible expenses, including the decrease in the cash surrender value of executive life insurance, which increase the rate of tax expenses resulting from income while reducing the rate of tax benefits from losses. Additionally, earnings in jurisdictions with higher tax rates decreased the net income tax benefit in relation to the overall pre-tax loss.

**Liquidity and Capital Resources**

Net cash provided by operations was \$1.7 million for the first three months of 2009 compared to cash used for operations of \$0.7 million in the first three months of 2008, primarily due to improved working capital utilization which was mostly offset by the net loss.

Working capital, including cash and cash equivalents, at March 31, 2009, was \$93.6 million as compared to \$90.0 million at December 31, 2008. An increase in cash and a decrease in current liabilities were mostly offset by decreases in receivables and inventories.

Capital expenditures were \$1.2 million for the first three months of both 2009 and 2008. Net cash provided by financing activities in the first three months of 2009 was \$3.5 million compared to \$2.8 million in the first three months of 2008, primarily reflecting increased net borrowings on the Company's revolving line of credit.

The Company announced a cash dividend of \$.03 per common share in the first quarter of 2009, compared to the cash dividend of \$.20 per share announced in the first quarter of 2008. The Amended Credit Facility entered into in March 2009 restricts the quarterly dividend to \$260,000.

Cash from operations and the revolving line of credit are expected to be adequate to finance the Company's future operations. However, if market and other conditions change from those we anticipate due to a prolonged economic slowdown, our liquidity may be adversely affected. Additionally, further declines in our stock price may reduce the Company's market value compared to the book value of our net assets, which may lead to impairment of our assets.

**Table of Contents**

**ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There have been no material changes in market risk at March 31, 2009 from that reported in the Company's Annual Report on Form 10-K for the year ended December 31, 2008.

**ITEM 4. CONTROLS AND PROCEDURES**

The Company's Chief Executive Officer and Chief Financial Officer have concluded, based on their evaluation as of the end of the period covered by this report, that the Company's disclosure controls and procedures (as defined in the Securities Exchange Act of 1934 Rules 13a-15(e) and 15d-15(e)) are effective to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding financial disclosures.

There was no change in the Company's internal control over financial reporting that occurred during the quarter ended March 31, 2009 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II  
OTHER INFORMATION**

ITEMS 1, 1A, 2, 3, 4 and 5 of Part II are inapplicable and have been omitted from this report.

**ITEM 6. EXHIBITS**

Exhibit #

- |      |  |
|------|--|
| 15   | Letter from Ernst & Young LLP Regarding Unaudited Interim Financial Information  |
| 31.1 | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                             |
| 31.2 | Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002                             |
| 32   | Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |

**Table of Contents**

**SIGNATURES**

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

LAWSON PRODUCTS, INC.  
(Registrant)

Dated April 30, 2009

/s/ Thomas J. Neri  
Thomas J. Neri  
Chief Executive Officer

Dated April 30, 2009

/s/ F. Terrence Blanchard  
F. Terrence Blanchard  
Chief Financial Officer