LAMSON & SESSIONS CO
Form 10-Q
October 28, 2004

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

FORM 10-Q

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

For the quarterly period ended October 2, 2004

OR

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

For the transition period from ______________ to _______________

Commission File Number 1-313

THE LAMSON & SESSIONS CO.
(Exact name of Registrant as specified in its charter)

Ohio	34-0349210
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
25701 Science Park Drive Cleveland, Ohio	44122-7313
(Address of principal executive offices)	(Zip Code)

216/464-3400
(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report.)

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 [ ]

Indicate by check mark whether the Registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes [ ] No [X]

APPLICABLE ONLY TO ISSUERS INVOLVED

IN BANKRUPTCY PROCEEDINGS DURING
THE PRECEDING FIVE YEARS:

Indicate by check mark whether the Registrant has filed all documents and reports required to be filed by Sections 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court.

Yes [ ] No [ ]

APPLICABLE ONLY TO CORPORATE ISSUERS:

As of October 2, 2004 the Registrant had outstanding 13,837,024 common shares.

PART I

ITEM 1 - FINANCIAL STATEMENTS

CONSOLIDATED INCOME STATEMENTS (UNAUDITED)
THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

(Dollars in thousands, except per share data)

	THIRD QUARTER ENDED				NINE	
	2004		2003		2004	
NET SALES	$ 106,403	100.0%	$ 95,251	100.0%	$ 294,153	10
Cost of products sold	87,993	82.7%	79,968	84.0%	241,752	8
GROSS PROFIT	18,410	17.3%	15,283	16.0%	52,401	1
Operating expenses	12,903	12.1%	10,713	11.2%	36,879	1
Litigation settlement	1,728	1.6%	-	0.0%	1,728	
Other expense (income)	395	0.4%	-	0.0%	(231)	-
OPERATING INCOME	3,384	3.2%	4,570	4.8%	14,025	
Interest expense, net	1,992	1.9%	2,094	2.2%	5,897	
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	1,392	1.3%	2,476	2.6%	8,128	
Income tax provision	559	0.5%	958	1.0%	3,251	
INCOME FROM CONTINUING OPERATIONS	833	0.8%	1,518	1.6%	4,877	
Income from discontinued operations, net of income tax of $256	-	0.0%	-	0.0%	401	
NET INCOME	$ 833	0.8%	$ 1,518	1.6%	$ 5,278	
BASIC EARNINGS PER COMMON SHARE:						
Earnings from continuing operations	$ 0.06		$ 0.11		$ 0.35	
Earnings from discontinued operations, net of tax	-		-		0.03	
NET EARNINGS	$ 0.06		$ 0.11		$ 0.38	
DILUTED EARNINGS PER COMMON SHARE:						
Earnings from continuing operations	$ 0.06		$ 0.11		$ 0.35	
Earnings from discontinued operations, net of tax	-		-		0.03	

NET EARNINGS	$ 0.06	$ 0.11	$ 0.37

See notes to Consolidated Financial Statements (Unaudited).

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CONSOLIDATED BALANCE SHEETS (UNAUDITED)
THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

(Dollars in thousands)

	THIRD QUARTER ENDED 2004
ASSETS	
CURRENT ASSETS	
Cash and cash equivalents	$ 533
Accounts receivable, net of allowances of $1,634, $1,532 and $2,152, respectively	59,561
Inventories, net	
Raw materials	3,922
Work-in-process	4,827
Finished goods	31,381
	40,130
Deferred tax assets	8,961
Prepaid expenses and other	5,293
TOTAL CURRENT ASSETS	114,478
PROPERTY, PLANT AND EQUIPMENT	
Land	3,320
Buildings	24,897
Machinery and equipment	118,161
	146,378
Less allowances for depreciation and amortization	98,536
TOTAL NET PROPERTY, PLANT AND EQUIPMENT	47,842
GOODWILL	21,519
PENSION ASSETS	30,388
DEFERRED TAX ASSETS	13,455
OTHER ASSETS	5,350
TOTAL ASSETS	$ 233,032
LIABILITIES AND SHAREHOLDERS' EQUITY	
CURRENT LIABILITIES	
Accounts payable	$ 32,388
Accrued compensation and benefits	11,787
Customer volume & promotional accrued expenses	6,208
Other accrued expenses	9,940
Taxes	3,738
Secured credit agreement - current	83,100

Current maturities of long-term debt	860
TOTAL CURRENT LIABILITIES	148,021
LONG-TERM DEBT	11,756
POST-RETIREMENT BENEFITS AND OTHER LONG-TERM LIABILITIES	28,749
SHAREHOLDERS' EQUITY	
Common shares	1,384
Other capital	75,787
Retained earnings (deficit)	(28,551)
Accumulated other comprehensive income (loss)	(4,114)
TOTAL SHAREHOLDERS' EQUITY	44,506
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 233,032

See notes to Consolidated Financial Statements (Unaudited).

CONSOLIDATED STATEMENTS OF CASH FLOW (UNAUDITED)
THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

(Dollars in thousands)

	NINE MONTHS ENDED	
	2004	2003
OPERATING ACTIVITIES		
Net income	$ 5,278	$ 3,447
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation	6,901	6,890
Amortization	1,199	1,199
Gain on sale of property, plant and equipment	(933)	-
Deferred income taxes	2,862	2,102
Net change in working capital accounts:		
Accounts receivable	(21,365)	(15,781)
Inventories	(9,987)	(2,335)
Prepaid expenses and other	(316)	(104)
Accounts payable	15,460	5,445
Accrued expenses and other current liabilities	2,349	(1,741)
Pension plan contributions	(1,792)	(1,067)
Other long-term items	1,893	2,285
CASH PROVIDED BY OPERATING ACTIVITIES	1,549	340
INVESTING ACTIVITIES		
Net additions to property, plant and equipment	(4,592)	(5,787)
Refund of deposits on equipment operating leases	580	-
Proceeds from sale of property, plant and equipment	1,595	-
Acquisitions and related items	(187)	(750)

CASH USED IN INVESTING ACTIVITIES	(2,604)	(6,537)
FINANCING ACTIVITIES		
Net borrowings under secured credit agreement	1,700	6,000
Payments on other long-term borrowings	(734)	(748)
Purchase and retirement of treasury stock	(205)	-
Exercise of stock options	359	2
CASH PROVIDED BY FINANCING ACTIVITIES	1,120	5,254
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	65	(943)
Cash and cash equivalents at beginning of year	468	1,496
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 533	$ 553

See notes to Consolidated Financial Statements (Unaudited).

THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

NOTE A - BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements do not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals and changes in accounting estimates) considered necessary for a fair presentation have been included. Certain 2003 amounts have been reclassified to conform with 2004 classifications.

NOTE B - INCOME TAXES

The year-to-date 2004 income tax provision was calculated based on management's estimate of the annual effective tax rate of 40% for the year. The provisions for 2004 and 2003 are primarily non-cash charges.

NOTE C - BUSINESS SEGMENTS

The Company's reportable segments are as follows:

Carlon - Industrial, Residential, Commercial, Telecommunications and Utility Construction: The major customers served are electrical contractors and distributors, original equipment manufacturers, electric power utilities, cable television (CATV), telephone and telecommunications companies. The principal products sold by this segment include electrical and telecommunications raceway systems and a broad line of enclosures, electrical outlet boxes and fittings. Examples of the applications for the products included in this segment are multi-cell duct systems and High Density Polyethylene ("HDPE") conduit designed to protect underground fiber optic cables, allowing future cabling expansion and flexible conduit used inside buildings to protect communications cable.

Lamson Home Products - Consumer: The major customers served are home centers and mass merchandisers for the "do-it-yourself" (DIY) home improvement market. The products included in this segment are electrical outlet boxes, liquidtight conduit, electrical fittings, door chimes and lighting controls.

PVC Pipe: This business segment primarily supplies electrical, power and communications conduit to the electrical distribution, telecommunications, consumer, power utility and sewer markets. The electrical and telecommunications conduit is made from polyvinyl chloride ("PVC") resin and is used to protect wire or fiber optic cables supporting the infrastructure of power or telecommunications systems.

THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

NOTE C - BUSINESS SEGMENTS - CONTINUED

(Dollars in thousands)

	THIRD QUARTER ENDED		NINE MONTHS ENDED	
	2004	2003	2004	2003
NET SALES				
Carlon	$ 51,857	$ 43,755	$ 139,487	$ 116,879
Lamson Home Products	24,019	22,259	67,053	59,834
PVC Pipe	30,527	29,237	87,613	85,055
	$ 106,403	$ 95,251	$ 294,153	$ 261,768
OPERATING INCOME (LOSS)				
Carlon	$ 4,565	$ 4,204	$ 12,812	$ 9,885
Lamson Home Products	1,431	3,696	6,283	9,544
PVC Pipe	(597)	(2,115)	(765)	(2,824)
Corporate Office	(1,620)	(1,215)	(4,536)	(4,428)
Other (Expense) Income (see Note I)	(395)	-	231	-
	$ 3,384	$ 4,570	$ 14,025	$ 12,177
DEPRECIATION AND AMORTIZATION				
Carlon	$ 1,313	$ 1,688	$ 4,078	$ 5,136
Lamson Home Products	458	433	1,393	1,286
PVC Pipe	891	615	2,629	1,667
	$ 2,662	$ 2,736	$ 8,100	$ 8,089

In September 2004 the Company settled its patent infringement litigation as the result of a mediation process. The effect of this litigation settlement has reduced operating income by $864,000 in both the Carlon and Lamson Home Products business segments in the third quarter of 2004. Total assets by business segment at October 2, 2004, January 3, 2004 and October 4, 2003 are as follows:

(Dollars in thousands)

	OCTOBER 2,	JANUARY 3,	OCTOBER 4,

	2004	2004	2003
IDENTIFIABLE ASSETS			
Carlon	$ 87,075	$ 79,900	$ 89,470
Lamson Home Products	33,484	30,065	31,674
PVC Pipe	50,307	34,232	41,667
Corporate Office (includes deferred tax and pension assets)	62,166	64,116	62,749
	$233,032	$208,313	$225,560

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NOTE D - COMPREHENSIVE INCOME

The components of comprehensive income for the third quarter and first nine months of 2004 and 2003 are as follows:

(Dollars in thousands)

	THIRD QUARTER ENDED		NINE MONTHS ENDED	
	OCTOBER 2, 2004	OCTOBER 4, 2003	OCTOBER 2, 2004	OCTOBER 4, 2003
Net income	$ 833	$1,518	$ 5,278	$3,447
Foreign currency translation adjustments	(56)	57	(78)	114
Interest rate swaps, net of tax	124	252	533	469
Comprehensive income	$ 901	$1,827	$ 5,733	$4,030

The components of accumulated other comprehensive loss, at October 2, 2004, January 3, 2004 and October 4, 2003 are as follows:

(Dollars in thousands)

	OCTOBER 2, 2004	JANUARY 3, 2004	OCTOBER 4, 2003
Foreign currency translation adjustments	$ (519)	$ (441)	$ (500)
Minimum pension liability adjustments, net of tax	(3,289)	(3,289)	(3,706)
Interest rate swaps, net of tax	(306)	(839)	(1,081)
Accumulated other comprehensive loss	$(4,114)	$(4,569)	$(5,287)

THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

NOTE E - EARNINGS PER SHARE CALCULATION

The following table sets forth the computation of basic and diluted earnings per share:

(Dollars and shares in thousands, except per share amounts)

	THIRD QUARTER ENDED		NINE MONTHS ENDED	
	2004	2003	2004	2003
BASIC EARNINGS-PER-SHARE COMPUTATION				
Net Income	$ 833	$ 1,518	$ 5,278	$ 3,447
Average Common Shares Outstanding	13,809	13,786	13,793	13,785
Basic Earnings Per Share	$ 0.06	$ 0.11	$ 0.38	$ 0.25
DILUTED EARNINGS-PER-SHARE COMPUTATION				
Net Income	$ 833	$ 1,518	$ 5,278	$ 3,447
Basic Shares Outstanding	13,809	13,786	13,793	13,785
Stock Options Calculated Under the Treasury Stock Method	373	140	287	76
Total Shares	14,182	13,926	14,080	13,861
Diluted Earnings Per Share	$ 0.06	$ 0.11	$ 0.37	$ 0.25

NOTE F - DERIVATIVES AND HEDGING

The Company recognizes all derivative financial instruments as either assets or liabilities at fair value. Derivative instruments that are not hedges are adjusted to fair value through net income. Changes in the fair value of derivative instruments that are classified as fair value hedges are offset against changes in the fair value of the hedged assets, liabilities, or firm commitments, through net income. Changes in the fair value of derivative instruments that are classified as cash flow hedges are recognized in other comprehensive income until such time as the hedged items are recognized in net income.

During the first quarter of 2001, the Company entered into two interest rate swap agreements for a total notional amount of $58.5 million, of which $22.0 million was outstanding at October 2, 2004. The agreements are coterminous with the Company's secured credit facility and expire in August 2005. The swap agreements effectively fix the interest rate on its variable rate debt at 5.41% and 5.48% plus the Company's risk premium of 1.5% to 4.0%, respectively. These transactions are considered cash flow hedges and, therefore, the fair market value at the end of the third quarter of 2004 of a $306,000 (net of $195,000 in tax) loss, has been recognized in other comprehensive income (loss). There is no ineffectiveness on the cash flow hedges, therefore, all changes in the fair value of these derivatives are recorded in equity and not included in the current period's income statement. The entire $501,000 of loss on the fair value of the hedges is classified in current accrued liabilities.

The Company has no derivative instruments that are classified as fair value hedges.

THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

NOTE G - DISCONTINUED OPERATIONS

As of the end of the first quarter of 2004 the Company was informed that YSD Industries Inc. ("YSD"), a business which the Company sold in 1988, was selling the assets of the business and would be unable to fund certain post-retirement medical and life insurance benefits, for which the Company was contingently liable. The Company had recorded a net charge ($2.7 million) at the 2003 year-end reflecting the actuarial calculation of this estimated liability for payments to eligible participants through February 2011 when the Company's obligation will end. As a result of YSD's asset sale, the Company was able to realize payment of $668,000 for notes receivable that had been previously written off as uncollectible in 2003. The net impact of this recovery, $401,000 (net of tax), has been recorded as income from discontinued operations in the first quarter of 2004.

NOTE H - STOCK COMPENSATION PLANS

The Company currently has three stock compensation plans. The Company accounts for those plans under the recognition and measurement principles of APB Opinion No. 25, "Accounting for Stock Issued to Employees," and related interpretations. No stock-based employee compensation cost is reflected in net income, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. In accordance with SFAS No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure," the following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation," to stock-based employee compensation.

(Dollars in thousands, except per share data)

		THIRD QUARTER ENDED		NINE MO
		2004	2003	2004
Net income	As reported	$ 833	$ 1,518	$ 5,278
Total stock-based employee compensation, net of tax		(135)	(156)	(374
Net income	Pro forma	$ 698	$ 1,362	$ 4,904
Basic earnings per share	As reported	$ 0.06	$ 0.11	$ 0.38
	Pro forma	0.05	0.10	0.36
Diluted earnings per share	As reported	$ 0.06	$ 0.11	$ 0.37
	Pro forma	0.05	0.10	0.35

NOTE I - SALE OF ASSETS

In the first quarter of 2004, the Company sold a manufacturing facility located in Pasadena, Texas for net proceeds of $1.5 million. The remaining production equipment is being relocated to other Lamson & Sessions facilities over the next quarter. The Company anticipates incurring total severance, training and other moving costs of $800,000 to $1,000,000 in 2004. These costs are charged against other income as required under Financial Accounting Standard (FAS) No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." During the third quarter the Company incurred a charge of $0.4 million, primarily the accrual of severance costs and expenditures on training and moving costs. For the nine months ended October 2, 2004, a gain on the sale of the facility ($0.9 million), net of severance and other costs associated with the closure of the facility ($0.7 million), was incurred totaling $0.2 million.

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THE LAMSON & SESSIONS CO. AND SUBSIDIARIES

NOTE J - PENSION AND OTHER POST-RETIREMENT BENEFIT PLANS

The Company sponsors several qualified and non-qualified pension plans and other post-retirement benefit plans for its current and former employees. As of January 1, 2003 the Company eliminated the salary defined benefit pension plan for future employees. This action makes all defined benefit pension and other post-retirement benefit plans closed to new entrants and will reduce future service costs.

The components of net periodic benefit cost (income) are as follows:

(Dollars in thousands)

	THIRD QUARTER ENDED				NINE MONTHS ENDED		
	PENSION BENEFITS		OTHER BENEFITS		PENSION BENEFITS		OTHER
	2004	2003	2004	2003	2004	2003	2004
Service cost	$ 298	$ 267	$ 1	$ 2	$ 894	$ 801	$
Interest cost	1,219	1,261	168	292	3,657	3,783	46
Expected return on assets	(1,486)	(1,350)	-	-	(4,458)	(4,050)	
Net amortization and deferral	388	603	(53)	47	1,164	1,809	(
Defined contribution plans	250	161	-	-	815	684	
	$ 669	$ 942	$ 116	$ 341	$ 2,072	$ 3,027	$ 45

Contributions of $983,000 were made in the third quarter of 2004, bringing total contributions by the Company to its defined benefit pension plans to $1,792,000 in 2004. The Company expects to make $855,000 in contributions over the next 12 months, a reduction from previous estimates.

The above information includes the effect of YSD's other post-retirement benefit costs which were assumed in April 2004.

On December 8, 2003, the Medicare Prescription Drug, Improvement and Modernization Act of 2003 (the Act) was signed into law. The Act introduces a prescription drug benefit under Medicare (Medicare Part D) as well as a federal subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. In accordance with FSP No. 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003," the effects of the subsidy resulted in a $0.6 million reduction of the accumulated post-retirement benefit obligation, which will be recognized prospectively.

NOTE K - DEBT CLASSIFICATION

The Company's secured credit agreement matures in August 2005. As a result, the debt was reclassified as current at the end of the third quarter of 2004. The Company intends to refinance this obligation in the first half of 2005.

ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis provides information which management believes is relevant to an assessment and understanding of the Company's consolidated results of operations and financial condition. The discussion should be read in conjunction with the Consolidated Financial Statements.

EXECUTIVE OVERVIEW

The Company continues to experience strong sales growth, recording the highest quarterly net sales levels in its history. A surge in demand for telecommunications duct to support Fiber-to-the-Premise (i.e. FTTP) projects and the strong housing start results helped to raise sales activity. Generally, order levels slowed in July and August but picked up in September recording the highest monthly net sales in over five years.

Escalating resin costs remain the Company's foremost challenge. With oil prices at record levels PVC and HDPE feedstocks have been increasing in price, driving resin producers to pass the higher costs through with higher prices. Typically, resin costs begin to decline in the third quarter and reach their low point at year-end. This is not happening in 2004. Although some of the Carlon and PVC Pipe segment business contains price escalators, much of it is dependent upon end market demand in order to receive higher prices. Margins are most significantly impacted by the fact that Lamson Home Products has been unable, thus far, to obtain any price increases from its major retail customers. In addition, the higher oil prices are causing increased fuel costs resulting in rising freight costs.

In order to reduce costs and improve efficiencies, the Company continues to implement its closure plan for its Pasadena, Texas facility. A portion of the production capacity has been moved and installed at its Clinton, Iowa facility. The project is on schedule to be completed in the fourth quarter of 2004.

Finally, in September 2004 the Company settled its patent infringement litigation as a result of a mediation process. In connection with the settlement, the Company recorded a net charge of $1.7 million in the third quarter.

2004 COMPARED WITH 2003

RESULTS OF CONTINUING OPERATIONS

The following table sets forth, for the periods indicated, items from the Consolidated Income Statements as a percentage of net sales for the third quarter and nine months ended:

	THIRD QUARTER ENDED		NINE MONTHS ENDED	
	2004	2003	2004	2003
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of products sold	82.7	84.0	82.2	83.0
Gross profit	17.3	16.0	17.8	17.0
Operating expenses	12.1	11.2	12.5	12.3
Litigation settlement	1.6	-	0.6	-
Other expense (income)	0.4	-	(0.1)	-
Operating income	3.2	4.8	4.8	4.7
Interest expense	1.9	2.2	2.0	2.5
Income from continuing operations before income taxes	1.3	2.6	2.8	2.2
Income tax provision	0.5	1.0	1.1	0.9
Income from continuing operations	0.8%	1.6%	1.7%	1.3%

Net sales for the third quarter of 2004 increased to $106.4 million, an $11.1 million or 11.6% increase, over the third quarter of 2003. All three business segments reflected higher net sales levels as telecom construction continued on a similar pace as the second quarter, home improvement DIY sales were supported by healthy home sales and improved spending on sewer infrastructure projects began to be realized. Year-to-date net sales total $294.2 million, a $32.4 million, or 12.4% increase, over the $261.8 million in net sales for the first nine months of 2003.

Gross profit, although hindered by higher raw material costs, improved to $18.4 million, 17.3% of net sales, for the third quarter of 2004, compared with $15.3 million, 16.0% of net sales, for the third quarter of 2003. For the nine months ended October 2, 2004 the gross profit was up by $7.8 million, totaling $52.4 million, 17.8% of net sales compared with $44.6 million, 17.0% of net sales for the nine months ended October 4, 2003, a 17.5% improvement. As indicated earlier, the cost of PVC continued to rise through the third quarter of 2004. Procurement costs were up 21.0% this quarter compared with the third quarter of 2003, and up an average of 16.0% for the first nine months of 2004 compared with the same period in 2003. These increased costs have been only partially offset by price increases and productivity improvements.

Operating expenses increased to $12.9 million, or 12.1% of net sales, and $36.9 million, or 12.5% of net sales for the third quarter and first nine months, respectively. In the third quarter, operating expenses were $2.2 million higher than the $10.7 million in the third quarter of 2003. Much of the increase is caused by higher variable selling expenses as sales were up by almost 12.0%. In addition, the Company had higher incentive compensation expense ($1.4 million), which was offset by reduced pension ($350,000) and retiree medical expenses ($225,000) in the current quarter compared with the prior year third quarter. In the first nine months of 2004, operating expenses were $4.4 million, or 12.4% higher than the $32.4 million of expenses in 2003. A majority of the increase is a result of the 12.4% higher sales level in 2004 year-to-date compared with the first nine months of 2003, causing more variable selling expenses. As noted in the third quarter, comparative incentive compensation costs are higher ($2.6 million) than last year. In addition, for the first nine months of 2004 higher medical

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expenses for active employees ($980,000) and professional fees ($300,000), addressing Sarbanes-Oxley compliance items, were incurred while there was a reduction in costs from lower pension and retiree medical expenses along with recovery of a bankruptcy claim. Operating income was $14.0 million for the first nine months of 2004. Included in these results are the net effects of a litigation settlement of $1.7 million, completed in September 2004, and the sale and closure of the Company's Pasadena, Texas facility (see Note G).

Net interest declined to $5.9 million for the first nine months of 2004 compared with $6.4 million in the same period in the prior year. Average borrowings over the first nine months of 2004 are lower by $3.4 million from the first nine months of 2003 while interest rates are 5.63% for 2004 year-to-date down from the 6.21% average for the prior year-to-date period.

The Company's earnings before interest, taxes, depreciation and amortization (EBITDA) was $6.0 million for the third quarter of 2004 and $22.1 million for the first nine months of 2004 compared with $7.3 million and $20.3 million for the respective periods in 2003.

The components of this calculation are as follows:

(Dollars in thousands)

	THIRD QUARTER ENDED		NINE MONTHS ENDED	
	2004	2003	2004	2003
Operating income	$3,384	$4,570	$14,025	$12,177
Depreciation	2,263	2,337	6,901	6,890
Amortization	399	399	1,199	1,199
EBITDA	$6,046	$7,306	$22,125	$20,266
EBITDA Margin (EBITDA/Net Sales)	5.7%	7.7%	7.5%	7.7%

EBITDA is a calculation used by management to measure liquidity. EBITDA is not a recognized term under accounting principles generally accepted in the United States and does not purport to be an alternative to operating income or cash flows from operating activities as a measure of liquidity.

The following is a reconciliation of EBITDA to cash provided (used) by operating activities:

(Dollars in thousands)

	THIRD QUARTER ENDED	NINE MONTHS ENDED

	2004	2003	2004	2003
EBITDA	$ 6,046	$ 7,306	$ 22,125	$ 20,266
Gain on sale of property, plant and equipment (investing activities)	-	-	(933)	-
Interest expense	(1,992)	(2,094)	(5,897)	(6,432)
Increase in net operating (assets)	(4,259)	(1,723)	(13,746)	(13,494)
Cash (used) provided by operating activities	$ (205)	$ 3,489	$ 1,549	$ 340

BUSINESS SEGMENTS

CARLON

The Carlon business segment had net sales of $51.9 million in the third quarter 2004, an 18.5% increase over the $43.8 million in net sales reported in the prior year third quarter. All three quarters of 2004 have experienced double digit percentage net sales growth from their comparable quarter in 2003. This expansion is led again by

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an approximate 25.0% increase in telecom wireline product sales, primarily from higher demand for HDPE conduit, to support the initial rollout of fiber-to-the-premise projects. Electrical product sales are also up by about 6.0% in the third quarter 2004 and 10.5% year-to-date compared with their respective periods in 2003. Carlon has realized market expansion as well as some price increases to offset some of the raw material cost increases. Year-to-date, Carlon's net sales have increased by $22.6 million, or 19.3%, to $139.5 million from $116.9 million in the first nine months of 2003.

Gross margin was favorably impacted by the higher telecom sales volume, enabling the HDPE extrusion facilities to run at close to 60.0% capacity for the last two quarters. By achieving some price increases Carlon has been able to mitigate a portion of the steep raw material cost increases. The increased volume has also allowed the Company to better leverage its fixed costs.

Operating income for Carlon was $4.6 million (8.8% of net sales) and $12.8 million (9.2% of net sales) in the third quarter 2004 and the first nine months of 2004, respectively. This compares with operating income of $4.2 million (9.6% of net sales) and $9.9 million (8.5% of net sales) in the third quarter 2003 and the first nine months of 2003, respectively. Included in the business segment's operating expenses for the third quarter of 2004 is approximately $0.85 million related to a litigation settlement. Operating expenses year-to-date 2004 are approximately $2.5 million higher than the comparable period of 2003. In addition to the litigation charge and related legal fees, Carlon has incurred higher variable selling expenses and product development expenses. These expenses were somewhat offset by the partial recovery ($300,000) of an accounts receivable that was written off in 2002 relating to the Adelphia bankruptcy.

LAMSON HOME PRODUCTS

Lamson Home Products continued its steady growth, recording $24.0 million in net sales in the third quarter 2004, a 7.9%, or $1.8 million increase, over the $22.3 million in net sales in the third quarter of 2003. In addition to the business segment's electrical box and fitting product lines, it has seen more recent growth in the innovative chimes and lighting control products that it offers. This business segment continues to gain shelf space at many of its retail, DIY customers.

The business segment has been hit the hardest by the dramatic increases in PVC resin costs over the past year. Unfortunately, despite these well documented rising costs, they have not been recovered in price increases from the "big box" retailers. This has caused a reduction in gross margin, compared with the prior year, of approximately 300 basis points. The Company continues to invest in new equipment and other productivity-improvement initiatives in an attempt to mitigate these margin reductions.

Operating income was $1.4 million, or 6.0% of net sales, in the third quarter 2004 compared with $3.7 million, or 16.6% of net sales, in the third quarter 2003. Included in this quarter's operating expenses is $0.85 million related to a litigation settlement. Year-to-date 2004 operating income totaled $6.3 million, or 9.4% of net sales, compared with $9.5 million, or 16.0% of net sales, for the first nine months of 2003. In addition to the lower gross margins in 2004 and litigation and related legal expenses, the business segment is incurring higher variable selling expenses and new product development costs to support, in particular, the chimes and lighting control product line expansions.

PVC PIPE

Net sales for the third quarter 2004 in the PVC Pipe business segment rose to $30.5 million, a $1.3 million, or 4.4% improvement over the third quarter of 2003. Healthy residential construction activity continues to support this business segment along with a resurgence of sewer infrastructure spending. Rigid pipe volume was relatively slow in July and August before beginning to rebound in September. It ended this quarter about 17.5% behind the third quarter of 2003. The volume decline in the third quarter 2004 was offset by increased pricing of almost 18.0% compared with the third quarter 2003. For the first nine months of 2004 net sales were $87.6 million, $2.6 million, or 3.0% higher than the $85.1 million in net sales reported in the comparable period of 2003. Volume of pipe pounds sold was down by 6.0% year-to-date 2004, while price was higher by almost

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9.0% over the same period last year. The Vylon large diameter sewer pipe product line continued to see increased shipment and order rates during the third quarter.

Gross margin was impacted by higher PVC resin costs, but the majority of these increases were reflected in higher selling prices, improving margins over 2003. Lower conduit sales volume has driven PVC extrusion utilization this quarter under 70.0% in order to control the related pipe inventory. On a positive note, the favorable product mix from Vylon sewer pipe sales has helped to offset this lower utilization as these engineered products command a much higher margin than standard electrical conduit.

The PVC Pipe business segment had a $0.6 million operating loss for the third quarter of 2004 resulting in a business segment operating loss-to-date of $0.8 million. This reflects an improvement over the prior year third quarter and year-to-date reported operating losses of $2.1 million and $2.8 million, respectively. The improvements this year come primarily at the gross margin line as operating expenses for the most part are similar to 2003. Operating expenses have increased slightly this year from expanded Vylon product research and development costs in order to gain new business.

LIQUIDITY AND CAPITAL RESOURCES

The Company's primary source of liquidity and capital resources is cash from operating activities and availability under its secured credit facility.

Cash provided by operating activities was $1.5 million in the first nine months of 2004 compared with $0.3 million in the first nine months of 2003. Although the Company grew its investment in working capital year-to-date to support increased business activity, it was able to maintain positive cash flow through improved operating results. Accounts receivable alone has grown $21.4 million since the 2003 year-end, a 55.9% increase, and reflects a $7.1 million, or a 13.5%, increase over the third quarter of 2003. This is directly attributable to the higher sales levels especially late in the third quarter of 2004 as days sales outstanding, calculated using a 3-month rolling average, was 50.1 days at the end of the third quarter of 2004 compared with 47.3 days at the end of the third quarter of 2003.

Inventory began to decline slightly in the third quarter 2004 in anticipation of the seasonal slowdown experienced in the winter months. Inventory levels of $40.1 million remain $10.0 million higher than year-end and $5.6 million more than the end of the third quarter 2003. Despite this increase, inventory turns rose to 7.7 times at the end of the third quarter 2004, compared with 7.3 times at the prior third quarter-end. Much of the increased inventory levels are to support new business obtained by the Lamson Home Products segment and higher demand seen for telecommunication products, especially HDPE conduit. PVC resin pounds in inventory at October 2, 2004 were 14.6% higher than year-end 2003 and 10.7% more than at October 4, 2003. The cost per pound of PVC resin in inventory has increased by approximately 25.0% since year-end 2003 and the end of the third quarter of 2003.

Accounts payable at October 2, 2004 was $32.4 million, an increase of $15.5 million from year-end 2003 and $5.7 million higher than October 4, 2003. The increase in payables primarily reflects the comparatively higher cost of inventory and increased business activity and the timing of the 2003 year-end payments which lowered the payables balance at year-end. Total accruals were $27.9 million at October 2, 2004, $3.1 million higher than the $24.8 million at October 4, 2003. The current accrual balances reflect a higher anticipated incentive compensation estimate, the remainder of the litigation settlement, higher retiree medical payable (primarily for the addition of YSD retirees) and selling and marketing programs partially offset by lower freight accruals due to timing of payments compared with the prior year third quarter.

Capital expenditures increased during the third quarter bringing the amount invested year-to-date to $4.6 million compared with $5.8 million invested at this time last year. Investments during the third quarter of 2004 include the fixed asset additions to support the move of capacity from Pasadena, Texas to other facilities, productivity investments in both the Company's molding and PVC extrusion facilities and tooling to support new product offerings.

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As of the end of the third quarter of 2004 the Company's secured credit facility was classified as a current debt as its maturity date is in August 2005. The Company is not in violation with any of its covenants, has adequate credit capacity and expects to pay down its bank debt during the fourth quarter as the need for working capital slows. It is also anticipated that the Company will refinance this obligation in the first half of 2005 pending the evaluation of various strategic alternatives being investigated by management and the Company's investment bankers.

CRITICAL ACCOUNTING ESTIMATES

We have no material changes to the disclosure on this matter since the end of our most recent fiscal year, January 3, 2004 except as follows.

DEFERRED TAX ASSETS

As of October 2, 2004 the Company had approximately $22.4 million of net deferred tax assets including loss carryforwards that expire through 2022 and other temporary differences. The valuation of these deferred tax assets would be negatively impacted if corporate statutory income tax rates decline. In October 2004, a Corporate tax reduction bill was enacted. The Company is evaluating the impact on the value of its net operating loss carryforward and other timing differences, which is not expected to be material. The realization of these net assets is based primarily upon estimates of future taxable income. Current expectations of operating results are sufficient to sustain realization of these net assets. However, should taxable income estimates for the carryforward period be significantly reduced, the full realization of net deferred tax assets may not occur.

OUTLOOK FOR 2004

The third quarter has seen a continuation of the upswing in telecom product sales in the Carlon business segment. In October, the Federal Communications Commission (FCC) relieved the telecom industry of unbundling requirements for FTTP loops. We believe this will stimulate more outside plant capital spending to build-out the last mile of the fiber network.

Residential construction remains strong with housing starts approximately 2.0 million units for the last year. We expect this pace to decline slightly to the 1.7 to 1.8 million unit range through next year as mortgage interest rates and construction costs rise. Non-residential and industrial construction should, however, offset this decline as vacancy rates have stabilized. Improved corporate profits and capital spending should result in modest growth in commercial construction through 2005.

Resin costs, both HDPE and PVC, are expected to stay at the current high levels even through the winter months when they traditionally have declined. It is currently expected with the high oil and natural gas prices, supported by the strong global demand for these resins, that these costs may average 10.0% higher in 2005 than 2004. The Company intends to pass on these material related cost increases with further price increases in 2005 wherever possible.

The Company continues its management of working capital as evidenced by inventory turns reaching 7.7 turns compared with 7.3 turns a year ago. Despite very high net sales levels this quarter the days sales outstanding remains at 50 days. Payments for pension contributions and a litigation settlement lowered cash flow generated this quarter; however, we still expect substantial positive operating cash flow in the fourth quarter 2004 reducing outstanding debt at year-end to the lowest level since 2000.

As announced in early October, the Company has hired an investment banker to review various strategic alternatives in order to improve shareholder value including the potential sale of all or a portion of the Company. As a result, management has deemed it prudent to delay the refinancing of its secured credit facility which expires in August 2005. Management believes the refinancing will take place in the first half of 2005 pending the conclusion of the strategic review.

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Based on the results through the third quarter and expectations for our markets, we anticipate net sales growth will be 10.0% to 12.0% for 2004 and an additional 8.0% to 10.0% for 2005.

Despite the litigation charge of $1.7 million incurred in the third quarter of 2004, we continue to believe projected earnings for 2004 will be between 43 to 48 cents per diluted share.

Certain sections of this Quarterly Report on Form 10-Q, including this Outlook Section, contain forward-looking comments. The comments are subject to, and the actual future results may be impacted by, the cautionary limitations and factors outlined in the following narrative comments.

This Management's Discussion and Analysis of Financial Condition and Results of Operations contain expectations that are forward-looking statements that involve risks and uncertainties within the meaning of the Private Securities Litigation Reform Act of 1995. Actual results may differ materially from those expected as a result of a variety of factors, such as: (i) the volatility of resin pricing, (ii) the ability of the Company to pass through raw material cost increases to its customers, (iii) maintaining a stable level of housing starts, telecommunications infrastructure spending, consumer confidence and general construction trends, (iv) the continued availability and reasonable terms of bank financing (v) the outcome and effects of the Company's exploration of strategic alternatives and (vi) any adverse change in the recovery trend of the country's general economic condition affecting the markets for the Company's products. Because forward-looking statements are based on a number of beliefs, estimates and assumptions by management that could ultimately prove to be inaccurate, there is no assurance that any forward-looking statement will prove to be accurate.

ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We have no material changes to the disclosure on this matter since the end of our most recent fiscal year, January 3, 2004.

ITEM 4 - CONTROLS AND PROCEDURES

As of October 2, 2004, an evaluation was performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures. Based on that evaluation, the Company's management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Company's disclosure controls and procedures were effective. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect internal controls subsequent to their evaluation.

PART II

ITEM 1 - LEGAL PROCEEDINGS

On September 23, 1999, the Company announced that a United States District Court jury in the Northern District of Illinois found that the Company willfully infringed on a patent held by Intermatic Incorporated ("Intermatic") of Spring Grove, Illinois, relating to the design of an in-use weatherproof electrical outlet cover, and awarded Intermatic $12.5 million in damages plus pre-judgment interest of approximately $1.5 million. The Company pursued a vigorous appeal and on December 17, 2001 the United States Court of Appeals ruled that, as a matter of law, Lamson & Sessions' products did not infringe Intermatic's patent and that the Company has no liability to Intermatic. The trial jury's earlier verdict in favor of Intermatic in the amount of $12.5 million, plus pre-judgment and post-judgment interest estimated to be in excess of $3.0 million, was reversed. Intermatic filed for a rehearing of the ruling to the Court of Appeals en banc, which was denied. Intermatic then filed a petition for certiorari with the United States Supreme Court. The United States Supreme Court reversed the decision of the Court of Appeals and remanded the case back to it. In March 2003, the Court of Appeals remanded this litigation back to the United States District Court for reconsideration. On September 17, 2004, the Company announced the settlement of this litigation arrived at through a mediation process. The net effect of that settlement has been reflected in the third quarter 2004 operating results.

The Company is also a party to various other claims and matters of litigation incidental to the normal course of its business. Management believes that the final resolution of these matters will not have a material adverse effect on the Company's financial position, cash flows or results of operations.

ITEM 6 - EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

31.1 Certification of John B. Schulze, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of James J. Abel, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of John B. Schulze, Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of James J. Abel, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K.

1. The Company's current report on Form 8-K, dated July 28, 2004, relating to the Company's earnings for the second quarter of 2004.

2. The Company's current report on Form 8-K, dated September 17, 2004, relating to the Company's settlement of its patent infringement litigation with Intermatic Incorporated of Spring Grove, Illinois.

3. The Company's current report on Form 8-K, dated October 5, 2004, relating to the Company's exploration of strategic alternatives.

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.

THE LAMSON & SESSIONS CO.

(Registrant)

October 28, 2004 By: /s/ James J. Abel

James J. Abel

Executive Vice President, Secretary,
Treasurer and Chief Financial Officer