

# THE EASTERN COMPANY

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ANNUAL REPORT 2008



# Letter To Our Shareholders



The deterioration of the economy in 2008 affected our company as it did so many others. Many of the expectations on which we had based our 2008 business plans slowly eroded as the year went on. In the fourth quarter particularly, many of our customers responded to the severe economic pressures in their marketplaces by cutting back purchases, downsizing operations, re-scheduling delivery of product and in some cases canceling orders. Some of those actions have continued into the early part of 2009. We have had to respond and modify our activities accordingly.

At first glance, our results for 2008 appear to reflect the growing distress in the economy. Sales totaled \$135.9 million versus \$156.3 million in 2007, while net income totaled \$4.5 million versus \$10.1 million in 2007. However, the 2008 results for our core businesses actually compared favorably with those for 2007. That's because the 2007 results had been bolstered by a military contract to provide latching systems for Humvees. Sales under the contract contributed \$20.5 million to 2007 sales. It was because of the outsized impact from this non-core contract that we specifically noted, in all of our 2008 reports making comparisons with 2007, that the contract had had a one-time effect. With the contract excluded, 2007 sales totaled \$135.8 million—indicating no fall-off in sales during 2008.

Nevertheless, there's no question that most of the diverse markets we serve were affected either directly or indirectly

last year by the deterioration in the U.S. economy. In our planning, we had anticipated 10% growth in sales, but the much lower growth that occurred in our core businesses resulted in lower gross margins. This was because of the reduced utilization of our facilities, which we had not expected.

## Segment Performance in 2008

### Security Products Group—

Several economic factors negatively affected this segment. Reduced travel activity in general, as well as the airlines' policy regarding the checking of baggage, softened what had been a robust demand for the locks we furnish to the luggage industry under the SearchAlert™ brand. We also produce hardware for the Recreational Vehicle industry, which softened when gasoline prices spiked at mid-year, causing a drop-off in the industry's business and in its hardware requirements. Additionally, the consumer credit crunch and housing industry problems had their effect on the appliance markets to which we provide oven latches.

**Metal Products Group—**While the financial results for this segment in 2008 were far from what we expected, sales were actually up 48% from 2007, bolstered in large part by demand for our proprietary mine roof anchor products used in underground mining. The poor financial results were caused by operational factors that we are continuing to address.

Coal has long played a dominant role in meeting the country's energy requirements, and we believe that this will continue to be the case in the U.S. as well as in China and other developing nations. We are committed to serving those markets.

**Industrial Hardware Group—**Our Eberhard units provide hardware to the trucking industry and to the manufacturers of service vehicles, buses and other transportation vehicles. And our Canadian Commercial Vehicles subsidiary furnishes sleeper cabs used on Class 8 trucks. All of the vehicle manufacturers were impacted negatively by the downturn in the economy. In the case of Canadian Commercial Vehicles, it was believed that the Class 8

*The 2008  
results for  
our core  
businesses  
actually  
compared  
favorably with  
those for 2007.*



truck market would recover in the second half of 2008, but it now appears the recovery may not occur until early in 2010. Rising activity in the trucking industry is generally considered a sign of improving economic health, since it means more goods are being brought to market.

The Eberhard division also furnishes highly engineered latching systems used in several military vehicles. We currently anticipate that, notwithstanding a weak economy, our military business will remain fairly strong in 2009, while the trucking industry and vehicular markets will continue to be soft.

### Dealing with the Downturn

With the contraction of the economy undermining our business plans, we took common-sense, though still painful, actions to mitigate its effects. These actions took the form of an aggressive program to reduce costs and expenses wherever practical but without undermining the basic strength of our operating units. Measures included:

- Reductions in our labor force, which we carried out with as much care and compassion as possible through layoffs, furloughs, shortened work schedules and organizational restructuring in our manufacturing and business processes. But we made these changes only to the extent they would not disrupt customer service.
- Continued vigorous efforts to contain increases we faced in the costs of raw material and health care and pension programs.
- Elimination or deferral of operating expenses that would not impair our current operations

These actions had to be carefully and thoughtfully executed in what was already a lean operation. We will continue to do more of the same if needed. Most important to us in making these difficult decisions is to give as much consideration as possible to all of our employees, whom we greatly value.

It is also critically important for us to balance our near-term operating results with our longer-term strategic commitments and initiatives. Such initiatives include:

- Continuing and strengthening our engineering momentum with the goal of developing new products, meeting the evolving needs of current customers and preparing ourselves for the economic recovery when it occurs.
- Moving forward on capital project initiatives for future growth and profitability while not jeopardizing our liquidity position.
- Searching for acquisitions which will enhance our product growth, increase our market share and give us entry into new markets.

In the fourth quarter of 2008, the deterioration in the general economy and uncertainty in the financial markets

caused a significant tightening of credit by financial institutions. During difficult economic periods, such as we are now facing, strong liquidity is vital. We believe the Company has sufficient assets and credit availability to sustain itself through the downturn. While the Company's \$12 million revolving credit line expires in the third quarter of 2009, we have received verbal assurances from our lender that a renewal of the line should not be an issue for us at that time. The Company will begin negotiations for this renewal during the second quarter.

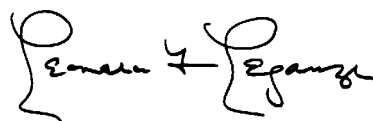
Another result of the financial breakdown in 2008 was that the value of the investment portfolios underlying the Company's pension plans was significantly lower at year-end than it had been at the end of 2007. As a result of this decline, the Company will need to make larger contributions to its plans over the next several years than would otherwise be the case. The Company will also experience additional charges against earnings. We are currently reviewing our investment policy to prevent future significant changes in contribution requirements as a result of changes in the market value of the plans' investments.

In recent years, some organizations have made the decision to discontinue defined benefit plans and rely on 401(k) plans as the main retirement option for their employees. While we have also looked carefully at this issue, we view the pension plans we sponsor as a valuable asset that helps us to retain current key employees and to attract new employees.

The detailed financial statements of the Company are included in the attached Form 10-K. As always, I urge you all to read it. With 2008, we completed our second year of full compliance with Section 404 of the Sarbanes-Oxley Act. Section 404 requires publicly traded companies to document, test and assess their internal financial controls. Included in our Form 10-K report are the required certifications stating that we are fully compliant with all provisions of the Act, and that the information contained in the report fairly presents, in all material respects, the financial condition and results of the operations of the Company.

When economic health returns, it will be important for us to be able to take advantage of the opportunities that we believe will be available. We cannot predict when or how the economy's problems will be resolved, but until then we will make every effort to put ourselves in a strong strategic position so that we can enjoy the benefits of that recovery.

As always, I thank our shareholders for their support and confidence, our Directors for their wise counsel and all our employees for their continuing hard work and dedication.



Leonard F. Leganza  
Chairman of the Board, President and Chief Executive Officer

# Financial Highlights (In Thousands)

|   | 2008             | 2007      | 2006      | 2005      | 2004      |
|---|------------------|-----------|-----------|-----------|-----------|
| Net Sales                                 | <b>\$135,878</b> | \$156,281 | \$138,465 | \$109,107 | \$100,130 |
| Net Income                                | <b>4,505</b>     | 10,081    | 9,659     | 4,367     | 4,758     |
| Income Taxes                              | <b>1,538</b>     | 4,765     | 5,187     | 2,653     | 2,071     |
| Income Before Taxes and Minority Interest | <b>6,002</b>     | 14,845    | 14,846    | 7,020     | 6,829     |
| Interest Expense                          | <b>1,064</b>     | 1,289     | 1,098     | 1,014     | 1,044     |
| Depreciation and Amortization             | <b>4,128</b>     | 4,370     | 3,746     | 3,460     | 3,461     |
| Capital Expenditures                      | <b>2,331</b>     | 2,868     | 6,722     | 1,750     | 2,062     |
| Dividends Paid                            | <b>1,938</b>     | 1,802     | 1,715     | 1,600     | 1,596     |

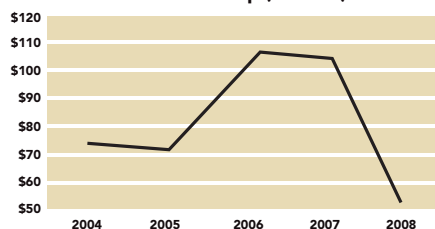
## PER SHARE DATA

|                                      |                  |           |           |           |           |
|--------------------------------------|------------------|-----------|-----------|-----------|-----------|
| Net Income (Diluted)                 | <b>\$0.73</b>    | \$1.68    | \$1.67    | \$0.75    | \$0.85    |
| Net Book Value                       | <b>10.14</b>     | 11.82     | 9.43      | 7.92      | 7.80      |
| Tangible Net Worth                   | <b>7.34</b>      | 8.81      | 6.30      | 5.61      | 5.42      |
| Net Working Capital                  | <b>7.91</b>      | 7.85      | 6.16      | 5.36      | 4.75      |
| Dividends                            | <b>0.33</b>      | 0.32      | 0.31      | 0.29      | 0.29      |
| Average Shares Outstanding (Diluted) | <b>6,159,563</b> | 5,989,754 | 5,768,108 | 5,828,837 | 5,618,552 |

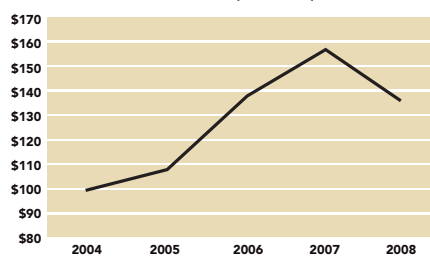
## FINANCIAL RATIOS

|  |              |       |       |       |       |
|--|--------------|-------|-------|-------|-------|
| Return on Investment                   | <b>6%</b>    | 19%   | 21%   | 10%   | 12%   |
| Net Income as a % of Sales             | <b>3%</b>    | 6%    | 7%    | 4%    | 5%    |
| Gross Profit Margin                    | <b>19%</b>   | 23%   | 25%   | 23%   | 25%   |
| Sales per Employee (in thousands)      | <b>\$195</b> | \$211 | \$199 | \$170 | \$158 |
| Net Income Per Employee (in thousands) | <b>\$6</b>   | \$14  | \$14  | \$7   | \$8   |
| Current Ratio                          | <b>4.8</b>   | 3.9   | 2.5   | 3.3   | 2.9   |

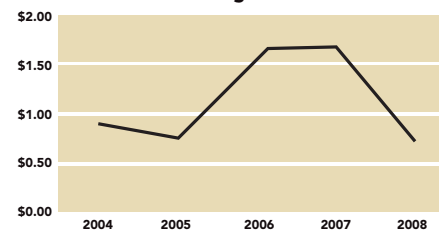
Market Cap (Millions)



Sales (Millions)



Earnings Per Share



# Security Products Group



## Greenwald Industries Division

Founded in 1954, Greenwald is a major manufacturer of coin and SmartCard vending solutions for route and retail laundry applications. Our full-line of products includes traditional coin/token chutes and drops, money boxes, meters, and state-of-the-art SmartCard readers and Add Value Stations. In 2006, Greenwald acquired Summit Manufacturing, a designer and manufacturer of oven latches, oven door switches and oven smoke eliminators for residential applications.



## The Illinois Lock Company/ CCL Security Products/Royal Lock Division World Lock Co. Ltd. World Security Industries Co. Ltd.

The Illinois Lock Company/CCL Security Products/Royal Lock Division produces custom-engineered locks for a variety of original equipment manufacturers and is a leading producer of keyless locks sold under well-known brand names such as Sesamee, Presto and Huski. With our Asian operations, World Lock and World Security, the Company can offer competitive pricing, service and delivery in a global economy.





# Industrial Hardware Group

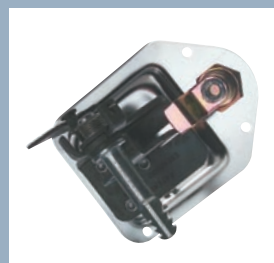
## Eberhard Manufacturing Division

The Eberhard Manufacturing Division of Cleveland, Ohio is a leading designer and manufacturer of industrial latching systems servicing various Original Equipment Manufacturers throughout North America. The extensive selection of products Eberhard provides includes external and internal operating handles and rotary latches for military, fire and rescue, service body, and other specialty and commercial vehicles; operating push buttons and slam latches for toolboxes and tonneau covers for the automotive and truck accessory markets. Eberhard also provides many other enclosure devices such as locking gear for over the road tractor trailers, operating devices for school and commercial buses as well as many access door devices for electrical, electronic and specialty metal enclosures.



## Eberhard Hardware Manufacturing Limited

Eberhard Hardware Manufacturing Limited of Ontario, Canada provides the wide line of traditional industrial latching products to the Canadian market as well as specialty hardware items for global markets. Working with toolbox OEM's in Canada and the United States, new and improved latching systems have also been developed. Additional specialty products include various connectors, brackets, stampings and assemblies for the appliance and electrical OEM markets.



## Sesamee Mexicana, S.A. de C.V.

Sesamee Mexicana is a distribution center for the Eberhard Manufacturing Division as well as other manufacturers of industrial and vehicular components. Located near Mexico City, Sesamee services the Original Equipment Manufacturers in the vehicular body, electrical enclosure and instrument case markets with hardware, drawer slides, rubber gaskets, and pneumatic gas springs as well as other complementary components.

## Canadian Commercial Vehicles Corporation

Canadian Commercial Vehicles ("CCV") is a full-service custom manufacturer of state-of-the-art lightweight honeycomb structures, fabricated metal products and assemblies for transport, construction, and industrial applications.



## Eastern Industrial Limited

Eastern Industrial, Ltd., Shanghai offers comprehensive capabilities for Asian sourcing, machine tool design, engineering, rapid prototyping, extensive manufacturing including metal stampings and plastic injection molding to final assembly.

# Metal Products Group

## Frazer & Jones Division

The Frazer & Jones Division is the leading producer of rock anchors in North America. These proprietary anchoring devices are a key component for underground mine roof support in coal and metallurgical mines. In the construction industry the rock anchors are used in tunneling, securing cross-country transmission towers and hydro construction. The Frazer & Jones Division is the only producer in the Western Hemisphere to combine design, engineering and the manufacturing of these products. Frazer & Jones also produces ductile and malleable iron castings to customer engineered specifications for the industrial hardware, pipefitting and construction industries.





## Board of Directors

**John W. Everets**  
Chairman  
Yorkshire Capital  
Boston, Massachusetts

**Charles W. Henry**  
Partner of Kernan & Henry  
Waterbury, Connecticut

**Leonard F. Leganza**  
Chairman of the Board, President  
and Chief Executive Officer  
of the Company

**David C. Robinson**  
Business Consultant

**Donald S. Tuttle, III**  
Business Consultant

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**Russell G. McMillen**  
Director Emeritus  
In July, 2008 Mr. McMillen passed away  
after more than 50 years of service with the  
Company.

## Officers and Executives

**Leonard F. Leganza**  
Chairman of the Board, President  
and Chief Executive Officer

**John L. Sullivan III**  
Vice President and  
Chief Financial Officer

**Kenneth R. Sapack**  
Chief Accounting Officer

**Gene A. Finelli**  
Treasurer

**Theresa P. Dews**  
Secretary

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**Brian H. Kay**  
Vice President  
Eberhard Manufacturing Division  
Eberhard Hardware Manufacturing, Ltd.  
Sesamee Mexicana, S.A. de C.V.  
Canadian Commercial Vehicles Corporation

**Leonard V. Samela**  
Vice President  
Greenwald Industries Division  
The Illinois Lock Company/  
CCL Security Products/  
Royal Lock Division

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**Roger Chang**  
Managing Director  
World Lock Co. Ltd.  
World Security Industries Co. Ltd.

**Richard E. Luehr**  
Managing Director  
Canadian Commercial Vehicles Corporation

**Mark F. Novakowski**  
Managing Director  
Frazer & Jones Division

# Summarized Financial Data

|   | 2008                  | 2007                  | 2006                  |
|---|-----------------------|-----------------------|-----------------------|
| <b>Statements of Earnings</b>                       |                       |                       |                       |
| Net sales   | \$ 135,878,490        | \$ 156,281,083        | \$ 138,465,411        |
| Cost of products sold                               | 110,415,392           | 120,343,196           | 103,881,660           |
| Other expenses                                      | 19,461,560            | 21,092,424            | 19,737,703            |
|   | <u>129,876,952</u>    | <u>141,435,620</u>    | <u>123,619,363</u>    |
| Income before income taxes and minority interest    | 6,001,538             | 14,845,463            | 14,846,048            |
| Income taxes  | 1,538,225             | 4,764,770             | 5,187,300             |
| Income before minority interest                     | 4,463,313             | 10,080,693            | 9,658,748             |
| Minority interest                                   | 41,310                | -                     | -                     |
| <b>NET INCOME</b>                                   | <u>\$ 4,504,623</u>   | <u>\$ 10,080,693</u>  | <u>\$ 9,658,748</u>   |
| Net income per share:                               |                       |                       |                       |
| Basic   | \$ 0.77               | \$ 1.79               | \$ 1.76               |
| Diluted   | \$ 0.73               | \$ 1.68               | \$ 1.67               |
| <b>Balance Sheets</b>                               |                       |                       |                       |
| <b>ASSETS</b>                                       |                       |                       |                       |
| Current assets                                      | \$ 61,692,263         | \$ 63,252,611         | \$ 59,326,242         |
| Property, plant and equipment, net                  | 23,910,709            | 25,234,214            | 25,815,717            |
| Prepaid pension cost                                | -                     | 1,792,657             | 266,358               |
| Deferred income taxes                               | 3,154,810             | -                     | -                     |
| Other assets, net                                   | 17,259,186            | 18,072,419            | 18,076,627            |
| <b>TOTAL ASSETS</b>                                 | <u>\$ 106,016,968</u> | <u>\$ 108,351,901</u> | <u>\$ 103,484,944</u> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>         |                       |                       |                       |
| Current liabilities                                 | \$ 12,947,508         | \$ 16,224,211         | \$ 23,780,282         |
| Deferred income taxes                               | -                     | 2,390,882             | 1,123,537             |
| Other long-term liabilities                         | 1,531,143             | 1,620,311             | -                     |
| Long-term debt, less current portion                | 11,428,571            | 14,383,060            | 17,506,802            |
| Accrued postretirement benefits                     | 1,062,719             | 1,111,234             | 1,221,156             |
| Accrued pension cost                                | 15,311,924            | 1,226,994             | 5,323,550             |
| Interest rate swap obligation                       | 1,169,848             | 577,941               | 138,412               |
| Minority interest                                   | 83,690                | -                     | -                     |
| Shareholders' equity                                | 62,481,565            | 70,817,268            | 54,391,205            |
| <b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>   | <u>\$ 106,016,968</u> | <u>\$ 108,351,901</u> | <u>\$ 103,484,944</u> |
| <b>Cash Flows</b>                                   |                       |                       |                       |
| <b>CASH FLOWS FROM OPERATIONS:</b>                  |                       |                       |                       |
| Net income  | \$ 4,504,623          | \$ 10,080,693         | \$ 9,658,748          |
| Depreciation and amortization                       | 4,128,312             | 4,369,998             | 3,745,693             |
| Other, net  | (1,019,710)           | (5,690,613)           | (5,541,487)           |
| Net cash provided by operating activities           | 7,613,225             | 8,760,078             | 7,862,954             |
| <b>INVESTING ACTIVITIES:</b>                        |                       |                       |                       |
| Purchases of plant, property and equipment          | (2,331,341)           | (2,867,829)           | (6,721,581)           |
| Other   | 13,246                | 25,120                | 19,374                |
| Business acquisitions                               | (128,325)             | -                     | (7,536,916)           |
| Net cash used by investing activities               | (2,446,420)           | (2,842,709)           | (14,239,123)          |
| <b>FINANCING ACTIVITIES:</b>                        |                       |                       |                       |
| Payments on debt                                    | (3,838,029)           | (3,111,907)           | (15,255,099)          |
| Proceeds from term loan                             | -                     | -                     | 20,000,000            |
| Tax benefit from stock options                      | 355,799               | 1,575,500             | -                     |
| Proceeds from sales of Common Stock                 | 1,861,486             | 2,562,997             | 203,700               |
| Purchases of Common Stock for treasury              | (610,526)             | (312,521)             | -                     |
| Dividends paid                                      | (1,938,172)           | (1,801,570)           | (1,715,035)           |
| Other   | (4)                   | (20)                  | (1,633)               |
| Net cash (used in) provided by financing activities | (4,169,446)           | (1,087,521)           | 3,231,933             |
| Effect of exchange rate changes on cash             | (239,456)             | 278,416               | (100,253)             |
| Net change in cash and cash equivalents             | 757,903               | 5,108,264             | (3,244,489)           |
| Cash and cash equivalents at beginning of year      | 8,209,722             | 3,101,458             | 6,345,947             |
| Cash and cash equivalents at end of year            | <u>\$ 8,967,625</u>   | <u>\$ 8,209,722</u>   | <u>\$ 3,101,458</u>   |

The information presented above has been derived from the audited consolidated financial statements of the Company as presented in the Form 10-K included in this report.

## Annual Meeting

The annual meeting of shareholders of The Eastern Company will be held on Wednesday, April 22, 2009 at 11:00a.m., local time, at the office of the Company, 112 Bridge Street, Naugatuck, CT 06770

## Independent Registered Public Accounting Firm

UHY LLP, Hartford, Connecticut

## Transfer Agent and Registrar

American Stock Transfer & Trust Co.  
40 Wall Street, New York, NY 10005  
1-800-937-5449

## Dividend Reinvestment & Stock Purchase Plan

The Eastern Company offers a Dividend Reinvestment Plan (DRP) which also features a no-load stock purchase program. It is available to all interested investors who would like to initiate or increase their holdings in The Eastern Company stock. To receive a brochure and application form for this plan, contact The Eastern Company directly at (203) 729-2255, ext. 104, or phone the program administrator, American Stock Transfer & Trust Co. at 1-800-278-4353. You may also enroll online by logging onto [www.INVESTPOWER.com](http://www.INVESTPOWER.com) and by entering the Company Ticker Symbol EML under Plan Search.

## Forward-Looking Statements

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

## Common Stock Market Prices and Dividends Paid

The Company's Common Stock is traded on the NYSE Alternext (formerly the American Stock Exchange) (ticker symbol EML). High and low stock prices and dividend payments for the past two years were:

| 2008    |                              |         |                            |
|---------|------------------------------|---------|----------------------------|
| Quarter | Sales Price<br>High      Low |         | Cash Dividends<br>Declared |
| First   | \$18.55                      | \$14.51 | \$.08                      |
| Second  | 20.00                        | 15.00   | .08                        |
| Third   | 16.10                        | 13.10   | .08                        |
| Fourth  | 13.40                        | 7.88    | .09                        |

| 2007    |                              |         |                            |
|---------|------------------------------|---------|----------------------------|
| Quarter | Sales Price<br>High      Low |         | Cash Dividends<br>Declared |
| First   | \$29.30                      | \$18.99 | \$.08                      |
| Second  | 33.90                        | 24.00   | .08                        |
| Third   | 29.28                        | 16.00   | .08                        |
| Fourth  | 23.77                        | 17.28   | .08                        |



# THE EASTERN COMPANY

## INDUSTRIAL HARDWARE GROUP

Eberhard Manufacturing Division  
Cleveland, Ohio  
[www.eberhard.com](http://www.eberhard.com)

Eberhard Hardware Manufacturing, Ltd.  
Tillsonburg, Ontario, Canada  
[www.eberhardcanada.com](http://www.eberhardcanada.com)

Canadian Commercial Vehicles Corporation  
Kelowna, British Columbia, Canada  
[www.ccvbc.com](http://www.ccvbc.com)

Eastern Industrial, Ltd.  
Shanghai, China  
[www.eischina.com](http://www.eischina.com)

Sesamee Mexicana, S.A. de C.V.  
Lerma, Mexico  
[www.sesamee.com.mx](http://www.sesamee.com.mx)

## SECURITY PRODUCTS GROUP

Greenwald Industries Division  
Chester, Connecticut  
[www.greenwaldindustries.com](http://www.greenwaldindustries.com)

The Illinois Lock Company/  
CCL Security Products/ Royal Lock Division  
Wheeling, Illinois  
[www.illinoislock.com](http://www.illinoislock.com)  
[www.cclsecurity.com](http://www.cclsecurity.com)  
[www.royallock.com](http://www.royallock.com)

World Lock Co. Ltd.  
World Security Industries Co. Ltd.  
Taipei, Taiwan; China  
[www.worldlock.com.tw](http://www.worldlock.com.tw)

## METAL PRODUCTS GROUP

Frazer & Jones Division  
Syracuse, New York  
[www.frazerandjones.com](http://www.frazerandjones.com)

