EASTERN CO
Form 10-K
March 11, 2009

**UNITED STATES SECURITIES AND EXCHANGE COMMISSION**

**Washington, D.C. 20549**

**FORM 10-K**

**(Mark One)**

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

For the Fiscal Year ended January 3, 2009

**OR**

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

For the transition period from ________________ to _______________

**Commission File Number 0-599**

**THE EASTERN COMPANY**

(Exact name of registrant as specified in its charter)

| | |
|---|---|
| **Connecticut**<br>(State or other jurisdiction of incorporation or organization) | **06-0330020**<br>(IRS Employer Identification No.) |
| **112 Bridge Street, Naugatuck, Connecticut**<br>(Address of principal executive offices) | **06770**<br>(Zip Code) |

Registrant s telephone number, including area code**(203) 729-2255**

Securities registered pursuant to Section 12(b) of the Act: **None**

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

**<u>Common Stock No Par Value</u>**

(Title of Class)

Indicate by check mark if the registrant is a well known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes o No x

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 **x** No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

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 definitions of large accelerated filer , accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b2 of the Act).

Yes o No x

As of June 28, 2008, the last day of registrant s most recently completed second fiscal quarter, the aggregate market value of the voting stock held by non-affiliates of the registrant was $80,980,629 (based on the closing sales price of the registrant s common stock on the last trading date prior to that date). Shares of the registrant s common stock held by each officer and director and shares held in trust by the pension plans of the Company have been excluded in that such persons may be deemed to be affiliates. This determination of affiliate status is not necessarily a conclusive determination for other purposes.

As of February 25, 2009, 5,965,681 shares of the registrant s common stock, no par value per share, were issued and outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of the annual proxy statement dated March 17, 2009 are incorporated by reference into Part III.

The Eastern Company

Form 10-K

FOR THE FISCAL YEAR ENDED JANUARY 3, 2009

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SAFE HARBOR STATEMENT

UNDER THE PRIVATE SECURITIES

LITIGATION REFORM ACT OF 1995

This Annual Report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such statements reflect the Company s current expectations regarding its products, its markets and its future financial and operating performance. These statements, however, are subject to risks and uncertainties that may cause the Company s actual results in future periods to differ materially from those expected. Such risks and uncertainties include, but are not limited to, unanticipated slowdowns in the Company s major markets, changing customer preferences, lack of success of new products, loss of customers, competition, increased raw material prices, problems associated with foreign sourcing of parts and products, worldwide conditions and foreign currency fluctuations that may affect results of operations, and other factors discussed from time to time in the Company s filings with the Securities and Exchange Commission. The Company is not obligated to update or revise the aforementioned statements for those new developments.

**PART I**

**ITEM 1 BUSINESS**

**(a) General Development of Business**

The Eastern Company (the Company ) was incorporated under the laws of the State of Connecticut in October, 1912, succeeding a co-partnership established in October, 1858.

The business of the Company is the manufacture and sale of industrial hardware, security products and metal products from four U.S. operations and six wholly-owned foreign subsidiaries. The Company maintains nine physical locations.

**RECENT DEVELOPMENTS**

On August 13, 2008, the Company entered into a joint venture agreement to further develop existing technology for use in the Security Products segment. The joint venture is currently not material to the consolidated financial statements of the Company. The Company's 80% ownership of this joint venture has been consolidated into its financial statements with the remaining 20% ownership accounted for as a minority interest therein.

Effective January 11, 2008 the Company acquired certain assets from Auto-Vehicle Parts Company that included a certain product line owned by one of its divisions, the F.A. Neider Company ( Neider ). Neider produces the footman loop products, or strap fasteners, which are used to fasten straps, traps, tools, and cargo to a vehicle, container, or trailer. Neider manufactures footman loops used in the following markets: military, aerospace, service body, and trailer. The footman loop product line was integrated into the Company s Industrial Hardware segment. The cost of the Neider acquisition was $128,325, inclusive of transaction costs.

During the third quarter of 2006, the Company received orders from a military contractor for component parts used in retro-fitting Humvees as part of the military s up-armor program to provide additional troop protection. These component parts were shipped from September 2006 through the early part of the second quarter of 2007. This program resulted in approximately $39 million in total sales for the Industrial Hardware segment of the Company during the period from September 2006 to April 2007, when the shipments were completed.

Effective November 8, 2006, the Company acquired certain assets of Summit Manufacturing, Inc. ( Summit ), which was integrated into the Company s Security Products segment. Summit designs and manufactures appliance hardware and accessories, including, but not limited to, oven door latches, oven door switches and smoke eliminators and provides subcontract assembly services. The cost of the Summit acquisition was $546,000, inclusive of transaction costs and outstanding debt paid at closing, plus the assumption of $369,000 in current liabilities.

Effective September 25, 2006, the Company acquired certain assets of Royal Lock Corporation ( Royal ), which was also integrated into the Company s Security Products segment. Royal is a supplier of cam locks, switch locks, padlocks, latches, handles and specialty hardware parts. The cost of the Royal acquisition was $6,991,000, inclusive of transaction costs, plus the assumption of $775,000 in current liabilities.

All of the above acquisitions have been accounted for using the purchase method. The acquired businesses are included in the consolidated operating results of the Company from the date of acquisition. Neither the actual results nor the pro forma effects of these acquisitions are material to the Company s financial statements.

In October 2006, the Company s common stock was split 3-for-2.

**(b) <u>Financial Information about Industry Segments</u>**

Financial information about industry segments is included in Note 11 to the Company s financial statements, included at Item 8 of this Annual Report on Form 10-K.

**(c) <u>Narrative Description of Business</u>**

The Company operates in three business segments: Industrial Hardware, Security Products and Metal Products.

**Industrial Hardware**

The Industrial Hardware segment consists of Eberhard Manufacturing, Eberhard Hardware Manufacturing Ltd., Canadian Commercial Vehicles Corporation, Eastern Industrial Ltd. and Sesamee Mexicana, S.A. de C.V. The units design, manufacture and market a diverse product line of industrial and vehicular hardware throughout North America. The segment s locks, latches, hinges, handles, lightweight honeycomb composite structures and related hardware can be found on tractor-trailer trucks, moving vans, off-road construction and farming equipment, school buses, military vehicles and recreational boats. They are also used on pickup trucks, sport utility vehicles and fire and rescue vehicles. In addition, the segment manufactures a wide selection of fasteners and other closure devices used to secure access doors on various types of industrial equipment such as metal cabinets, machinery housings and electronic instruments. Eastern Industrial expands the range of offerings of this segment to include plastic injection molding.

Typical products include passenger restraint locks, slam and draw latches, dead bolt latches, compression latches, cam-type vehicular locks, hinges, tool box locks, light-weight sleeper boxes for Class 8 trucks and school bus door closure hardware. The products are sold directly to original equipment manufacturers and to distributors through a distribution channel consisting of in-house salesmen and outside sales representatives. Sales and customer service efforts are concentrated through in-house sales personnel where greater representation of our diverse product lines can be promoted across a variety of markets.

The Industrial Hardware segment sells its products to a diverse array of markets, such as the truck, bus and automotive industries as well as to the industrial equipment, military and marine sectors. Although service, quality and price are major criteria for servicing these markets, the continued introduction of new or improved product designs and the acquisition of synergistic product lines are vital for maintaining and increasing market share.

**Security Products**

The Security Products segment, made up of Greenwald Industries, Illinois Lock Company/CCL Security Products/Royal Lock, World Lock Company Ltd. and World Security Industries Ltd., is a leading manufacturer of security products. This segment manufactures electronic and mechanical locking devices, both keyed and keyless, for the computer, electronics, vending and gaming industries. The segment also supplies its products to the luggage, furniture, laboratory equipment and commercial laundry industries. Greenwald manufactures and markets coin acceptors and other coin security products used primarily in the commercial laundry markets, as well as hardware and accessories for the appliance industry. In addition, the segment provides a new level of security for the access control, municipal parking and vending markets through the use of smart card technology.

Greenwald s products include timers, drop meters, coin chutes, money boxes, meter cases, smart cards, value transfer stations, smart card readers, card management software, access control units, oven door latches, oven door switches and smoke eliminators. Illinois Lock Company/CCL Security Products/Royal Lock sales include cabinet locks, cam locks, electric switch locks, tubular key locks and combination padlocks. Many of the products are sold under the names SEARCHALERT , PRESTOSEAL , DUO, X-STATIC®, EXCALIBUR , WARLOCK , LITE LOCK , SESAMEE®, BIG TAG®, PRESTOLOCK® and HUSKI . These products are sold to original equipment manufacturers, distributors, route operators, and locksmiths via in-house salesmen and outside sales representatives. Sales efforts are concentrated through national and regional sales personnel where greater representation of our diverse product lines can be promoted across a variety of markets.

The Security Products segment continuously seeks new markets where it can offer competitive pricing and provide customers with engineered solutions for their security needs.

**Metal Products**

The Metal Products segment, based at the Company s Frazer & Jones facility, is the largest and most efficient producer of expansion shells for use in supporting the roofs of underground mines. This segment also manufactures specialty malleable and ductile iron castings.

Typical products include mine roof support anchors, couplers for railroad braking systems, adjustable clamps for construction and fittings for electrical installations. Mine roof support anchors are sold to distributors and directly to mines, while specialty castings are sold to original equipment manufacturers.

Rising oil and natural gas prices have resulted in increased demand for coal, which has led to increased demand for our highly engineered proprietary mine roof support products produced by this segment of the Company. In addition, this segment has seen an increase in demand in its contract casting business. This is directly related to the weakening U.S. dollar against the



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EURO and Chinese RMB, making our malleable and ductile iron contract castings more competitive against global competition.

**General**

Raw materials and outside services were readily available from domestic sources for all of the Company s segments during 2008 and are expected to be readily available in 2009 and the foreseeable future. The Company also obtains materials from Asian affiliated and nonaffiliated sources. The Company has not experienced any significant problems obtaining material from its Asian sources in 2008 and does not expect any such problems in 2009. In 2008, the Company experienced price fluctuations for zinc, brass and stainless steel, used mainly in the Industrial Hardware and Security Products segments, as well as scrap iron used in the Metal Products segment. These higher prices had a negative impact on gross margin in 2008, and will continue to negatively impact gross margin in 2009 if prices do not stabilize or the Company is not able to increase selling prices to its customers.

Patent protection for the various product lines within the Company is limited, but is sufficient to protect the Company s competitive positions. Foreign sales and license agreements are not significant.

None of the Company s business segments are seasonal.

The Company, across all its business segments, has increased its emphasis on sales and customer service by fulfilling the rapid delivery requirements of our customers. As a result, investments in additional inventories are made on a selective basis.

Customer lists for all business segments are broad-based geographically and by markets, and sales are generally not highly concentrated by customer. However, due to the military Humvee retro-fit contract, one customer in the Industrial Hardware Segment accounted for approximately 15% of total sales in 2006 and 14% of total sales in 2007. No other customers equaled 10% or more of the Company s consolidated sales for any year presented.

The dollar amount of the backlog of orders received by the Company is believed to be firm as of the fiscal year end January 3, 2009 at $18,936,000, as compared to $22,802,000 at December 29, 2007. The main reasons for the decrease from 2007 to 2008 are the timing of orders received from customers and changes in customer ordering habits, such as not issuing blanket purchase orders due to the uncertain current economic conditions.

The Company encounters competition in all of its business segments. The Company has been successful in dealing with this competition by offering high quality diversified products with the flexibility of meeting customer needs on a timely basis. This is accomplished by effectively using internal engineering resources and cost effective manufacturing capabilities, expanding product lines through product development and acquisitions, and maintaining sufficient inventory for fast turnaround of customer orders. However, imports from Asia and Latin America with favorable currency exchange rates and low cost labor have created additional competitive pressures. The Company currently utilizes three wholly-owned subsidiaries in Asia to help offset offshore competition.

Research and development expenditures in 2008 were $1,293,000 and represented approximately 1% of gross revenues. In 2007 and 2006 they were $1,439,000 and $1,354,000, respectively. The research costs are primarily attributable to the Greenwald Industries and Eberhard Mfg. divisions. Greenwald performs ongoing research, in both the mechanical and smart card product lines, which is necessary in order to remain competitive and to continue to provide technologically advanced smart card systems. Eberhard develops new products for the various markets they serve based on changing customer requirements to remain competitive. Other research projects include the development of various locks, and transportation and industrial hardware products.

The Company does not anticipate that compliance with federal, state or local environmental laws or regulations will have a material effect on the Company s capital expenditures, earnings or competitive position.

The average number of employees in 2008 was 696.

**(d) Financial Information about Geographic Areas**

The Company includes four separate operating divisions located within the United States, two wholly-owned Canadian subsidiaries (one located in Tillsonburg, Ontario, Canada, and one in Kelowna, British Columbia, Canada), a wholly-owned Taiwanese subsidiary located in Taipei, Taiwan, a wholly-owned subsidiary in Hong Kong, a wholly-owned subsidiary in Shanghai, China, and a wholly-owned subsidiary in Lerma, Mexico.

Individually, the Canadian, Taiwanese, Hong Kong, Chinese and Mexican subsidiaries revenue and assets are not significant. Substantially all other revenues are derived from customers located in the United States.

Financial information about foreign and domestic operations revenues and identifiable assets is included in Note 11 to the Company s financial statements, included at Item 8 of this Annual Report on Form 10-K. Information about risks attendant to the Company s foreign operations is set forth at Item 1A of this Annual Report on Form 10-K.

**(e) Available Information**

The Company makes available, free of charge through its Internet website at http://www.easterncompany.com, its annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as soon as reasonably practicable after such material is electronically filed with or furnished to the Securities and Exchange Commission. The public may read and copy any materials that the Company files with the SEC at the SEC s Public Reference Room, 450 Fifth Street, N.W., Washington, DC 20549 or by calling the SEC at 1-800-SEC-0330. The Company s reports filed with, or furnished to, the SEC are also available on the SEC s website at www.sec.gov.

**ITEM 1A RISK FACTORS**

In addition to the other information contained in this Form 10-K and the exhibits hereto and the Company s other filings with the SEC, the following risk factors should be considered carefully in evaluating the Company s business. The Company s business, financial condition or results of operation could be materially adversely affected by any of these risks or additional risks not presently known to the Company, or by risks the Company currently deems immaterial which may also adversely affect its business, financial condition, or results of operations, such as: changes in the economy, including changes in inflation, tax rates and interest rates; risk associated with possible disruption in the Company s operations due to terrorism and other manmade or natural disasters; future regulatory actions, legal issues or environmental matters; loss of, or changes in, executive management; and changes in accounting standards which are adverse to the Company. Also, there can be no assurance that the Company has correctly identified and appropriately assessed all factors affecting its business or that information publicly available with respect to these matters is complete and correct.

**The Company s business is subject to risks associated with conducting business overseas.**

International operations could be adversely affected by changes in political and economic conditions, trade protection measures, restrictions on repatriation of earnings, differing intellectual property rights, and changes in regulatory requirements that restrict the sales of products or increase costs. Changes in exchange rates between the U.S. dollar and other currencies could result in increases or decreases in earnings, and may adversely affect the value of the Company s assets outside the United States. The Company s operations are also subject to the effects of international trade agreements and regulations. Although generally these trade agreements have positive effects, they can also impose requirements that adversely affect the Company s business, such as setting quotas on product that may be imported from a particular country into the Company s key markets in North America.

The Company s ability to import products in a timely and cost-effective manner may also be affected by conditions at ports or issues that otherwise affect transportation and warehousing providers, such as port and shipping capacity, labor disputes, severe weather or increased homeland security requirements in the United States or other countries. These issues could delay importation of products or require the Company to locate alternative ports or warehousing providers to avoid disruption to customers. These alternatives may not be available on short notice or could result in higher transit costs, which could have an adverse impact on the Company s business, financial conditions or results of operations.

See also **ITEM 7A - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK** of this Form 10-K.

In addition, the Company s growth strategy involves expanding sales of its products into foreign markets. There is no guarantee that the Company s products will be accepted by foreign customers or how long it may take to develop sales of the Company s products in these foreign markets.

**Increases in the price or reduced availability of raw materials.**

Raw materials needed to manufacture products are obtained from numerous suppliers. Under normal market conditions, these raw materials are readily available on the open market from a variety of producers. However, from time to time the prices and availability of these raw materials fluctuate, which could impair the Company s ability to procure the required raw materials for its operations or increase the cost of manufacturing its products. If the price of raw materials increases, the Company may be unable to pass these increases on to its customers and could experience reduction to its profit margins. Also, any decrease in the availability of raw materials could impair the Company s ability to meet production requirements in a timely manner.

**Increased competition in the markets the Company services could impact revenues and earnings.**

Any change in competition may result in lost market share or reduced prices, which could result in reduced profit margins. This may impair the ability to grow or even maintain current levels of revenues and earnings. While the Company has an extensive customer base, loss of certain customers could adversely affect the Company s business, financial condition or results of operations until such business is replaced, and no assurances can be made that the Company would be able to regain or replace any lost customers.

**The Company is required to evaluate its internal control over financial reporting under Section 404 of the Sarbanes-Oxley Act of 2002.**

The Company is an accelerated filer as defined in Rule 12b-2 under the Securities Exchange Act of 1934, as amended, and is required to comply with Section 404 of the Sarbanes-Oxley Act of 2002. Section 404 requires the Company to include in its report management s assessment of the effectiveness of the Company s internal control over financial reporting as of the end of the fiscal period for which the Company is filing its 10-K. This report must also include disclosure of any material weaknesses in internal control over financial reporting that the Company has identified. Additionally, the Company s independent registered public accounting firm is required to issue a report on the Company s internal control over financial reporting and their evaluation of the operating effectiveness of the Company s internal control over financial reporting. The Company s assessment requires it to make subjective judgments, and the independent registered public accounting firm may not agree with the Company s assessment. If the Company or its independent registered public accounting firm were unable to complete the assessments within the period prescribed by Section 404 and thus be unable to conclude that the internal control over financial reporting is effective, investors could lose confidence in the Company s reported financial information, which could have an adverse effect on the market price of the Company s common stock or impact the Company s borrowing ability. In addition, changes in operating conditions and changes in compliance with policies and procedures currently in place may result in inadequate internal control over financial reporting in the future.

**The inability to identify or complete acquisitions could limit future growth.**

As part of its growth strategy, the Company continues to pursue acquisitions of complementary products or businesses. The ability to grow through acquisitions depends upon the Company s ability to identify, negotiate, complete and integrate suitable acquisitions. The Company makes certain assumptions based on the information provided by potential acquisition candidates and also conducts due diligence to ensure the information provided is accurate and based on reasonable assumptions. However, the Company may be unable to realize the anticipated benefits from an acquisition or predict accurately how an acquisition will ultimately affect the business, financial condition or results of operations.

**Demand for new products and the inability to develop and introduce new competitive products at favorable profit margins could adversely affect the Company s performance and prospects for future growth, and the Company would not be positioned to maintain current levels of revenues and earnings.**

The uncertainties associated with developing and introducing new products, such as the market demands and the costs of development and production, may impede the successful development and introduction of new products. Acceptance of the new products may not meet sales expectations due to several factors, such as the Company s failure to accurately predict market demand or its inability to resolve technical issues in a timely and cost-effective manner. Additionally, the inability to develop new products on a timely basis could result in the loss of business to competitors.

**The Company could be subject to litigation which could have a material impact on the Company s business, financial condition or results of operations.**

From time to time, the Company s operations are parties to or targets of lawsuits, claims, investigations and proceedings, including product liability, personal injury, patent and intellectual property, commercial, contract, environmental and employment matters, which are defended and settled in the ordinary course of business. While the Company is unable to predict the outcome of any of these matters, it does not believe, based upon currently available information, that the resolution of any pending matter will have a material adverse effect on its business, financial condition or results of operations. See ITEM 3 LEGAL PROCEEDINGS in this Form 10-K for a discussion of current litigation.

**The Company could be subject to additional tax liabilities.**

The Company is subject to income tax laws in the United States, its states and municipalities and those of other foreign jurisdictions in which the Company has business operations. These laws are complex and subject to interpretations by the taxpayer and the relevant governmental taxing authorities. Significant judgment and interpretation is required in determining the Company s worldwide provision for income taxes. In the ordinary course of business, transactions arise where the ultimate tax determination is uncertain. Although the Company believes its tax estimates are reasonable, the final outcome of tax audits and any related litigation could be materially different from that which is reflected in historical income tax provisions and accruals. Based on the status of a given tax audit or related litigation, a material effect on the Company s income tax provision or net income may result during the period or periods from the initial recognition of a particular matter in the Company s reported financial results to the final closure of that tax audit or settlement of related litigation when the ultimate tax and related cash flow is known with certainty.

**The Company s goodwill or indefinite-lived intangible assets may become impaired, which could require a significant charge to earnings to be recognized.**

Under accounting principles generally accepted in the United States, goodwill and indefinite-lived intangible assets are not amortized but are reviewed for impairment at least annually. Future operating results used in the assumptions, such as sales or profit forecasts, may not materialize, and the Company could be required to record a significant charge to earnings in the financial statements during the period in which any impairment is determined, resulting in an unfavorable impact on our results of operations. Numerous assumptions are used in the evaluation of impairment, and there is no guarantee that the Company s independent registered public accounting firm would reach the same conclusion as the Company or an independent valuation firm, which could result in a disagreement between management and the independent registered public accounting firm.

**The Company may need additional capital in the future, and it may not be available on acceptable terms, if at all.**

From time-to-time, the Company has historically relied on outside financing to fund expanded operations, capital expenditure programs and acquisitions. The Company may require additional capital in the future to fund operations or strategic opportunities. The Company cannot be assured that additional financing will be available on favorable terms, or at all. In addition, the terms of available financing may place limits on the Company s financial and operating flexibility. If the Company is unable to obtain sufficient capital in the future, the Company may not be able to expand or acquire complementary businesses and may not be able to continue to develop new products or otherwise respond to changing business conditions or competitive pressures.

**The Company s stock price is highly volatile due to low float, which is the number of shares of the Company s common stock that are outstanding and available for trading by the public.**

The Company s stock price may change dramatically when buyers seeking to purchase shares of the Company s common stock exceed the shares available on the market, or when there are no buyers to purchase shares of the Company s common stock when shareholders are trying to sell their shares.

**The Company may not be able to reach acceptable terms for contracts negotiated with its labor unions and be subject to work stoppages or disruption of production.**

The Company has been successful in negotiating new contracts over the years, but cannot guarantee that will continue. Failure to negotiate new union contracts could result in disruption of production, inability to deliver product or a number of unforeseen circumstances, any of which could have an unfavorable material impact on the Company s results of operations or financial statements. The Company does not have any union contracts that expire during 2009.

**Deterioration in the creditworthiness of several major customers could have a material impact on the Company s business, financial condition or results of operations.**

Included as a significant asset on the Company s balance sheet is accounts receivable from our customers. If several large customers become insolvent or otherwise unable to pay for products, or become unwilling or unable to make payments in a timely manner, it could have an unfavorable material impact on the Company s results of operations or financial statements. Although the Company is not dependent on any one customer, and the Company does not have any customers exceeding 10% of total accounts receivable, deterioration in several major customers at the same time could have an unfavorable material impact on the Company s results of operations or financial statements.

**The Company s operating results may fluctuate, which makes the results of operations difficult to predict and could cause the results to fall short of expectations.**

The Company s operating results may fluctuate as a result of a number of factors, many outside of our control. As a result, comparing the Company s operating results on a period-to-period basis may not be meaningful, and past results should not be relied upon as an indication of future performance. Quarterly, year to date and annual costs and expenses as a percentage of revenue may differ significantly from historical or projected rates. Future operating results may fall below expectations. These types of events could cause the price of the Company s stock to fall.

**New or existing U.S. or foreign laws could subject the Company to claims or otherwise impact the Company s business, financial condition or results of operations.**

The Company is subject to a variety of laws in both the U.S. and foreign countries that are costly to comply with, can result in negative publicity and diversion of management time and effort, and can subject the Company to claims or other remedies.

**ITEM 1B UNRESOLVED STAFF COMMENTS**

None.

**ITEM 2 PROPERTIES**

The corporate office of the Company is located in Naugatuck, Connecticut in a two-story 8,000 square foot administrative building on 3.2 acres of land.

All of the Company s properties are owned or leased and are adequate to satisfy current requirements. All of the Company s properties have the necessary flexibility to cover any long-term expansion requirements.

**The Industrial Hardware Group includes the following:**

The Eberhard Manufacturing Division in Strongsville, Ohio owns 9.6 acres of land and a building containing 138,000 square feet, located in an industrial park. The building is steel frame, one-story, having curtain walls of brick, glass and insulated steel panel. The building has two high bays, one of which houses two units of automated warehousing.

The Eberhard Hardware Manufacturing, Ltd., a wholly-owned Canadian subsidiary in Tillsonburg, Ontario, owns 4.4 acres of land and a building containing 31,000 square feet in an industrial park. The building is steel frame, one-story, having curtain walls of brick, glass and insulated steel panel. It is particularly suited for light fabrication, assembly and warehousing and is adequate for long-term expansion requirements.

The Canadian Commercial Vehicles Corporation, a wholly-owned subsidiary in Kelowna, British Columbia, leases 55,415 square feet of building space located in an industrial park. The building is made from brick and concrete, contains approximately 5,400 square feet of office space on two levels and houses a modern paint booth for finishing our products. The building is protected by a F1 rated fire suppression system and alarmed for fire and security. The current lease expires December 31, 2009 and is renewable.

The Eastern Industrial Ltd., a wholly-owned subsidiary in Shanghai, China, leases brick and concrete buildings containing approximately 45,600 square feet, located in both industrial and commercial areas. A five-year lease was signed in 2003, which expired on September 8, 2008 and was extended through March 31, 2009. Eastern Industrial Ltd. will be relocating in March 2009 to a lower cost leased facility. The new facility will consist of brick and concrete buildings containing approximately 47,500 square feet with a five-year lease expiring on March 31, 2014 .

The Sesamee Mexicana subsidiary moved in February 2009 into a leased facility containing approximately 22,500 square feet located in an industrial park in Lerma, Mexico. The current lease expires December 31, 2009 and is renewable. The building is steel framed with concrete block and glass curtain walls.

**The Security Products Group includes the following:**

The Greenwald Industries Division in Chester, Connecticut owns 26 acres of land and a building containing 120,000 square feet. The building is steel frame, one story, having brick over concrete blocks.

The Illinois Lock Company/CCL Security Products/Royal Lock Division owns 2.5 acres of land and a building containing 44,000 square feet in Wheeling, Illinois. The building is brick and located in an industrial park. The Company is also leasing approximately 10,000 square feet of warehouse space occupied by Royal Lock through March 2009.

The World Lock Co. Ltd. subsidiary leases 5,285 square feet located in Taipei, Taiwan. The building is made from brick and concrete and is protected by a fire alarm and sprinklers.

**The Metal Products Group consists of:**

The Frazer and Jones Division in Solvay, New York owns 17.9 acres of land and buildings containing 205,000 square feet constructed for foundry use. These facilities are well adapted to handle the division s current and future casting requirements.

All owned properties are free and clear of any encumbrances.

**ITEM 3 LEGAL PROCEEDINGS**

During 2008, the Company reached a settlement relating to an investigation by the U.S. Department of Environmental Protection and N.Y. Department of Environmental Conservation relating to various anonymous complaints regarding its metal castings facility. Settlement payments and remediation costs approximated $250,000.

During 2008, the U.S. Environmental Protection Agency identified the Company as a potentially responsible party in connection with a site in Cleveland, Ohio based on the ownership of the site by a division of the Company in the 1960 s. According to the Agency, the current occupant of the site filed bankruptcy, leaving behind plating operations which required remedial action. The Company declined to participate in the remedial action, and intends to defend against any efforts of the Agency to impose any liability against the Company for environmental conditions on this site which may have occurred in the years since its ownership.

There are no other legal proceedings, other than ordinary routine litigation incidental to the Company s business, to which either the Company or any of its subsidiaries is a party or to which any of their property is the subject.

**ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

No matters were submitted to a vote of security holders during the fourth quarter ended January 3, 2009.

**PART II**

**ITEM 5 MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES**

The Company s common stock is traded on the NYSE Alternext (formerly the American Stock Exchange) (ticker symbo**EML**). The approximate number of record holders of the Company common stock on January 3, 2009 was 560.

High and low stock prices and dividends for the last two years were:

| | 2008 | | | 2007 | | | |
|---|---|---|---|---|---|---|---|
| | Market Price | | | | Market Price | | |
| Quarter | High | Low | Dividend | Quarter | High | Low | Dividend |
| First | $18.55 | $14.51 | $.08 | First | $29.30 | $18.99 | $.08 |
| Second | 20.00 | 15.00 | .08 | Second | 33.90 | 24.00 | .08 |
| Third | 16.10 | 13.10 | .08 | Third | 29.28 | 16.00 | .08 |
| Fourth | 13.40 | 7.88 | .09 | Fourth | 23.77 | 17.28 | .08 |

The Company increased the dividend rate by 12.5% in the fourth quarter of 2008. The Company expects to continue its policy of paying regular cash dividends, although there is no assurance as to future dividends because they are dependent on future earnings, capital requirements, and financial conditions. The payment of dividends is subject to the restrictions of the Company s loan agreement if such payment would result in an event of default. See Item 7 Management s Discussion and Analysis of Financial Condition and Results of Operations, and Note 5 to the Company s financial statements included at Item 8 of this Annual Report on Form 10-K.

The following table sets forth information regarding securities authorized for issuance under the Company s equity compensation plans as of January 3, 2009, including the Company s 1995, 1997 and 2000 plans.

**Equity Compensation Plan Information**

| Plan category | Number of securities to be issued upon exercise of outstanding options, warrants and rights | Weighted-average exercise price of outstanding options, warrants and rights | Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) |
|---|---|---|---|
| | (a) | (b) | (c) |
| Equity compensation plans approved by security holders | 363,000[1] | $10.49 | 367,500[2] |
| Equity compensation plans not approved by security holders | 75,000[3] | 10.17 | - |
| Total | 438,000 | 10.43 | 367,500 |

[1] Includes options outstanding under the 1995 and 2000 plans.

[2] Includes shares available for future issuance under the 2000 plan.

[3] Includes options outstanding under the 1997 plan.

On September 17, 1997 the Compensation Committee of the Board of Directors of the Company adopted The Eastern Company 1997 Directors Stock Option Plan (the 1997 Plan ) which by its terms expired on September 16, 2007. The 1997 Plan authorized the grant of non-qualified stock options to the non-employee directors of the Company to purchase shares of common stock. The exercise price of any options granted under the 1997 Plan was set by the Compensation Committee. However, all options granted under the 1997 Plan have required an exercise price equal to 100% of the fair market value of the shares of common stock of the Company on the date of grant. While no more shares are available for grant under the plan, there are 75,000 shares reserved for issuance resulting from previous stock option grants.

Each director who is not an employee of the Company ( Outside Director ) is paid a director s fee for his services at the annual rate of $24,600. All annual fees paid to non-employee members of the Board of Directors of the Company are paid in common stock of the Company or cash, in accordance with the Directors Fee Program adopted by the shareholders on March 26, 1997 and amended on January 5, 2004. The directors make an annual election, within a reasonable time before their first quarterly payment, to receive their fees in the form of cash, stock or a combination thereof. The election remains in force for one year.

**Issuer Purchases of Equity Securities**

| Period | (a) Total Number of Shares Purchased | (b) Average Price Paid per Share | (c ) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | (d) Maximum Number that May Yet Be Purchased Under the Plans or Programs |
|---|---|---|---|---|
| September 28 November 1, 2008 | - | - | - | - |
| November 2 November 29, 2008 | - | - | - | - |
| November 30, 2008 January 3, 2009 | 15,795 | $13.29 | - | - |
| Total | 15,795 | $13.29 | - | - |

The Company does not have any share repurchase plans or programs. The figures shown in the table above are for shares delivered to the Company to exercise stock options.

**Stock Performance Graph**

The following graph sets forth the Company s cumulative total shareholder return based upon an initial $100 investment made on December 31, 2003 (i.e., stock appreciation plus dividends during the past five fiscal years) compared to the Dow Jones Wilshire 5000 Index and the S&P Industrial Machinery Index.

The Company manufactures and markets a broad range of locks, latches, fasteners and other security hardware that meets the diverse security and safety needs of industrial and commercial customers. Consequently, while the S&P Industrial Machinery Index being used for comparison is the standard index most closely related to the Company, it does not completely represent the Company s products or market applications. The Dow Jones Wilshire 5000 is a market index made up of 5,000 publicly-traded companies, including those having both large and small capitalization.

| | **Dec. 03** | **Dec. 04** | **Dec. 05** | **Dec. 06** | **Dec. 07** | **Dec. 08** |
|---|---|---|---|---|---|---|
| **The Eastern Company** | $100 | $131 | $131 | $199 | $191 | $92 |
| **Wilshire 5000** | $100 | $112 | $120 | $139 | $146 | $92 |
| **S&P © Industrial Machinery** | $100 | $118 | $116 | $132 | $160 | $96 |

**ITEM 6 SELECTED FINANCIAL DATA**

| | 2008 | 2007 | 2006 | 2005 | 2004 |
|---|---|---|---|---|---|
| **INCOME STATEMENT ITEMS (in thousands)** | | | | | |
| Net sales | $ 135,878 | $ 156,281 | $ 138,465 | $ 109,107 | $ 100,130 |
| Cost of products sold | 110,415 | 120,343 | 103,882 | 84,375 | 74,999 |
| Depreciation and amortization | 4,128 | 4,370 | 3,746 | 3,460 | 3,461 |
| Interest expense | 1,064 | 1,289 | 1,098 | 1,014 | 1,044 |
| Income before income taxes and minority interest | 6,002 | 14,845 | 14,846 | 7,020 | 6,829 |
| Income taxes | 1,538 | 4,765 | 5,187 | 2,653 | 2,071 |
| Net income before minority interest | 4,464 | 10,081 | 9,659 | 4,367 | 4,758 |
| Minority interest | 41 | | | | |
| Net income | 4,505 | 10,081 | 9,659 | 4,367 | 4,758 |
| Dividends | 1,938 | 1,802 | 1,715 | 1,600 | 1,596 |
| **BALANCE SHEET ITEMS (in thousands)** | | | | | |
| Inventories | $ 30,797 | $ 30,491 | $ 28,043 | $ 20,768 | $ 20,478 |
| Working capital | 48,745 | 47,028 | 35,546 | 31,223 | 26,692 |
| Property, plant and equipment, net | 23,911 | 25,234 | 25,816 | 22,397 | 23,907 |
| Total assets | 106,017 | 108,352 | 103,485 | 81,622 | 78,072 |
| Shareholders equity | 62,482 | 70,817 | 54,391 | 46,172 | 43,817 |
| Capital expenditures | 2,331 | 2,868 | 6,722 | 1,750 | 2,062 |
| Long-term obligations, less current portion | 11,429 | 14,383 | 17,507 | 12,384 | 11,805 |
| **PER SHARE DATA** | | | | | |
| Net income per share | | | | | |
| Basic | $ .77 | $ 1.79 | $ 1.76 | $ .80 | $ .87 |
| Diluted | .73 | 1.68 | 1.67 | .75 | .85 |
| Dividends | .33 | .32 | .31 | .29 | .29 |
| Shareholders equity (Basic) | 10.63 | 12.58 | 9.94 | 8.47 | 8.05 |
| Average shares outstanding: Basic | 5,875,140 | 5,631,073 | 5,474,137 | 5,455,073 | 5,441,312 |
| Diluted | 6,159,563 | 5,989,754 | 5,768,108 | 5,828,837 | 5,618,552 |

The information in the table above reflects a 3-for-2 stock split effective October 2006.

**ITEM 7 MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**Summary**

Net sales for 2008 decreased 13% to $135.9 million from $156.3 million in 2007. Net income for 2008 decreased to $4.5 million, or $.73 per diluted share, from $10.1 million, or $1.68 per diluted share in 2007. Net sales and net income in 2007 were favorably impacted by shipments of approximately $20.5 million from the Industrial Hardware segment to fulfill orders received in September 2006 to produce door latching components for a military project to up-armor existing Humvees. The military project was completed in April of 2007. The Company s core business units sales in 2008 of $135.9 million were comparable to 2007. Net sales in the Industrial Hardware segment decreased approximately 26% in 2008, as a consequence of the military project that benefited the 2007 period and softness in the Class 8 truck market. Sales decreased in the Security Products segment by 9%, resulting from the economic slowdown in the many markets we serve. The Metal Products segment sales increased by 48%, primarily resulting from increased shipments of mine roof support products.

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The following table shows, for the fourth quarter of 2008 and 2007, selected line items from the consolidated statements of income as a percentage of net sales, by segment.

| | 2008 Fourth Quarter | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Industrial Hardware | | Security Products | | Metal Products | | Total | |
| Net sales | 100.0 | % | 100.0 | % | 100.0 | % | 100.0 | % |
| Cost of products sold | 72.7 | % | 76.8 | % | 106.1 | % | 80.3 | % |
| Gross margin | 27.3 | % | 23.2 | % | -6.1 | % | 19.7 | % |
| Selling and administrative expense | 14.8 | % | 18.2 | % | 8.9 | % | 14.9 | % |
| Operating profit | 12.5 | % | 5.0 | % | -15.0 | % | 4.8 | % |

| | 2007 Fourth Quarter | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | Industrial Hardware | | Security Products | | Metal Products | | Total | |
| Net sales | 100.0 | % | 100.0 | % | 100.0 | % | 100.0 | % |
| Cost of products sold | 78.6 | % | 76.1 | % | 101.5 | % | 79.9 | % |
| Gross margin | 21.4 | % | 23.9 | % | -1.5 | % | 20.1 | % |
| Selling and administrative expense | 14.6 | % | 16.0 | % | 19.2 | % | 15.7 | % |
| Operating profit | 6.8 | % | 7.9 | % | -20.7 | % | 4.4 | % |

The following table shows the amount of change from the fourth quarter of 2007 to the fourth quarter of 2008 in sales, cost of products sold, gross margin, selling and administrative expenses and operating profit, by segment (dollars in thousands).

| | Industrial Hardware | | Security Products | | Metal Products | | Total | |
|---|---|---|---|---|---|---|---|---|
| Net sales | $ (813 | ) | $ (2,939 | ) | $ 2,301 | | $ (1,451 | ) |
| Volume | -15.6 | % | -25.3 | % | 49.2 | % | -13.0 | % |
| Prices | 2.6 | % | 4.4 | % | 10.9 | % | 4.3 | % |
| New Products | 7.8 | % | 0.8 | % | 4.6 | % | 4.4 | % |
| | -5.2 | % | -20.1 | % | 64.7 | % | -4.3 | % |
| Cost of products sold | $ (1,508 | ) | $ (2,150 | ) | $ 2,603 | | $ (1,055 | ) |
| | -12.3 | % | -19.3 | % | 72.1 | % | -3.9 | % |
| Gross margin | $ 695 | | $ (789 | ) | $ (302 | ) | $ (396 | ) |
| | 20.8 | % | -22.6 | % | -556.7 | % | -5.8 | % |
| Selling and administrative expenses | $ (94 | ) | $ (222 | ) | $ (159 | ) | $ (475 | ) |
| | -4.1 | % | -9.4 | % | -23.4 | % | -9.0 | % |
| Operating profit | $ 789 | | $ (567 | ) | $ (143 | ) | $ 79 | |
| | 74.3 | % | -49.3 | % | -19.4 | % | 5.4 | % |

Net sales in the fourth quarter of 2008 decreased 4% to $32.3 million from $33.8 million a year earlier. Net income for the quarter increased 20% to $1.1 million (or $.17 per diluted share) from $887,000 (or $.15 per diluted share) a year earlier. The decrease in sales from 2007 to 2008 is primarily attributable to the economic slowdown in many of the markets served by our Industrial Hardware and Security Products segments. The decrease in sales volume of existing products in those two segments was partially offset by the introduction of new products and price increases to customers, in addition to increased demand for products from the Metal Products segment. The increase in profit from 2007 to 2008 is the result of the 2007 period being reduced by a $250,000 environmental contingency reserve that was recorded in December 2007 related to the Metal Products segment.

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Gross margin for the fourth quarter of 2008 decreased 5.8% from the fourth quarter of 2007. The decrease is primarily the result of lower sales volume in the 2008 fourth quarter in the Industrial Hardware and Security Products segment as a result of the economic slowdown which affected many of the markets we serve, as well as an increase in research and development expenses in the 2008 period.

Selling and administrative expenses for the fourth quarter of 2008 decreased 9.0% compared to the prior year quarter. The overall decrease was due to lower payroll and payroll related charges and the impact of the $250,000 environmental contingency reserve set up in the fourth quarter of 2007.

On December 30, 2006, the Company adopted the recognition and disclosure provisions of SFAS No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R)* ( SFAS No. 158 ), which was issued by the FASB in September 2006. This standard requires employers to recognize the underfunded or overfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in the funded status in the year in which the changes occur through accumulated other comprehensive income. Additionally, SFAS No. 158 requires employers to measure the funded status of a plan as of the date of its year-end statement of financial position. As allowed under SFAS 158, the Company adopted the measurement date provision in 2008. See also Note 10, Retirement Benefit Plans, included at Item 8 of this 10-K.

In June 2006, the FASB issued Interpretation No. 48 ( FIN 48), *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109* ( SFAS 109 ). This interpretation clarifies the accounting for uncertainty in income taxes recognized in a company s financial statements in accordance with SFAS 109, *Accounting for Income Taxes*. FIN 48 details how companies should recognize, measure, present, and disclose uncertain tax positions that have been or are expected to be taken. As such, financial statements will reflect expected future tax consequences of uncertain tax positions presuming the taxing authorities full knowledge of the position and all relevant facts. The Company adopted FIN 48 in the first quarter of 2007. See also Note 8, Income Taxes, included at Item 8 of this Form 10-K.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, *Fair Value Measurements,* ( SFAS 157 ). SFAS 157 defines fair value, establishes a framework for measuring the fair value of assets and liabilities, and expands disclosure requirements regarding the fair value measurement. SFAS 157 does not expand the use of fair value measurements. This statement, as issued, is effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. FASB Staff Position (FSP) FAS No. 157-2 was issued in February 2008 and deferred the effective date of SFAS 157 for non-financial assets and liabilities to fiscal years beginning after November 2008. As such, the Company adopted SFAS 157 as of December 30, 2007 for financial assets and liabilities only. There was no material impact on the Company s consolidated financial statements. As of January 3, 2009, the Company s financial liability subject to SFAS 157 consisted of an interest rate swap agreement (included in Interest rate swap obligation on the consolidated balance sheets). The Company determined fair value for the derivative liability based on third party valuation models (i.e. Level 2 as defined under SFAS 157). The Company does not have any financial assets subject to SFAS 157. The adoption of SFAS No. 157 related to the Company s financial assets and liabilities did not have a material impact on the fair value measurement or require expanded disclosures. See also Note 13, Financial Instruments and Fair Value Measurements, included at Item 8 of this Form 10-K.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115* ( SFAS 159 ). SFAS 159 expands the use of fair value accounting but does not affect existing standards which require assets or liabilities to be carried at fair value. The objective of SFAS 159 is to improve financial reporting by providing companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. Under SFAS 159, a company may elect to use fair value to measure eligible items at specified election dates and report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date. Eligible items include, but are limited to, accounts receivable, accounts payable, and issued debt. If elected, SFAS 159 was effective for the Company s 2008 fiscal year. The Company has not elected to measure any additional assets or liabilities at fair value that are not already measured at fair value under existing standards.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), Business Combinations ( SFAS No. 141(R) ), which replaces SFAS No. 141. This standard significantly changes the principles and requirements for how the acquirer of a business recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the acquiree. The statement also provides guidance for recognizing and measuring the goodwill acquired in the business combination and determines what information to disclose to enable users of the financial statements to evaluate the nature and financial effects of the business combination. This statement is effective prospectively, except for certain retrospective adjustments to deferred tax balances, for fiscal years beginning after December 15, 2008. The Company has not determined the impact, if any, of the adoption of SFAS No. 141(R).

In December 2007, the FASB issued SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements an amendment of ARB No. 51,* ( SFAS No. 160 ). SFAS 160 clarifies the classification of noncontrolling interests in consolidated balance sheets and reporting transactions between the reporting entity and holders of noncontrolling interests. Under this statement, noncontrolling interests are considered equity and reported as an element of consolidated equity. Further, net income encompasses all consolidated subsidiaries with disclosure of the attribution of net income between controlling and noncontrolling interests. SFAS No. 160 is effective prospectively for fiscal years beginning after December 15, 2008. The Company has not determined the impact, if any, of the adoption of SFAS No. 160.

In March 2008, the FASB issued SFAS No. 161, *Disclosures About Derivative Instruments and Hedging Activities an amendment of FASB Statement No. 133* ( SFAS No. 161 ), which expands the disclosure requirements in SFAS 133 about an entity s derivative instruments and hedging activities. SFAS No. 161 expands the disclosure provisions to apply to all entities with derivative instruments subject to SFAS No. 133 and its related interpretations. The provisions also apply to related hedged items, bifurcated derivatives, and nonderivative instruments that are designated and qualify as hedging instruments. Entities with instruments subject to SFAS No. 161 must provide more robust qualitative disclosures and expanded quantitative disclosures. Such disclosures, as well as existing SFAS No. 133 required disclosures, generally will need to be presented for every annual and interim reporting period. SFAS No. 161 is effective for fiscal years and interim periods beginning after November 15, 2008. The Company has not determined the impact, if any, of the adoption of SFAS No. 161.

In April 2008, the FASB issued FSP SFAS No. 142-3, *Determination of the Useful Life of Intangible Assets* ( FSP SFAS No. 142-3 ). FSP SFAS No. 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, *Goodwill and Other Intangible Assets* ( SFAS No. 142 ). The intent of FSP SFAS No. 142-3 is to improve the consistency between the useful life of a recognized intangible asset under SFAS No. 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS No. 141(R) and other applicable accounting literature. FSP SFAS No. 142-3 is effective for financial statements issued for fiscal years beginning after December 15, 2008 and must be applied prospectively to intangible assets acquired after the effective date. The Company has not determined the impact, if any, of the adoption of FSP SFAS No. 142-3.

In May 2008, the FASB issued SFAS No. 162, *Hierarchy of Generally Accepted Accounting Principles* ( SFAS No. 162 ). This statement is intended to improve financial reporting by identifying a consistent framework, or hierarchy, for selecting accounting principles to be used in preparing financial statements of nongovernmental entities that are presented in conformity with GAAP. This statement will be effective 60 days following the U.S. Securities and Exchange Commission s approval of the Public Company Accounting Oversight Board amendment to AU Section 411, *The Meaning of Present Fairly in Conformity with Generally Accepted Accounting Principles*. The Company has not determined the impact, if any, of the adoption of SFAS No. 162.

In June 2008, the FASB issued Staff Position ("FSP") Emerging Issue Task Force ("EITF") Issue No. 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* ("FSP EITF 03-6-1"). FSP EITF 03-6-1 provides that unvested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings per share pursuant to the two-class method. FSP EITF 03-6-1 is effective for fiscal years beginning after December 15, 2008. Upon adoption, a company is required to retrospectively adjust its earnings per share data, including any amounts related to interim periods, summaries of earnings and selected financial data, to conform to the provisions of FSP EITF 03-6-1. The Company has not determined the impact, if any, of the adoption of FSP EITF 03-6-1.

In December 2008, the FASB issued FSP SFAS No. 132(R)-1, Employers Disclosures about Postretirement Benefit Plan Assets ( FSP SFAS 132(R)-1 ), which requires additional disclosures for employers pension and other postretirement benefit plan assets. As pension and other postretirement benefit plan assets were not included within the scope of SFAS No. 157, FSP SFAS 132(R)-1 requires employers to disclose information about fair value measurements of plan assets similar to the disclosures required under SFAS No. 157, the investment policies and strategies for the major categories of plan assets, and significant concentrations of risk within plan assets. FSP SFAS 132(R)-1 will be effective for fiscal years ending after December 15, 2009. As FSP SFAS 132(R)-1 provides only disclosure requirements, the adoption of this standard will not have a material impact on the Company s Consolidated Financial Statements.

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**Critical Accounting Policies and Estimates**

The preparation of the financial statements in accordance with accounting principles generally accepted in the United States ( U.S. GAAP ) requires management to make judgments, estimates and assumptions regarding uncertainties that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses. Areas of uncertainty that require judgments, estimates and assumptions include items such as the accounting for derivatives; environmental matters; the testing of goodwill and other intangible assets for impairment; proceeds on assets to be sold; pensions and other postretirement benefits; and tax matters. Management uses historical experience and all available information to make its estimates and assumptions, but actual results will inevitably differ from the estimates and assumptions that are used to prepare the Company s financial statements at any given time. Despite these inherent limitations, management believes that Management s Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and related footnotes provide a meaningful and fair presentation of the Company.

Management believes that the application of these estimates and assumptions on a consistent basis enables the Company to provide the users of the financial statements with useful and reliable information about the Company s operating results and financial condition.

*Allowance for Doubtful Accounts*

The Company maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. The Company reviews the collectibility of its receivables on an ongoing basis taking into account a combination of factors. The Company reviews potential problems, such as past due accounts, a bankruptcy filing or deterioration in the customer s financial condition, to ensure the Company is adequately accrued for potential loss. Accounts are considered past due based on when payment was originally due. If a customer s situation changes, such as a bankruptcy or creditworthiness, or there is a change in the current economic climate, the Company may modify its estimate of the allowance for doubtful accounts. The Company will write off accounts receivable after reasonable collection efforts have been made and the accounts are deemed uncollectible.

*Inventory Reserve*

Inventories are valued at the lower of cost or market. Cost is determined by the last-in, first-out ( LIFO ) method at the Company s U.S. facilities. Accordingly, a LIFO valuation reserve is calculated using the dollar value link chain method.

We review the net realizable value of inventory in detail on an ongoing basis, giving consideration to deterioration, obsolescence and other factors. Based on these assessments, we provide for an inventory reserve in the period in which an impairment is identified. The reserve fluctuates with market conditions, design cycles and other economic factors.

*Goodwill and Other Intangible Assets*

Intangible assets with finite useful lives are amortized generally on a straight-line basis over the periods benefited. Goodwill and other intangible assets with indefinite useful lives are not amortized. Each year during the second quarter, the carrying value of goodwill and other intangible assets with indefinite useful lives is tested for impairment. The Company uses the discounted cash flow method to calculate the fair value of goodwill associated with its reporting units. No impairments of goodwill were deemed to exist. The determination of discounted cash flows is based on the businesses strategic plans and long-range planning forecasts. The revenue growth rates included in the plans are management s best estimates based on current and forecasted market conditions. Profit margin assumptions are projected by each business based on the current cost structures and anticipated cost reductions. There can be no assurance that operations will achieve the future cash flows reflected in the projections. If different assumptions were used in these plans, the related discounted cash flows used in measuring impairment could be different and an impairment of assets might need to be recorded. In light of the economic downturn that accelerated in the second half of 2008, management re-evaluated the impairment testing that was completed in the second quarter of 2008, and determined that an interim impairment test of goodwill was not required. Management s determination was based on the fact that the businesses strategic plans and long-range planning forecasts are still valid, the Company has not lost any significant customers, and the decline in the Company s market capitialization is in line with the comparative market indicies as shown in the Stock Performance Graph included in Item 5 of this Form 10-K.

*Pension and Other Postretirement Benefits*

The amounts recognized in the consolidated financial statements related to pension and other postretirement benefits are determined from actuarial valuations. Inherent in these valuations are assumptions about such factors as expected return on plan assets, discount rates at which liabilities could be settled, rate of increase in future compensation levels, mortality rates, and trends in health insurance costs. These assumptions are reviewed annually and updated as required. In accordance with U.S. GAAP, actual results that differ from the assumptions are accumulated and amortized over future periods and, therefore, affect the expense recognized and obligations recorded in future periods.

The discount rate used is based on comparisons to the Moody s Aa Corporate Bond index, as well as a hypothetical yield curve that creates a reference portfolio of high quality corporate bonds whose payments mimic the plan s benefit payment stream. The expected long-term rate of return on assets is developed with input from the Company s actuarial firms. Also considered is the Company s historical experience with pension fund asset performance in comparison with expected returns. The long-term rate-of-return assumption used for determining net periodic pension expense for 2008 was 8.5%. The Company reviews the long-term rate of return each year. Future actual pension income and expense will depend on future investment performance, changes in future discount rates, and various other factors related to the population of participants in the Company s pension plans.

The Company expects to make cash contributions of $1,052,000 and $135,000 to its pension plans and postretirement plan, respectively in 2009.

**RESULTS OF OPERATIONS**

**Fiscal 2008 Compared to Fiscal 2007**

The following table shows, for 2008 and 2007, selected line items from the consolidated statements of income as a percentage of net sales, by segment.

| | **2008 Industrial Hardware** | | **Security Products** | | **Metal Products** | | **Total** | |
|---|---|---|---|---|---|---|---|---|
| Net sales | 100.0 | % | 100.0 | % | 100.0 | % | 100.0 | % |
| Cost of products sold | 77.8 | % | 77.0 | % | 102.7 | % | 81.3 | % |
| Gross margin | 22.2 | % | 23.0 | % | -2.7 | % | 18.7 | % |
| Selling and administrative expense | 13.5 | % | 15.7 | % | 8.1 | % | 13.5 | % |
| Operating profit | 8.7 | % | 7.3 | % | -10.8 | % | 5.2 | % |

| | **2007 Industrial Hardware** | | **Security Products** | | **Metal Products** | | **Total** | |
|---|---|---|---|---|---|---|---|---|
| Net sales | 100.0 | % | 100.0 | % | 100.0 | % | 100.0 | % |
| Cost of products sold | 72.5 | % | 76.8 | % | 104.3 | % | 77.0 | % |
| Gross margin | 27.5 | % | 23.2 | % | -4.3 | % | 23.0 | % |
| Selling and administrative expense | 11.6 | % | 14.6 | % | 12.0 | % | 12.8 | % |
| Operating profit | 15.9 | % | 8.6 | % | -16.3 | % | 10.2 | % |

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The following table shows the amount of change from 2007 to 2008 in sales, cost of products sold, gross margin, selling and administrative expenses, and operating profit, by segment (dollars in thousands):

| | Industrial Hardware | Security Products | Metal Products | Total |
|---|---|---|---|---|
| Net sales | $ (21,561) | $ (5,560) | $ 6,718 | $ (20,403) |
| Volume | -32.2 % | -12.0 % | 29.4 % | -18.8 % |
| Prices | 1.2 % | 1.7 % | 15.1 % | 2.6 % |
| New Products | 4.6 % | 1.1 % | 3.7 % | 3.1 % |
| | -26.4 % | -9.2 % | 48.2 % | -13.1 % |
| Cost of products sold | $ (12,426) | $ (4,185) | $ 6,683 | $ (9,928) |
| | -21.0 % | -9.0 % | 46.0 % | -8.2 % |
| Gross margin | $ (9,135) | $ (1,375) | $ 35 | $ |