

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

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**FORM 10-Q**

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(Mark One)

**Quarterly Report under Section 13 OR 15(d) of the Securities Exchange Act of 1934**  
For quarterly period ended **June 30, 2019**  
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**

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**LAWSON PRODUCTS, INC.**  
(Exact name of registrant as specified in its charter)

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**Delaware**  
(State or other jurisdiction of  
incorporation or organization)

**8770 W. Bryn Mawr Avenue, Suite 900, Chicago, Illinois**  
(Address of principal executive offices)

**36-2229304**  
(I.R.S. Employer  
Identification No.)

**60631**  
(Zip Code)

**(773) 304-5050**

(Registrant's telephone number, including area code)

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

Title of each class	Trading Symbol	Name of each exchange on which registered
Common stock, \$1.00 par value	LAWS	NASDAQ Global Select Market

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

Indicate by check mark whether the registrant has submitted electronically 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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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

Large accelerated filer	<input type="checkbox"/>	Accelerated filer	<input checked="" type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/> (Do not check if a smaller reporting company)	Smaller reporting company	<input checked="" type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

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

The number of shares outstanding of the registrant's common stock, \$1 par value, as of July 15, 2019 was 8,989,343.

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**“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 expressions 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:

- the effect of general economic and market conditions;
- the ability to generate sufficient cash to fund our operating requirements;
- the ability to meet the covenant requirements of our lines of credit;
- the market price of our common stock may decline;
- inventory obsolescence;
- work stoppages and other disruptions at transportation centers or shipping ports;
- changing customer demand and product mixes;
- increases in energy costs, tariffs and the cost of raw materials, including commodity prices;
- decreases in demand from oil and gas customers due to lower oil prices;
- disruptions of our information and communication systems;
- cyber attacks or other information security breaches;
- failure to recruit, integrate and retain a talented workforce including productive sales representatives;
- the inability to successfully make or integrate acquisitions into the organization;
- foreign currency fluctuations
- failure to manage change within the organization;
- highly competitive market;
- changes that affect governmental and other tax-supported entities;
- violations of environmental protection or other governmental regulations;
- negative changes related to tax matters;
- Luther King Capital's significant influence over the Company given its ownership percentage; and
- all other factors discussed in the Company’s “Risk Factors” set forth in its Annual Report on Form 10-K for the year ended December 31, 2018.

The Company undertakes no obligation to update any such factors 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.

PART I - FINANCIAL INFORMATION

ITEM 1 - FINANCIAL STATEMENTS

Lawson Products, Inc.  
Condensed Consolidated Balance Sheets  
(Dollars in thousands, except share data)

	June 30, 2019	December 31, 2018
ASSETS	(Unaudited)	
<b>Current assets:</b>		
Cash and cash equivalents	\$ 6,915	\$ 11,883
Restricted cash	800	800
Accounts receivable, less allowance for doubtful accounts of \$596 and \$549, respectively	45,570	37,682
Inventories, net	55,360	52,887
Miscellaneous receivables and prepaid expenses	4,742	3,653
<b>Total current assets</b>	<b>113,387</b>	<b>106,905</b>
Property, plant and equipment, net	17,630	23,548
Deferred income taxes	19,021	20,592
Goodwill	20,794	20,079
Cash value of life insurance	13,167	12,599
Intangible assets, net	12,895	13,112
Lease assets	11,840	—
Other assets	298	307
<b>Total assets</b>	<b>\$ 209,032</b>	<b>\$ 197,142</b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current liabilities:</b>		
Revolving lines of credit	\$ 8,823	\$ 10,823
Accounts payable	16,550	15,207
Lease obligation	3,708	—
Accrued expenses and other liabilities	34,904	40,179
<b>Total current liabilities</b>	<b>63,985</b>	<b>66,209</b>
Security bonus plan	12,353	12,413
Lease obligation	10,500	5,213
Deferred compensation	5,670	5,304
Deferred tax liability	2,900	2,761
Other liabilities	4,292	6,069
<b>Total liabilities</b>	<b>99,700</b>	<b>97,969</b>
<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 - 9,032,948 and 9,005,716 shares, respectively		
Outstanding - 8,983,162 and 8,955,930 shares, respectively	9,033	9,006
Capital in excess of par value	16,973	15,623
Retained earnings	84,728	77,338
Treasury stock – 49,786 shares	(1,234)	(1,234)
Accumulated other comprehensive loss	(168)	(1,560)
<b>Total stockholders' equity</b>	<b>109,332</b>	<b>99,173</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 209,032</b>	<b>\$ 197,142</b>

See notes to condensed consolidated financial statements.

**Lawson Products, Inc.**  
**Condensed Consolidated Statements of Income and Comprehensive Income**  
(Dollars in thousands, except per share data)  
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Product revenue	\$ 85,996	\$ 80,397	\$ 167,911	\$ 155,367
Service revenue	10,101	9,985	19,529	19,474
<b>Total revenue</b>	<b>96,097</b>	<b>90,382</b>	<b>187,440</b>	<b>174,841</b>
Product cost of goods sold	40,580	37,856	78,587	72,688
Service costs	4,474	3,395	8,887	6,804
<b>Gross profit</b>	<b>51,043</b>	<b>49,131</b>	<b>99,966</b>	<b>95,349</b>
<b>Operating expenses:</b>				
Selling expenses	21,867	22,004	43,609	43,944
General and administrative expenses	27,553	21,573	49,190	44,014
Operating expenses	49,420	43,577	92,799	87,958
<b>Operating income</b>	<b>1,623</b>	<b>5,554</b>	<b>7,167</b>	<b>7,391</b>
Interest expense	(146)	(264)	(343)	(504)
Other income (expense), net	339	(777)	811	(490)
<b>Income before income taxes</b>	<b>1,816</b>	<b>4,513</b>	<b>7,635</b>	<b>6,397</b>
Income tax expense	509	1,319	2,182	1,967
<b>Net income</b>	<b>\$ 1,307</b>	<b>\$ 3,194</b>	<b>\$ 5,453</b>	<b>\$ 4,430</b>
<b>Basic income per share of common stock</b>	<b>\$ 0.15</b>	<b>\$ 0.36</b>	<b>\$ 0.61</b>	<b>\$ 0.50</b>
<b>Diluted income per share of common stock</b>	<b>\$ 0.14</b>	<b>\$ 0.35</b>	<b>\$ 0.58</b>	<b>\$ 0.48</b>
<b>Weighted average shares outstanding:</b>				
Basic weighted average shares outstanding	8,976	8,903	8,969	8,896
Effect of dilutive securities outstanding	405	314	379	304
Diluted weighted average shares outstanding	9,381	9,217	9,348	9,200
<b>Comprehensive income:</b>				
Net income	\$ 1,307	\$ 3,194	\$ 5,453	\$ 4,430
Other comprehensive income (loss), net of tax				
Adjustment for foreign currency translation	717	22	1,392	(1,461)
<b>Net comprehensive (loss) income</b>	<b>\$ 2,024</b>	<b>\$ 3,216</b>	<b>\$ 6,845</b>	<b>\$ 2,969</b>

See notes to condensed consolidated financial statements.

**Lawson Products, Inc.**  
**Condensed Consolidated Statements of Changes in Stockholders' Equity - 2019**  
**(Dollars in thousands)**  
**(Unaudited)**

	Common Stock		Capital in Excess of Par Value	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Outstanding Shares	\$1 Par Value					
Balance at January 1, 2019	8,955,930	\$ 9,006	\$ 15,623	\$ 77,338	\$ (1,234)	\$ (1,560)	\$ 99,173
Change in accounting principle <sup>(1)</sup>	—	—	—	1,937	—	—	1,937
Net income	—	—	—	4,146	—	—	4,146
Adjustment for foreign currency translation	—	—	—	—	—	675	675
Stock-based compensation	—	—	666	—	—	—	666
Shares issued	6,520	6	(6)	—	—	—	—
Balance at March 31, 2019	8,962,450	9,012	16,283	83,421	(1,234)	(885)	106,597
Net income	—	—	—	1,307	—	—	1,307
Adjustment for foreign currency translation	—	—	—	—	—	717	717
Stock-based compensation	—	—	711	—	—	—	711
Shares issued	20,712	21	(21)	—	—	—	—
Balance at June 30, 2019	8,983,162	\$ 9,033	\$ 16,973	\$ 84,728	\$ (1,234)	\$ (168)	\$ 109,332

(1) The Company adopted the ASC No.842, Leases (ASC 842) on January 1, 2019 using the modified retrospective approach. See Note 2 - Leases for further details.

See notes to condensed consolidated financial statements.

**Lawson Products, Inc.**  
**Condensed Consolidated Statements of Changes in Stockholders' Equity - 2018**  
**(Dollars in thousands)**  
**(Unaudited)**

	Common Stock		Capital in Excess of Par Value	Retained Earnings	Treasury Stock	Accumulated Other Comprehensive Income (Loss)	Total Stockholders' Equity
	Outstanding Shares	\$1 Par Value					
Balance at January 1, 2018	8,888,028	\$ 8,921	\$ 13,005	\$ 71,453	\$ (711)	\$ 822	\$ 93,490
Change in accounting principle <sup>(2)</sup>	—	—	—	(329)	—	—	(329)
Net income	—	—	—	1,236	—	—	1,236
Adjustment for foreign currency translation	—	—	—	—	—	(1,483)	(1,483)
Stock-based compensation	—	—	651	—	—	—	651
Shares issued	307	1	(1)	—	—	—	—
Balance at March 31, 2018	8,888,335	8,922	13,655	72,360	(711)	(661)	93,565
Net income	—	—	—	3,194	—	—	3,194
Adjustment for foreign currency translation	—	—	—	—	—	22	22
Stock-based compensation	—	—	673	—	—	—	673
Shares issued	30,304	30	(30)	—	—	—	—
Balance at June 30, 2018	8,918,639	\$ 8,952	\$ 14,298	\$ 75,554	\$ (711)	\$ (639)	\$ 97,454

(2) The Company adopted the ASC 606, Revenue from Contracts with Customers (ASC 606) on January 1, 2018 using the modified retrospective approach.

See notes to condensed consolidated financial statements.

**Lawson Products, Inc.**  
**Condensed Consolidated Statements of Cash Flows**  
(Dollars in thousands)  
(Unaudited)

	Six Months Ended June 30,	
	2019	2018
<b>Operating activities:</b>		
Net income	\$ 5,453	\$ 4,430
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Depreciation and amortization	2,933	3,365
Stock-based compensation	5,247	1,057
Deferred income taxes	1,591	1,380
Changes in operating assets and liabilities:		
Accounts receivable	(7,974)	(4,632)
Inventories	(1,882)	(682)
Prepaid expenses and other assets	(1,629)	(1,563)
Accounts payable and other liabilities	(6,406)	(1,745)
Other	434	238
<b>Net cash (used in) provided by operating activities</b>	<b>\$ (2,233)</b>	<b>\$ 1,848</b>
<b>Investing activities:</b>		
Purchases of property, plant and equipment	\$ (944)	\$ (1,428)
Business acquisition	—	(157)
<b>Net cash used in investing activities</b>	<b>\$ (944)</b>	<b>\$ (1,585)</b>
<b>Financing activities:</b>		
Net (payments on) proceeds from revolving lines of credit	\$ (2,000)	\$ 1,528
Payment of financing lease principal	(123)	—
Proceeds from stock option exercises	16	—
<b>Net cash (used in) provided by financing activities</b>	<b>\$ (2,107)</b>	<b>\$ 1,528</b>
<b>Effect of exchange rate changes on cash and cash equivalents</b>	<b>\$ 316</b>	<b>\$ (215)</b>
<b>Increase (decrease) in cash, cash equivalents and restricted cash</b>	<b>(4,968)</b>	<b>1,576</b>
Cash, cash equivalents and restricted cash at beginning of period	12,683	5,216
<b>Cash, cash equivalents and restricted cash at end of period</b>	<b>\$ 7,715</b>	<b>\$ 6,792</b>
Cash and cash equivalents	\$ 6,915	\$ 5,992
Restricted cash	800	800
Cash, cash equivalents and restricted cash	<b>\$ 7,715</b>	<b>\$ 6,792</b>
Supplemental disclosure of cash flow information		
Net cash paid for income taxes	\$ 259	\$ 1,101

See notes to condensed consolidated financial statements.



## Notes to Condensed Consolidated Financial Statements

### Note 1 — Basis of Presentation and Summary of Significant Accounting Policies

The accompanying unaudited condensed consolidated financial statements of Lawson Products, Inc. (the "Company") have been prepared in accordance with 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 generally accepted accounting principles. Reference should be made to the Company's Annual Report on Form 10-K for the year ended December 31, 2018. 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 and six month periods ended June 30, 2019 are not necessarily indicative of the results that may be expected for the year ending December 31, 2019.

The Company has two operating segments. The first segment, the Lawson operating segment, distributes maintenance, repair and operations ("MRO") products to customers primarily through a network of sales representatives offering vendor managed inventory ("VMI") service to customers throughout the United States and Canada. The second segment, The Bolt Supply House Ltd. ("Bolt Supply") operating segment, distributes MRO products primarily through its branches located in Western Canada. Bolt Supply had 14 branches in operation at the end of the second quarter 2019.

### Note 2 - Leases

In February 2016 the FASB established Topic ASC 842, Leases, by issuing Accounting Standards Update 2016-02. Lawson adopted ASC 842 as of January 1, 2019. The Company leases property used for distribution centers, office space, and Bolt branch locations throughout the US and Canada, along with various equipment located in distribution centers and corporate headquarters. The Company is also a lessor of its Decatur, Alabama property previously used in conjunction with a discontinued operation, and is a sublessor of a portion of its corporate headquarters.

#### *Lawson Operating Leases*

Lawson MRO primarily has two types of leases: leases for real estate and leases for equipment. Operating real estate leases that have a material impact on the operations of the Company are related to the Company's distribution network and headquarters. The Company possesses several additional property leases that are month to month basis and are not material in nature. Lawson MRO does not possess any leases that have residual value guarantees. Several property leases include renewal clauses which vary in length and may not include specific rent renewal amounts. The Company will revise the value of the right of use assets and associated lease liabilities when the Company is reasonably certain it will renew a lease.

The key change commencing on January 1, 2019 for the Company is the recognition of assets and liabilities of operating leases with lease terms longer than twelve months that were not previously capitalized on the balance sheet. The value of the Right Of Use ("ROU") assets and associated lease liabilities is calculated using the total cash payments over the course of the lease, discounted to the present value using the appropriate incremental borrowing rate. The right of use asset will be amortized over its useful life. Similar to deferred rent under ASC 840, the lease liability is reduced in conjunction with the lease payments made, with adjustments made to the lease liability in order to account for non-straight line cash payments through the life of the lease.

Bolt primarily leases the real estate for its branch locations as well as its distribution center in Calgary, Alberta. Bolt possesses additional property leases that are month to month and not material in nature. Bolt property leases include renewal clauses which vary in length and may not include specific rent renewal amounts. The Company will revise the value of the right of use asset and associated lease liability when the Company is reasonably certain it will renew a lease.

#### *Lease of McCook Distribution Facility*

Upon adoption of ASC 842, the previously capitalized financing asset and lease liability for the McCook distribution facility was removed from the balance sheet and re-established as a ROU asset and a lease liability as an operating lease. The Company did not include the lease renewal periods in its assessment of the McCook lease as it did not meet the reasonably certain threshold required under ASC 842. Changes in the value of the assets and liabilities associated with the property due to adoption of ASC 842 have been accounted for as an adjustment to beginning retained earnings of \$1.9 million.

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*Accounting Policy Elections*

As part of the transition to ASC 842, the Company elected the following practical expedients:

The transitional package of practical expedients as prescribed by ASC 842. Per the practical expedient for the transition to ASC 842, the Company did not reassess expired leases, existing lease classifications or initial indirect costs for existing leases in the calculation of the right to use asset and lease liability.

The Company elected the modified retrospective method of transition, which resulted in no restatement of prior period results with the adoption impact being recorded to opening retained earnings.

The Company did not capitalize short term leases, for all asset classes defined as leases with a term of shorter than twelve months, on the balance sheet. These leases have not been transitioned to ASC 842.

As a practical expedient, the Company did not reassess the accounting for initial direct costs of current leases.

The Company elected not to use the hindsight practical expedient in determining the lease term.

The Company recognizes certain lease components and non-lease components together and not as separate parts of a lease for real estate leases. The Company will exercise this practical expedient in the future by asset class.

*Significant Assumptions*

The Company is required to determine a discount rate for the present value of lease payments. If the rate is not included in the lease or cannot be readily determined, the Company must estimate the incremental borrowing rate to be used for the discount rate. The Company determined that Lawson MRO and Bolt have different discount rates for leases, as both reporting units have separate borrowing agreements. The Lawson MRO segment will discount the present value of the total payments for the operating and financing leases using the incremental borrowing rate of 5.5%, given the similarity of the lease terms amongst asset classes. The Bolt segment will discount the present value of the total payments of each operating and financing lease at its incremental borrowing rate of 4.2%. The discount rate of Lawson MRO and Bolt will be reviewed on a periodic basis and updated as needed.

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The expenses and income generated by the leasing activity of Lawson as lessee for the three and six months ending June 30, 2019 are as follows (Dollars in thousands):

Lease Type	Classification	Three Months Ending June 30, 2019	Six Months Ending June 30, 2019
Consolidated Operating Lease Expense <sup>(1)</sup>	Operating expenses	\$ 1,227	\$ 2,502
Consolidated Financing Lease Amortization	Operating expenses	51	99
Consolidated Financing Lease Interest	Interest expense	7	13
Consolidated Financing Lease Expense		58	112
Sublease Income <sup>(2)</sup>	Operating expenses	(80)	(160)
Net Lease Cost		\$ 1,205	\$ 2,454

<sup>(1)</sup> Includes short term lease expense, which is immaterial

<sup>(2)</sup> Sublease income from sublease of a portion of the Company headquarters. The sublease was terminated in June 2019 and the Company has no other subleases.

The Company recorded \$1.1 million of operating lease expense in the second quarter of 2018 and \$2.2 million of operating lease expense in the first two quarters of 2018.

The value of the net assets and liabilities generated by the leasing activity of Lawson as lessee as of June 30, 2019 are as follows (Dollars in thousands):

Lease Type	Amount
Total ROU operating lease assets <sup>(1)</sup>	\$ 11,142
Total ROU financing lease assets <sup>(2)</sup>	698
Total lease assets	\$ 11,840
Total current operating lease obligation	\$ 3,434
Total current financing lease obligation	274
Total current lease obligations	\$ 3,708
Total long term operating lease obligation	\$ 10,089
Total long term financing lease obligation	411
Total long term lease obligation	\$ 10,500

<sup>(1)</sup> Operating lease assets are recorded net of accumulated amortization of \$1.4 million as of June 30, 2019

<sup>(2)</sup> Financing lease assets are recorded net of accumulated amortization of \$0.1 million as of June 30, 2019

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The value of the lease liabilities generated by the leasing activities of Lawson as lessee as of June 30, 2019 were as follows (Dollars in thousands):

<b>Maturity Date of Lease Liabilities</b>	<b>Operating Leases</b>	<b>Financing Leases</b>	<b>Total</b>
Year one	\$ 4,032	\$ 267	\$ 4,299
Year two	4,044	240	4,284
Year three	3,981	126	4,107
Year four	1,880	79	1,959
Year five	845	25	870
Subsequent years	55	—	55
Total lease payments	14,837	737	15,574
Less: Interest	1,314	52	1,366
Present value of lease liabilities	\$ 13,523	\$ 685	\$ 14,208

The Company's future minimum lease commitments as of December 31, 2018, were as follows (Dollars in thousands):

<b>Maturity Date of Lease Liabilities</b>	<b>Operating Leases <sup>(2)(3)</sup></b>	<b>Financing Lease <sup>(3)(4)</sup></b>	<b>Capital Leases <sup>(4)</sup></b>
Year one	\$ 2,574	\$ 1,395	\$ 201
Year two	2,369	1,444	155
Year three	2,349	1,493	91
Year four	2,008	760	11
Year five	1,130	—	—
Subsequent years	374	—	—
Total lease payments <sup>(1)</sup>	\$ 10,804	\$ 5,092	\$ 458

- (1) Minimum lease payments exclude payments to landlord for real estate taxes and common area maintenance
- (2) On January 1, 2019, the Company elected the modified retrospective method of transition to adopt the new lease standard ASC 842, which resulted in no restatement of prior period results. At December 31, 2018, prior to adoption of the new lease standard, operating lease obligations were not included as a liability on the balance sheet. Therefore, the operating lease obligations are included in the table for comparative purposes only and the total lease liability is not included as it is not applicable
- (3) The \$5.1 million minimum lease obligation attributable to the McCook lease that was classified as a financing lease on December 31, 2018 was reclassified as an operating lease under the new accounting standard adopted on January 1, 2019
- (4) Lease obligations classified as capital leases on December 31, 2018 were reclassified as financing leases under the new lease standard adopted on January 1, 2019

The weighted average lease terms and interest rates of the leases held by Lawson as of June 30, 2019 are as follows:

<b>Lease Type</b>	<b>Weighted Average Term in Years</b>	<b>Weighted Average Interest Rate</b>
Operating Leases	3.8	5.2%
Financing Leases	3.2	5.5%

The cash outflows of the leasing activity of Lawson as lessee for the six months ending June 30, 2019 are as follows (Dollars in thousands):

<b>Cash Flow Source</b>	<b>Classification</b>	<b>Amount</b>
Operating cash flows from operating leases	Operating activities	\$ 1,857
Operating cash flows from financing leases	Operating activities	7
Financing cash flows from financing leases	Financing activities	123

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*Lawson as Lessor*

The Company is a lessor of its facility in Decatur, Alabama, which was previously used in conjunction with a discontinued operation. The lease expires in February, 2024. Both the lessor and lessee have a put option to each other upon the completion of the remediation of the environmental matter at a pre-negotiated price less 50% of the rent paid upon the put option being exercised. The net book value at June 30, 2019 is \$0.4 million. The Company classifies this lease as an operating lease. The operating lease of the Decatur facility generated approximately \$0.1 million of income to the Company for the six months ending June 30, 2019.

Annual lease income classified as operating expenses of \$0.2 million is anticipated through the earlier of the put option exercise or February, 2024.

**Note 3 - Revenue Recognition**

*Adoption of ASC 606*

On January 1, 2018 the Company adopted Accounting Standards Codification 606-Revenue From Contracts With Customers ("ASC 606"). As part of the Company's adoption of ASC 606, it concluded that it has two separate performance obligations, and accordingly, two separate revenue streams: products and services. As a result, the Company reports two separate revenue streams and two separate costs of revenues.

ASC 606 defines a five step process to recognize revenues at the time and in an amount that reflects the consideration expected to be received for the performance obligations that have been provided. ASC 606 defines contracts as written, oral and through customary business practice. Under this definition, the Company considers contracts to be created at the time an order to purchase product is agreed upon regardless of whether or not there is a written contract.

*Performance Obligations*

Lawson has two operating segments; the Lawson segment and the Bolt Supply segment. Customer contracts have the following performance obligations:

The Lawson segment has two distinct performance obligations offered to its customers: a product performance obligation and a service performance obligation. Although the Company has identified that it offers its customers both a product and a service obligation, the customer only receives one invoice per transaction with no price breakout between these obligations. The Company does not price its offerings based on any breakout between these obligations.

Lawson generates revenue primarily from the sale of MRO products to its customers. Revenue related to product sales is recognized at the time that control of the product has been transferred to the customer: either at the time the product is shipped or the time the product has been received by the customer. The Company does not commit to long-term contracts to sell customers a certain minimum quantity of products.

The Lawson segment offers a VMI service proposition to its customers. A portion of these services, primarily related to stocking of product and maintenance of the MRO inventory, is provided a short period of time after control of the purchased product has been transferred to the customer. Since some components of VMI service have not been provided at the time the control of the product transfers to the customer, that portion of expected consideration is deferred until the time that those services have been provided.

The Bolt Supply segment does not provide VMI services for its customers or provide services in addition to product sales to customers. Revenue is recognized at the time that control of the product has been transferred to the customer which is either upon delivery or shipment depending on the terms of the contract.

*Accounting Policy Elections*

The Company has elected to treat shipping and handling costs after the control of the product has been transferred to the customer as a fulfillment cost.

Sales taxes that are imposed on our sales and collected from customers are excluded from revenues.

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The Company expenses sales commissions when incurred as the amortization period is one year or less.

#### Significant Judgments

The Company employs certain significant judgments to estimate the dollar amount of revenue, and related expenses, allocated to the sale of product and service. These judgments include, among others, the percentage of customers that take advantage of the VMI services offered, the amount of revenue to be allocated to the VMI service based on the value of the service to its customers, and the amount of time after control of the product passes to the customer that the VMI service obligation is completed. It is assumed that any customer who averages placing orders at a frequency of longer than 30 days does not take advantage of the available VMI services offered. The estimate of the cost of sales is based on expenses directly related to sales representatives that provide direct VMI services to the customer.

#### Financial Impact of ASC 606 Adoption

As a result of applying ASC 606 the Company recorded a liability of \$0.7 million for deferred revenue on January 1, 2018. Expenses related to these revenues of \$0.4 million were also deferred resulting in a net reduction to opening retained earnings of \$0.3 million as of January 1, 2018. At June 30, 2019, the Company had a deferred revenue liability of \$0.7 million and a deferred expense of \$0.3 million for related expenses associated with the deferred service performance obligations, respectively. The deferral of revenue and expenses does not affect the amount, timing and any uncertainty of cash flows generated from operations.

Disaggregated revenue by geographic area follows:

(Dollars in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
United States	\$ 76,119	\$ 71,626	\$ 150,167	\$ 139,944
Canada	19,978	18,756	37,273	34,897
Consolidated total	<u>\$ 96,097</u>	<u>\$ 90,382</u>	<u>\$ 187,440</u>	<u>\$ 174,841</u>

Disaggregated revenue by product type follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
Fastening Systems	24.3%	24.6%	23.9%	24.4%
Fluid Power	15.2%	14.8%	15.2%	14.7%
Cutting Tools and Abrasives	13.0%	13.4%	13.1%	12.3%
Specialty Chemicals	11.7%	12.3%	11.5%	13.4%
Electrical	10.7%	10.8%	11.1%	11.0%
Aftermarket Automotive Supplies	7.6%	7.8%	8.0%	8.2%
Safety	4.7%	4.7%	4.7%	4.7%
Welding and Metal Repair	1.6%	2.1%	1.7%	2.0%
Other	11.2%	9.5%	10.8%	9.3%
Consolidated Total	<u>100.0%</u>	<u>100.0%</u>	<u>100.0 %</u>	<u>100.0 %</u>

#### Note 4 — Restricted Cash

The Company has agreed to maintain \$0.8 million in a money market account as collateral for an outside party that is providing certain commercial card processing services for the Company. The Company is restricted from withdrawing this balance without the prior consent of the outside party during the term of the agreement.

**Note 5 — Inventories, Net**

Inventories, net, consisting primarily of purchased goods which are offered for resale, were as follows:

	(Dollars in thousands)	
	June 30, 2019	December 31, 2018
Inventories, gross	\$ 60,144	\$ 58,215
Reserve for obsolete and excess inventory	(4,784)	(5,328)
Inventories, net	<u>\$ 55,360</u>	<u>\$ 52,887</u>

**Note 6 - Goodwill**

Goodwill activity for the first six months of 2019 and 2018 is included in the table below:

	(Dollars in thousands)	
	Six Months Ended June 30,	
	2019	2018
Beginning balance	\$ 20,079	\$ 19,614
Adjustment to original acquisition allocation	2	(17)
Impact of foreign exchange	713	(793)
Ending balance	<u>\$ 20,794</u>	<u>\$ 18,804</u>

**Note 7 - Intangible Assets**

The gross carrying amount and accumulated amortization by intangible asset class were as follows:

	(Dollars in thousands)					
	June 30, 2019			December 31, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value	Gross Carrying Amount	Accumulated Amortization	Net Carrying Value
Trade names	\$ 8,367	\$ (1,741)	\$ 6,626	\$ 8,090	\$ (1,447)	\$ 6,643
Customer relationships	7,301	(1,032)	6,269	7,114	(645)	6,469
	<u>\$ 15,668</u>	<u>\$ (2,773)</u>	<u>\$ 12,895</u>	<u>\$ 15,204</u>	<u>\$ (2,092)</u>	<u>\$ 13,112</u>

Amortization expense of \$0.7 million and \$0.4 million related to intangible assets was recorded in General and administrative expenses for the six months ended June 30, 2019 and 2018, respectively.

**Note 8 — Loan Agreement**

Lawson Loan Agreement

In 2012, the Company entered into a Loan and Security Agreement (“Loan Agreement”). The Loan Agreement consists of a \$40.0 million revolving line of credit facility, which includes a \$10.0 million sub-facility for letters of credit. Certain terms of the original Loan Agreement have been revised by subsequent amendments.

The Loan Agreement, as amended, expires in August 2020. Due to the lock box arrangement and a subjective acceleration clause contained in the Loan Agreement, any outstanding borrowings under the revolving line of credit are classified as a current liability.

Currently, credit available under the Loan Agreement, as amended, is based upon:

- a) 85% of the face amount of the Company’s eligible accounts receivable, generally less than 60 days past due, and
- b) the lesser of 60% of the lower of cost or market value of the Company’s eligible inventory, generally inventory expected to be sold within 18 months, or \$20.0 million.

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The applicable interest rates for borrowings are at the Prime rate or, if the Company elects, the LIBOR rate plus 1.50% to 1.85% based on the Company's debt to EBITDA ratio. The Loan Agreement is secured by a first priority perfected security interest in substantially all existing assets of the Company. Dividends are restricted to amounts not to exceed \$7.0 million annually.

At June 30, 2019, the Company had \$6.0 million of borrowings under its revolving line of credit facility and additional borrowing availability of \$30.7 million. The Company paid interest of \$0.4 million and \$0.5 million for the six months ended June 30, 2019 and 2018, respectively. The weighted average interest rate was 4.48% and 3.74% for the six months ended June 30, 2019 and 2018, respectively.

In the second quarter of 2019, the Company's Board of Directors authorized a program in which the Company may repurchase up to \$7.5 million of the Company's common stock from time to time in open market transactions, privately negotiated transactions or by other methods.

In addition to other customary representations, warranties and covenants, if the excess borrowing capacity is below \$10.0 million the Company is required to meet a minimum trailing twelve month EBITDA to fixed charges ratio, as defined in the amended Loan Agreement. On June 30, 2019, the Company's borrowing capacity exceeded \$10.0 million. Therefore, the Company was not subject to this financial covenant, however, for informational purposes the result of the financial covenant is provided below:

Quarterly Financial Covenant	Requirement	Actual
EBITDA to fixed charges ratio	1.10 : 1.00	7.55 : 1.00

Commitment Letter

Bolt Supply has a Commitment Letter with BMO Bank of Montreal ("BMO") dated March 30, 2017 which allows Bolt Supply to access up to \$5.5 million Canadian dollars in the form of either an overdraft facility or as commercial letters of credit. The Commitment Letter is cancellable at any time at BMO's sole discretion and is secured by substantially all of Bolt Supply's assets. It carries an interest rate of the bank's prime rate plus 0.25%. At June 30, 2019, Bolt Supply had \$3.7 million Canadian dollars of outstanding borrowings and remaining borrowing availability of \$1.8 million Canadian dollars. The Commitment Letter is subject to a working capital ratio of 1.35:1, a maximum ratio of debt to tangible net worth of 2.5:1 of the Bolt Supply assets and Debt Service Coverage Ratio 1.25:1 as defined in the Commitment Letter. At June 30, 2019, Bolt Supply was in compliance with all covenants which are subject to periodic review, at least annually, with the next review due by August 31, 2019.

**Note 9 — Severance Reserve**

Changes in the Company's reserve for severance as of June 30, 2019 and 2018 were as follows:

	(Dollars in thousands)	
	Six Months Ended June 30,	
	2019	2018
Balance at beginning of period	\$ 359	\$ 483
Charged to earnings	1,512	692
Payments	(409)	(532)
Balance at end of period	<u>\$ 1,462</u>	<u>\$ 643</u>



#### **Note 10 — Stock-Based Compensation**

The Company recorded stock-based compensation expense of \$5.2 million and \$1.1 million for the first six months of 2019 and 2018, respectively. A portion of stock-based compensation is related to the change in the market value of the Company's common stock.

A summary of stock-based awards issued during the six months ended June 30, 2019 follows:

##### Stock Performance Rights ("SPRs")

The Company issued 25,793 SPRs to key employees with an exercise price of \$30.54 per share that cliff vest on December 31, 2021 and have a termination date of December 31, 2026. SPRs entitle the recipient to receive a cash payment equal to the excess of the market value of the Company's common stock over the SPR exercise price when the SPRs are surrendered.

##### Restricted Stock Units ("RSUs")

The Company issued 10,045 RSUs to certain members of the Company's Board of Directors with a vesting date of May 14, 2020. The Company issued 16,781 RSUs to key employees that cliff vest on December 31, 2021. Each RSU is exchangeable for one share of the Company's common stock at the end of the vesting period.

##### Market Stock Units ("MSUs")

The Company issued 39,948 MSUs to key employees that cliff vest on December 31, 2021. MSU's are exchangeable for the Company's common stock at the end of the vesting period. The number of shares of common stock that will be issued upon vesting, ranging from zero to 59,922, will be determined based upon the trailing sixty-day weighted average closing price of the Company's common stock on December 31, 2021.

No stock options were excluded from the computation of diluted earnings per share for the three months ended June 30, 2019. For the three months ended June 30, 2018, stock options to purchase approximately 80,000 shares of the Company's common stock were excluded from the computation of diluted earnings per share because they were anti-dilutive. For the six months ended June 30, 2019 and 2018, stock options to purchase approximately 9,524 and 63,210 shares of the Company's common stock were excluded from the computation of diluted earnings per share because they were anti-dilutive.

#### **Note 11 — Income Taxes**

The Company recorded income tax expenses of \$2.2 million, a 28.6% effective tax rate for the six months ended June 30, 2019 and an income tax expense of \$2.0 million, a 30.7% effective tax rate for the six months ended June 30, 2018. The effective tax rates were higher than the U.S. statutory rate due primarily to state taxes, income in higher tax jurisdictions and an inclusion for global intangible low taxed income.

The Company and its subsidiaries are subject to U.S. Federal income tax, as well as income tax of multiple state and foreign jurisdictions. As of June 30, 2019, the Company is subject to U.S. Federal income tax examinations for the years 2015 through 2017 and income tax examinations from various other jurisdictions for the years 2011 through 2018.

Earnings from the Company's foreign subsidiaries are considered to be indefinitely reinvested. A distribution of these non-U.S. earnings in the form of dividends or otherwise may subject the Company to foreign withholding taxes and U.S. federal and state taxes.

#### **Note 12 — Contingent Liabilities**

In 2012, the Company identified that a site it owns in Decatur, Alabama, contains hazardous substances in the soil and groundwater as a result of historical operations prior to the Company's ownership. The Company retained an environmental consulting firm to further investigate the contamination including the measurement and monitoring of the site and the site was enrolled in the Alabama Department of Environmental Management ("ADEM") voluntary cleanup program.

The remediation plan was approved by ADEM in 2018. The plan consists of chemical injections throughout the affected area, as well as subsequent monitoring of the area for three consecutive periods. The injection process was completed in the first quarter of 2019 and the environmental consulting firm is monitoring the affected area. The Company made payments of \$1.3 million in the first two quarters of 2019 for services rendered by the environmental consulting firm. These payments were applied to the previously accrued environmental remediation liability. The Company believes the remaining environmental remediation liability of approximately \$0.1 million, classified within Accrued expenses and other liabilities on the accompanying Consolidated Balance

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Sheet, will be sufficient to cover the remaining cost of the plan. The Company does not expect to capitalize any amounts related to the remediation plan.

**Note 13 — Acquisition**

The Company completed the acquisition of Screw Products, Inc. in October 2018 for approximately \$5.2 million. The purchase price was funded with cash on hand and utilization of the Company's existing credit facility. Screw Products, Inc. is a distributor of bulk industrial products to large manufacturers and job shops. The Company allocated \$2.6 million of the purchase price to an intangible asset for customer relationships and \$0.5 million for intangible asset for trade names. These amounts were determined by a third party valuation firm with estimated useful lives of 10 and 15 years, respectively. The excess of the purchase price over the fair values of the identifiable assets and liabilities was recorded as goodwill and represents the expected future benefit to the Company from the acquisition of Screw Products. The Company's Lawson operating segment includes revenues of approximately \$0.7 million and \$1.5 million from Screw Products in the three and six months ended June, 30 2019, respectively.

The following table contains unaudited pro forma revenue and net income for Lawson Products assuming the Screw Products acquisition closed on January 1, 2018.

	(Dollars in thousands)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
<b>Revenue</b>				
Actual	\$ 96,097	\$ 90,382	\$ 187,440	\$ 174,841
Pro forma	96,097	91,261	187,440	176,469
<b>Net income</b>				
Actual	\$ 1,307	\$ 3,194	\$ 5,453	\$ 4,430
Pro forma	1,307	3,308	5,453	4,632

The pro forma disclosures in the table above include adjustments for, amortization of intangible assets and acquisition costs to reflect results as if the acquisition of Screw Products had closed on January 1, 2018 rather than on the actual acquisition date. This pro forma information utilizes certain estimates, is presented for illustrative purposes only and is not intended to be indicative of the actual results of operation. In addition, future results may vary significantly from the results reflected in the pro forma information. The unaudited pro forma financial information does not reflect the impact of future positive or negative events that may occur after the acquisition, such as anticipated cost savings from operating synergies.

**Note 14 – Segment Information**

The Company operates in two reportable segments. The businesses have been determined to be separate reportable segments because of differences in their financial characteristics and the methods they employ to deliver product to customers. The operating segments are reviewed by the Company's chief operating decision maker responsible for reviewing operating performance and allocating resources. The Lawson segment primarily relies on its large network of sales representatives to visit the customer at the customers' work location and provide VMI service and produce sales orders for product that is then shipped to the customer. The Bolt Supply segment primarily sells product to customers through its branch locations. Bolt Supply had 14 branches in operation at the end of the second quarter 2019.

Financial information for the Company's reportable segments follows:

	(Dollars in thousands)			
	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	2018	2019	2018
<b>Revenue</b>				
Lawson product revenue	\$ 74,866	\$ 70,632	\$ 147,905	\$ 137,569
Lawson service revenue	10,101	9,985	19,529	19,474
Total Lawson revenue	84,967	80,617	167,434	157,043
Bolt Supply	11,130	9,765	20,006	17,798
Consolidated total	<u>\$ 96,097</u>	<u>\$ 90,382</u>	<u>\$ 187,440</u>	<u>\$ 174,841</u>
<b>Gross profit</b>				
Lawson product gross profit	\$ 41,130	\$ 38,707	\$ 81,734	\$ 75,549
Lawson service gross profit	5,627	6,590	10,642	12,670
Total Lawson gross profit	46,757	45,297	92,376	88,219
Bolt Supply	4,286	3,834	7,590	7,130
Consolidated total	<u>\$ 51,043</u>	<u>\$ 49,131</u>	<u>\$ 99,966</u>	<u>\$ 95,349</u>
<b>Operating income</b>				
Lawson	\$ 654	\$ 4,794	\$ 6,113	\$ 6,284
Bolt Supply	969	760	1,054	1,107
Consolidated total	1,623	5,554	7,167	7,391
Interest expense	(146)	(264)	(343)	(504)
Other income (expense), net	339	(777)	811	(490)
Income before income taxes	<u>\$ 1,816</u>	<u>\$ 4,513</u>	<u>\$ 7,635</u>	<u>\$ 6,397</u>

**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS****Overview**

The Maintenance, Repair and Operations ("MRO") distribution industry is highly fragmented. We compete for business with several national distributors as well as a large number of regional and local distributors. The MRO business is significantly impacted by the overall strength of the manufacturing sector of the U.S. economy. One measure used to evaluate the strength of the industrial products market is the PMI index published by the Institute for Supply Management, which is considered by many economists to be a reliable near-term economic barometer of the manufacturing sector. A measure above 50 generally indicates expansion of the manufacturing sector while a measure below 50 generally represents contraction. The average monthly PMI was 52.2 in the second quarter of 2019 compared to 58.9 in the second quarter of 2018, indicating the U.S. manufacturing economy continues to grow, but at a slower pace than a year ago.

Our sales are also affected by the number of sales representatives and their productivity. Our sales force increased to an average of 980 sales representatives in the second quarter of 2019 from 966 sales representatives during the second quarter of 2018. Our Lawson segment sales representative productivity, measured as sales per rep per day, increased 3.0% to \$1,343 in the second quarter of 2019 from \$1,304 in the second quarter of 2018. Sales in 2019 also benefited from the acquisition of Screw Products, Inc. ("Screw Products") in the fourth quarter of 2018. We anticipate the size of our sales force to remain relatively stable for the remainder of 2019 as we concentrate our efforts on providing training and support to continue to increase the productivity of our existing sales representatives.

**Quarter ended June 30, 2019 compared to quarter ended June 30, 2018**

(Dollars in thousands)	2019		2018	
	Amount	% of Net Sales	Amount	% of Net Sales
Revenue	\$ 96,097	100.0 %	\$ 90,382	100.0 %
Cost of goods sold	45,054	46.9 %	41,251	45.6 %
Gross profit	51,043	53.1 %	49,131	54.4 %
Operating expenses:				
Selling expenses	21,867	22.8 %	22,004	24.3 %
General and administrative expenses	27,553	28.6 %	21,573	24.0 %
Total operating expenses	49,420	51.4 %	43,577	48.3 %
Operating income	1,623	1.7 %	5,554	6.1 %
Interest expense	(146)	(0.2)%	(264)	(0.2)%
Other income (expense), net	339	0.4 %	(777)	(0.9)%
Income before income taxes	1,816	1.9 %	4,513	5.0 %
Income tax expense	509	0.5 %	1,319	1.5 %
Net income	\$ 1,307	1.4 %	\$ 3,194	3.5 %

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*Revenue and Gross Profits*

(Dollars in thousands)	Three Months Ended June 30,		Increase	
	2019	2018	Amount	%
<b>Revenue</b>				
Lawson	\$ 84,967	\$ 80,617	\$ 4,350	5.4%
Bolt Supply	11,130	9,765	1,365	14.0%
Consolidated	<u>\$ 96,097</u>	<u>\$ 90,382</u>	<u>\$ 5,715</u>	6.3%
<b>Gross profit</b>				
Lawson	\$ 46,757	\$ 45,297	\$ 1,460	3.2%
Bolt Supply	4,286	3,834	452	11.8%
Consolidated	<u>\$ 51,043</u>	<u>\$ 49,131</u>	<u>\$ 1,912</u>	3.9%
<b>Gross profit margin</b>				
Lawson	55.0%	56.2%		
Bolt Supply	38.5%	39.3%		
Consolidated	53.1%	54.4%		

Total sales increased 6.3% to \$96.1 million in the second quarter of 2019 compared to \$90.4 million in the second quarter of 2018. The Lawson segment total sales were positively impacted by a 3.0% improvement in sales productivity of Lawson sales representatives and a solid MRO marketplace. A 14.0% improvement in Bolt Supply sales spread across multiple product categories and the inclusion of Screw Products sales of \$0.7 million which was acquired in the fourth quarter of 2018, also contributed to the increase. Average daily sales grew to \$1.502 million in the second quarter of 2019 compared to \$1.412 million in the prior year quarter with 64 selling days in both quarters. Excluding the impact of currency fluctuations, consolidated sales increased 7.1% for the quarter.

*Gross Profit*

Gross profit increased \$1.9 million to \$51.0 million in the second quarter of 2019 compared to \$49.1 million in the second quarter of 2018, primarily driven by increased sales, partially offset by an increase of service-related costs. Consolidated gross profit as a percent of sales was 53.1% compared to 54.4% a year ago. Lower gross margin profiles on both the Bolt Supply and Screw Products businesses also drove the lower consolidated percentage. The organic Lawson MRO segment gross margin as a percent of sales of 60.5% in the second quarter 2019 was essentially flat compared to a year ago before giving effect to the service-related costs.

*Selling, General and Administrative Expenses*

(Dollars in thousands)	Three Months Ended June 30,		Increase (Decrease)	
	2019	2018	Amount	%
<b>Selling expenses</b>				
Lawson	\$ 20,979	\$ 21,199	\$ (220)	(1.0)%
Bolt Supply	888	805	83	10.3%
Consolidated	<u>\$ 21,867</u>	<u>\$ 22,004</u>	<u>\$ (137)</u>	(0.6)%
<b>General and administrative expenses</b>				
Lawson	\$ 25,124	\$ 19,304	\$ 5,820	30.1%
Bolt Supply	2,429	2,269	160	7.1%
Consolidated	<u>\$ 27,553</u>	<u>\$ 21,573</u>	<u>\$ 5,980</u>	27.7%

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Selling expenses consist of compensation and support for our sales representatives. Selling expenses were \$21.9 million in the second quarter of 2019, essentially flat compared to \$22.0 million in the prior year quarter and, as a percent of sales, decreased to 22.8% from 24.3% in the second quarter of 2018. The decrease in selling expense as a percent of sales is primarily due to leveraging selling expenses over a higher sales base and an increase in service-related costs classified within gross profit.

General and administrative expenses consist of expenses to operate our distribution network and overhead expenses to manage the business. General and administrative expenses increased to \$27.6 million in the second quarter of 2019 from \$21.6 million in the prior year quarter. The increase was primarily driven by the \$4.8 million of stock based compensation expense, of which a portion fluctuates with the Company's stock price, and an increase in severance expense of \$1.4 million. During the second quarter of 2019 the Company incurred \$1.5 million of severance expense primarily related to the elimination of certain positions to better align various operating areas within the Company.

### *Interest Expense*

Interest expense decreased to \$0.1 million compared to \$0.3 million in the second quarter of 2019 and 2018 due to lower average debt balances.

### *Other Income (Expense), Net*

Other income (expense), net increased \$1.1 million in the second quarter of 2019 over the prior year quarter primarily due to the effect of changes in the Canadian currency exchange rate.

### *Income Tax Expense*

Income tax expense was \$0.5 million, resulting in a 28.0% effective tax rate for the three months ended June 30, 2019 compared to income tax expense of \$1.3 million and an effective tax rate of 29.2% for the three months ended June 30, 2018.

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**Six months ended June 30, 2019 compared to June 30, 2018**

(\$ in thousands)	2019		2018	
	Amount	% of Net Sales	Amount	% of Net Sales
Revenue	\$ 187,440	100.0 %	\$ 174,841	100.0 %
Cost of goods sold	87,474	46.7 %	79,492	45.5 %
Gross profit	99,966	53.3 %	95,349	54.5 %
<b>Operating expenses:</b>				
Selling expenses	43,609	23.3 %	43,944	25.1 %
General and administrative expenses	49,190	26.2 %	44,014	25.2 %
Total operating expenses	92,799	49.5 %	87,958	50.3 %
Operating income	7,167	3.8 %	7,391	4.2 %
Interest expense	(343)	(0.2)%	(504)	(0.3)%
Other income (expense), net	811	0.5 %	(490)	(0.2)%
Income before income taxes	7,635	4.1 %	6,397	3.7 %
Income tax expense	2,182	1.2 %	1,967	1.2 %
Net income	\$ 5,453	2.9 %	\$ 4,430	2.5 %

*Revenue and Gross Profit*

(Dollars in thousands)	Six Months Ended June 30,		Increase	
	2019	2018	Amount	%
<b>Revenue</b>				
Lawson	\$ 167,434	\$ 157,043	\$ 10,391	6.6%
Bolt Supply	20,006	17,798	2,208	12.4%
Consolidated	\$ 187,440	\$ 174,841	\$ 12,599	7.2%
<b>Gross profit</b>				
Lawson	\$ 92,376	\$ 88,219	\$ 4,157	4.7%
Bolt Supply	7,590	7,130	460	6.5%
Consolidated	\$ 99,966	\$ 95,349	\$ 4,617	4.8%
<b>Gross profit margin</b>				
Lawson	55.2%	56.2%		
Bolt Supply	37.9%	40.1%		
Consolidated	53.3%	54.5%		

*Revenue*

Revenue for the six months ended June 30, 2019 increased 7.2% to \$187.4 million from \$174.8 million for the six months ended June 30, 2018. The Lawson segment total sales were positively impacted by a 3.7% improvement in sales productivity of Lawson sales representatives and a strong MRO marketplace. A 12.4% improvement in Bolt Supply sales spread across multiple product categories and the inclusion of Screw Products sales of \$1.5 million which was acquired in the fourth quarter of 2018, also contributed to the increase. Average daily sales improved 7.2% to \$1.476 million in the first six months of 2019 compared to \$1.377 million in the prior year period with 127 selling days in both periods. Excluding the impact of currency fluctuations, consolidated sales increased 8.1% for the year to date.

[Table of Contents](#)*Gross Profit*

Gross profit increased to \$100.0 million in the first six months of 2019 compared to \$95.3 million in the first six months of 2018, primarily driven by increased sales. Consolidated gross profit as a percent of sales was 53.3% compared to 54.5% a year ago. Higher service-related costs and lower gross margin profiles on both the Bolt Supply and Screw Products businesses drove the lower consolidated percentage. Excluding these businesses, the core Lawson MRO segment gross margin as a percent of sales was 60.6% in the first half of 2019 compared to 60.5% a year ago before giving effect to the allocated service costs.

*Selling, General and Administrative Expenses*

(Dollars in thousands)	Six Months Ended June 30,		Increase (Decrease)	
	2019	2018	Amount	%
<b>Selling expenses</b>				
Lawson	\$ 41,932	\$ 42,498	\$ (566)	(1.3)%
Bolt Supply	1,677	1,446	231	16.0%
Consolidated	<u>\$ 43,609</u>	<u>\$ 43,944</u>	<u>\$ (335)</u>	<u>(0.8)%</u>
<b>General and administrative expenses</b>				
Lawson	\$ 44,331	\$ 39,437	\$ 4,894	12.4%
Bolt Supply	4,859	4,577	282	6.2%
Consolidated	<u>\$ 49,190</u>	<u>\$ 44,014</u>	<u>\$ 5,176</u>	<u>11.8%</u>

Selling expenses decreased to \$43.6 million for the first six months of 2019 from \$43.9 million in the first six months of 2018 and, as a percent of sales, decreased to 23.3% in the first six months of 2019 from 25.1% a year ago. The decrease in selling expense as a percent of sales is primarily due to leveraging selling expenses over a higher sales base and an increase of service-related costs within gross profit.

General and administrative expenses increased to \$49.2 million in the first six months of 2019 from \$44.0 million in the prior year period primarily driven by increased stock-based compensation expense of \$4.2 million, a portion of which varies with the company stock price, and increased severance expense of \$0.8 million. During the second quarter of 2019 the Company incurred \$1.5 million of severance expense primarily related to the elimination of certain positions to better align various operating areas within the Company.

*Interest Expense*

Interest expenses decreased \$0.2 million in the first six months of 2019, over the prior year, due primarily to lower average borrowings outstanding.

*Other Income (Expense), Net*

Other income (expense), net increased \$1.3 million in the first six months of 2019, primarily due to the effect of changes in the Canadian currency exchange rate.

*Income Tax Expense*

Income tax expenses were \$2.2 million resulting in a 28.6% effective tax rate for the first six months of 2019 compared to income tax expense of \$2.0 million and a 30.7% effective tax rate for the first six months of 2018.



## **Liquidity and Capital Resources**

Available cash and cash equivalents were \$6.9 million on June 30, 2019 compared to \$11.9 million on December 31, 2018. Net cash used in operations for the six months ended June 30, 2019 was \$2.2 million. Net cash generated by operations for the six months ended June 30, 2018 was \$1.8 million. Cash generated by operating earnings was partially offset by an increase in accounts receivable, primarily to support the increase in sales, and payments primarily for incentives, environmental remediation and other accruals that existed at December 31, 2018.

Capital expenditures, primarily for improvements to our distribution centers and information technology, were \$0.9 million and \$1.4 million for the six month periods ended June 30, 2019 and 2018, respectively.

The Company used \$2.1 million in financing activities in the first six months of 2019 primarily through a net paydown on its revolving lines of credit.

In the second quarter of 2019, our Board of Directors authorized a program in which we may repurchase up to \$7.5 million of our common stock from time to time in open market transactions, privately negotiated transactions or by other methods.

We believe cash provided by operations and funds available under our Loan Agreements are sufficient to fund our operating requirements, strategic initiatives and capital improvements for the next 12 months.

### *Lawson Loan Agreement*

On June 30, 2019, we had \$6.0 million of borrowings under our Lawson revolving line of credit facility and we had additional borrowing availability of \$30.7 million. Dividends are currently restricted under the Lawson Loan Agreement to amounts not to exceed \$7.0 million annually and no dividends were paid to shareholders in the six months ended June 30, 2019 and 2018.

In addition to other customary representations, warranties and covenants, if the excess borrowing capacity under our revolving line of credit facility is below \$10.0 million, we are required to meet a minimum trailing twelve month EBITDA to fixed charges ratio, as defined in the amended Loan Agreement. On June 30, 2019, our borrowing capacity exceeded \$10.0 million, therefore, we were not subject to this financial covenant. However, for informational purposes we have provided the result of the financial covenant below:

Quarterly Financial Covenant	Requirement	Actual
EBITDA to fixed charges ratio	1.10 : 1.00	7.55 : 1.00

While we were in compliance with the financial covenant for the quarter ended June 30, 2019, failure to meet this covenant requirement in future quarters could lead to higher financing costs, increased restrictions, or reduce or eliminate our ability to borrow funds and could have a material adverse effect on our business, financial condition and results of operations.

### *Bolt Commitment Letter*

At June 30, 2019, Bolt had \$3.7 million Canadian dollars of outstanding borrowings and remaining borrowing availability of \$1.8 million Canadian dollars under a Commitment Letter. The Commitment Letter is subject to a working capital ratio of 1.35:1, a maximum ratio of debt to tangible net worth of 2.5:1 of the Bolt assets and Debt Service Coverage Ratio 1.25:1 as defined in the Commitment Letter. At June 30, 2019, Bolt was in compliance with all covenants which are subject to periodic review, at least annually, with the next review due by August 31, 2019.

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

ITEM 3 of Part I is inapplicable and has been omitted from this report.

**ITEM 4. CONTROLS AND PROCEDURES**

Under the supervision and with the participation of our senior management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures, as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as of the end of the period covered by this report (the "Evaluation Date"). Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded as of the Evaluation Date that our disclosure controls and procedures were effective such that the information relating to Lawson, including our consolidated subsidiaries, required to be disclosed in our SEC reports (i) is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) includes, without limitation, controls and procedures designed to ensure that information required to be disclosed is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There were no changes in our internal control over financial reporting during the quarter ended June 30, 2019 that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

**PART II  
OTHER INFORMATION**

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

**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

The following table summarizes the repurchases of the Company's common stock for the three months ended June 30, 2019. The shares that were purchased were purchased for the sole purpose of satisfying tax withholding obligations of certain individuals upon the vesting of restricted stock awards granted to them by the Company. No shares were purchased in the open market.

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 (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
April 1 to April 30, 2019	—	\$ —	—	\$ —
May 1 to May 31, 2019	—	—	—	7,500,000
June 1 to June 30, 2019	—	—	—	7,500,000
Total	—	—	—	—

**ITEM 6. EXHIBITS**

**Exhibit #**

<a href="#"><u>31.1</u></a>	<a href="#"><u>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</u></a>
<a href="#"><u>31.2</u></a>	<a href="#"><u>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</u></a>
<a href="#"><u>32</u></a>	<a href="#"><u>Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</u></a>
<b>101.INS</b>	XBRL Instance Document
<b>101.SCH</b>	XBRL Taxonomy Extension Schema Document
<b>101.CAL</b>	XBRL Taxonomy Extension Calculation Linkbase Document
<b>101.DEF</b>	XBRL Taxonomy Extension Definition Linkbase Document
<b>101.LAB</b>	XBRL Taxonomy Extension Label Linkbase Document
<b>101.PRE</b>	XBRL Taxonomy Extension Presentation Linkbase Document

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: July 25, 2019

/s/ Michael G. DeCata

Michael G. DeCata  
President and Chief Executive Officer  
(principal executive officer)

Dated: July 25, 2019

/s/ Ronald J. Knutson

Ronald J. Knutson  
Executive Vice President, Chief Financial Officer, Treasurer and  
Controller  
(principal financial and accounting officer)

**CERTIFICATION**

I, Michael G. DeCata, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Lawson Products, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal nine months (the registrant’s fourth fiscal nine months in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: July 25, 2019

/s/ Michael G. DeCata  
Michael G. DeCata  
President and Chief Executive Officer  
(principal executive officer)

**CERTIFICATION**

I, Ronald J. Knutson, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Lawson Products, Inc. (the “registrant”);
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant’s other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) for the registrant and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant’s disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant’s internal control over financial reporting that occurred during the registrant’s most recent fiscal nine months (the registrant’s fourth fiscal nine months in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant’s internal control over financial reporting; and
5. The registrant’s other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant’s auditors and the audit committee of the registrant’s board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant’s ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant’s internal control over financial reporting.

Date: July 25, 2019

/s/ Ronald J. Knutson

Ronald J. Knutson  
Executive Vice President, Chief Financial Officer, Treasurer and Controller  
(principal financial and accounting officer)

**CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350 AS ADOPTED  
PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report of Lawson Products, Inc. (the "Company") on Form 10-Q for the period ending June 30, 2019 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned Chief Executive Officer and Chief Financial Officer of the Company hereby certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002 that based on their knowledge: (1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and (2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company as of and for the periods covered in the Report.

July 25, 2019

/s/ Michael G. DeCata  
Michael G. DeCata  
Lawson Products, Inc.  
President and Chief Executive Officer  
(principal executive officer)

/s/ Ronald J. Knutson  
Ronald J. Knutson  
Lawson Products, Inc.  
Executive Vice President, Chief Financial Officer,  
Treasurer and Controller  
(principal financial and accounting officer)