SMF ENERGY CORP
Form 10-Q
February 14, 2012

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 December 31, 2011

OR

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

Commission File Number 000-21825

SMF ENERGY CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	65-0707824
(State of Incorporation)	(IRS Employer Identification Number)

200 West Cypress Creek Road, Suite 400, Fort Lauderdale, Florida	33309
(Address of principal executive offices)	(Zip Code)

(954) 308-4200

(Registrant's telephone number, including area code)

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

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

Smaller reporting company x Large accelerated filer ¨ Non-accelerated filer ¨ (do not check if a smaller reporting company) Accelerated filer ¨

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

As of February 8, 2012 there were 8,587,523 shares of the registrant's common stock outstanding.

SMF ENERGY CORPORATION

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SMF ENERGY CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(in 000's, except share and per share data)

	December 31, 2011 (Unaudited)	June 30, 2011
ASSETS		
Current assets:		
Cash and cash equivalents	$ 53	$ 87
Accounts receivable, net of allowances of $1,226 and $1,011	18,962	20,872
Inventories, net of reserves of $108 and $94	2,737	2,125
Prepaid expenses and other current assets	871	706
Total current assets	22,623	23,790
Property and equipment, net of accumulated depreciation of $19,226 and $18,524	8,685	7,083
Identifiable intangible assets, net of accumulated amortization of $2,076 and $1,998	1,376	1,455
Goodwill	228	228
Deferred debt costs, net of accumulated amortization of $188 and $323	283	200
Deferred tax asset, net	3,738	-
Other assets	70	763
Total assets	$ 37,003	$ 33,519
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt	1,070	1,000
Accounts payable	8,615	9,361
Accrued expenses and other liabilities	4,210	3,668
Deferred tax liability, net	45	-
Total current liabilities	13,940	14,029
Long-term liabilities:		
Line of credit payable	7,223	7,921
Long-term debt, net of current portion	2,570	2,083
Promissory notes	800	800
Other long-term liabilities	633	685
Total liabilities	25,166	25,518
Commitments and Contingencies Shareholders' equity:		
Preferred stock, $0.01 par value; 5,000 Series D shares authorized; 534 and 599, respectively, issued and outstanding	-	-
Common stock, $0.01 par value; 50,000,000 shares authorized; 8,587,523 and 8,366,578, respectively, issued and outstanding	86	84
Additional paid-in capital	36,447	36,341
Accumulated deficit	(24,696)	(28,424)
Total shareholders' equity	11,837	8,001

Total liabilities and shareholders’ equity	$ 37,003	$ 33,519

The accompanying notes to the condensed unaudited financial statements are an integral part of these condensed consolidated balance sheets.

SMF ENERGY CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS (unaudited)

(in 000's, except per share data)

	For the Three Months Ended December 31, 2011	2010	For the Six Months Ended December 31, 2011	2010
Petroleum product sales and service revenues	$ 63,364	$ 46,608	$ 130,091	$ 91,665
Petroleum product taxes	7,193	5,956	14,671	11,960
Total revenues	70,557	52,564	144,762	103,625
Cost of petroleum product sales and service	59,275	42,820	121,022	84,039
Petroleum product taxes	7,193	5,956	14,671	11,960
Total cost of sales	66,468	48,776	135,693	95,999
Gross profit	4,089	3,788	9,069	7,626
Selling, general and administrative expenses	3,583	3,374	7,474	6,866
Executive retirement and related transition expenses	1,158	-	1,158	-
Operating income (loss)	(652)	414	437	760
Interest expense	(173)	(232)	(422)	(455)
Interest and other income	49	10	51	12
Income (loss) before income taxes	(776)	192	66	317
Income tax benefit (expense)	3,684	(58)	3,662	(69)
Net income	$ 2,908	$ 134	$ 3,728	$ 248
Basic and diluted net income per share computation:				
Net income per share attributable to common shareholders:				
Basic	$ 0.35	$ 0.02	$ 0.44	$ 0.03
Diluted	$ 0.33	$ 0.02	$ 0.43	$ 0.03
Weighted average common shares outstanding:				
Basic	8,405	8,505	8,386	8,527
Diluted	8,720	8,640	8,633	8,661
Dividends declared per common share	$ 0.015	$ -	$ 0.0275	$ -

The accompanying notes to the condensed unaudited financial statements are an integral part of these condensed unaudited consolidated statements of operations.

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SMF ENERGY CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(in 000's)

	For the Six Months Ended December 31, 2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 3,728	$ 248
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization:		
Depreciation for cost of sales items	442	446
Depreciation and amortization for selling, general and administrative items	480	594
Amortization of deferred debt costs	61	80
Amortization of stock-based compensation	343	70
Gain from sale of assets	(46)	(7)
Inventory reserve (recovery) provision	14	(4)
Provision for (recovery of) doubtful accounts	234	(113)
Deferred income tax benefit	(3,693)	-
Changes in operating assets and liabilities:		
Decrease in accounts receivable	1,676	147
Increase in inventories, prepaid expenses and other assets	(791)	(22)
Decrease in accounts payable, accrued expenses, and other liabilities	(510)	(1,154)
Net cash provided by operating activities	1,938	285
CASH FLOWS FROM INVESTING ACTIVITIES:		
Cash portion of Lufkin property purchase	(1,060)	-
Purchases of property and equipment	(373)	(251)
Proceeds from sale of equipment	74	22
Net cash used in investing activities	(1,359)	(229)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from line of credit	150,464	107,391
Repayments of line of credit	(151,161)	(106,821)
Proceeds from Lufkin real estate mortgage	1,057	-
Principal payments on term loan	(500)	(500)
Payment of loan costs	(144)	-
Payment of common shares dividends	(235)	-
Payment of preferred shares dividends	(13)	(13)
Capital lease payments	(81)	(31)
Repurchase and retirement of common stock	-	(140)
Common stock, preferred stock, and warrants issuance costs	-	(10)
Net cash used in financing activities	(613)	(124)

NET DECREASE IN CASH AND CASH EQUIVALENTS	(34)	(68)
CASH AND CASH EQUIVALENTS, beginning of period	87	115
CASH AND CASH EQUIVALENTS, end of period	$ 53	$ 47

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SMF ENERGY CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)

(in 000's)

(Continued)	For the Six Months Ended December 31, 2011	2010
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	$ 361	$ 402
Cash paid for income tax	$ 41	$ 51
SUPPLEMENTAL DISCLOSURE OF NON-CASH ACTIVITIES:		
Capital leases	$ 44	$ 591
Receivable settlement for Lufkin land and building	$ 693	$ -

The accompanying notes to the condensed unaudited financial statements are an integral part of these condensed unaudited consolidated statements of cash flows.

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SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

1. NATURE OF OPERATIONS

SMF Energy Corporation, a Delaware corporation, (the “Company”) provides petroleum product distribution services, transportation logistics and emergency response services to numerous industries including trucking, manufacturing, construction, shipping, utility, energy, chemical, telecommunications, waste and government services. The Company generates its revenues from commercial mobile and bulk fueling; the packaging, distribution and sale of lubricants; integrated out-sourced fuel management; transportation logistics, and emergency response services. The Company’s fleet of custom specialized tank wagons, tractor-trailer transports, box trucks and customized flatbed vehicles delivers diesel fuel and gasoline to customers’ locations on a regularly scheduled or as needed basis, refueling vehicles and equipment, re-supplying fixed-site and temporary bulk storage tanks, and emergency power generation systems; and distributes a wide variety of specialized petroleum products, lubricants and chemicals to its customers.

The Company is a Delaware corporation resulting from the February 2007 reincorporation of Streicher Mobile Fueling, Inc., a Florida corporation formed in 1996, in Delaware as SMF Energy Corporation.

At December 31, 2011, the Company was conducting operations through 34 service locations in the eleven states of Alabama, California, Florida, Georgia, Louisiana, Mississippi, Nevada, North Carolina, South Carolina, Tennessee and Texas.

2. CONDENSED SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation - The condensed unaudited consolidated financial statements include the accounts of SMF Energy Corporation and its wholly owned subsidiaries, SMF Services, Inc., H & W Petroleum Company, Inc., and Streicher Realty, Inc. Intercompany balances and transactions have been eliminated in consolidation.

The condensed unaudited consolidated financial statements included herein have been prepared in accordance with the instructions to Form 10-Q, and do not include all the information and footnotes required by generally accepted accounting principles; however, they do include all adjustments of a normal recurring nature that, in the opinion of management, are necessary to present fairly the financial position and results of operations of the Company as of and for the interim periods presented.

Operating results for the three and six months ended December 31, 2011 are not necessarily indicative of the results that may be expected for any subsequent period or the fiscal year ending June 30, 2012. These interim financial statements should be read in conjunction with the Company's audited consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the year ended June 30, 2011, as filed with the United States Securities and Exchange Commission (the "2011 Form 10-K").

SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

***Fair Value of Financial Instruments* -** The Company adopted ASC 825 *Financial Instruments,* which establish a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into three broad levels which distinguish between assumptions based on market data (observable inputs) and the Company's assumptions (unobservable inputs). The level in the fair value hierarchy within which the respective fair value measurement falls is determined based on the lowest level input that is significant to the measurement in its entirety. Level 1 inputs are quoted market prices in active markets for identical assets or liabilities, Level 2 inputs are other than quotable market prices included in Level 1 that are observable for the asset or liability either directly or indirectly through corroboration with observable market data. Level 3 inputs are unobservable inputs for the assets or liabilities that reflect management's own assumptions about the assumptions market participants would use in pricing the asset or liability.

3. CASH AND CASH EQUIVALENTS

Total cash and cash availability were approximately $5.8 million and $6.7 million at December 31, 2011 and June 30, 2011, respectively, and approximately $6.9 million on February 8, 2012. Total cash and cash availability includes cash and cash equivalents as presented in the Company's balance sheet and cash available to the Company for working capital, capital expenditures, dividends and debt service through its line of credit, as described in Note 5, Loan Facility.

The Company considers all highly liquid investments purchased with an original maturity of three months or less to be cash equivalents. The Company maintains its cash balances at financial institutions, which at times may exceed federally insured limits. The Federal Deposit Insurance Corporation currently insures balances up to $250,000. The Company has not experienced any losses in such bank accounts.

4. OUTSTANDING SHARES AND NET INCOME PER SHARE

As of December 31, 2011, there were 8,587,523 issued and outstanding shares of the Company's common stock, which includes 122,000 and 40,000 shares of unvested restricted shares issued on September 26, 2011 and November 30, 2011, respectively. The weighted average common shares used to calculate basic earnings per share do not include the unvested restricted shares. The restricted shares are evaluated under the treasury stock method for their dilutive effect. Basic net income per share is computed by dividing the net income attributable to common shareholders by the weighted average number of common shares outstanding during the period.

Diluted earnings per share is computed by dividing net earnings attributable to common shareholders by the weighted-average number of common shares outstanding, increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been issued. Conversion or exercise of the potential common shares is not reflected in diluted earnings per share unless the effect is dilutive. The dilutive effect, if any, of outstanding common share equivalents is reflected in diluted earnings per share by application of the if-converted and the treasury stock method, as applicable. In determining whether outstanding stock options and common stock warrants should be considered for their dilutive effect, the average market price of the common stock for the period has to exceed the exercise price of the outstanding common share equivalent.

SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

Diluted net income per share for the three and six-months ended December 31, 2011 and 2010, was diluted by additional common stock equivalents as follows (in thousands of shares):

	For the Three Months ended December 31,		For the Six Months ended December 31,	
	2011	2010	2011	2010
Incremental shares due to stock options awarded to employees and directors	17	2	6	1
Incremental shares due to debt conversion rights	89	-	89	-
Incremental shares due to preferred stock conversion rights	119	133	119	133
Incremental shares due to restricted shares	90	-	33	-
Total dilutive shares	315	135	247	134

Anti-dilutive common stock equivalents outstanding and not included in the computation of diluted net income per common share consisted of (in thousands of shares):

	For the Three Months ended December 31,		For the Six Months ended December 31,	
	2011	2010	2011	2010
Stock options	200	288	211	288
Common stock warrants	141	141	141	141
Unvested restricted shares	72	-	129	-
Promissory note conversion rights	-	89	-	89
Total common stock equivalents outstanding	413	518	481	518

SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

The following table sets forth the computation of basic and diluted net income per share (in thousands of dollars and shares, except per share amounts):

	For the Three Months Ended, December 31, 2011			December 31, 2010		
	Earnings	Weighted Average Common Shares	Per Share Amount	Earnings	Weighted Average Common Shares	Per Share Amount
Basic net income per share attributable to common shareholders	$2,908	8,405	$ 0.35	$134	8,505	$ 0.02
Effect of dilutive securities:						
Stock options	-	17		-	2	
Debt conversion right	3	89		-	-	
Preferred stock conversion rights	-	119		-	133	
Restricted shares	-	90		-	-	
Diluted net income per share attributable to common shareholders	$2,911	8,720	$ 0.33	$134	8,640	$ 0.02

	For the Six Months Ended, December 31, 2011			December 31, 2010		
	Earnings	Weighted Average Common Shares	Per Share Amount	Earnings	Weighted Average Common Shares	Per Share Amount
Basic net income per share attributable to common shareholders	$3,728	8,386	$ 0.44	$248	8,527	$ 0.03
Effect of dilutive securities:						
Stock options	-	6		-	1	
Debt conversion right	6	89		-	-	
Preferred stock conversion rights	-	119		-	133	
Restricted shares	-	33		-	-	
	$3,734	8,633	$ 0.43	$248	8,661	$ 0.03

Diluted net income per share attributable to common shareholders

5. LOAN FACILITY

On September 27, 2011, the Company amended and extended its loan facility with its principal lender with significant improvements in the terms. As of December 31, 2011, the loan facility was $28.7 million, comprised of a $25.0 million revolving line of credit (the "Line of Credit'), a $2.6 million term loan, originally based on a 60 month, fully amortized term, which matures on July 1, 2014 (the "Term Loan"), and a $1.057 million fifteen-year amortization mortgage loan (the "Mortgage Loan"). The amendment included a 5 year renewal of the Line of Credit and improved interest rates. The Line of Credit has a renewal date of September 27, 2016. Like the Term Loan, the Mortgage Loan is co-terminus with the Line of Credit. Interest is payable monthly based on a pricing matrix. At December 31, 2011, the interest rate for the Line of Credit was 2.83%. This rate was priced using 90 day LIBOR of 0.58%, plus the applicable margin of 2.25%. The applicable margin is determined quarterly based on a predetermined fixed charge coverage ratio pricing matrix with the applicable margins ranging from 2.00% to 3.00%.

SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

The Line of Credit enables the Company to satisfy its obligations during the time gap created between the payment for its petroleum products and the time when it collects this cost from its customers. As such, due to the volatility of petroleum products' pricing, the outstanding borrowings fluctuate with changes in petroleum market prices in addition to changes in demand from customers. As of December 31, 2011 and June 30, 2011, the Company had outstanding borrowings of $7.2 million and $7.9 million, respectively, under the Line of Credit, which does not include stand-by letters of credit that reduce the line's cash availability. Based on eligible receivables and inventories, and reduction from letters of credit outstanding at December 31, 2011 and June 30, 2011, the Company had $5.7 million and $6.6 million of cash availability under the Line of Credit, respectively.

The Line of Credit provides for certain affirmative and negative covenants that may limit the total availability based upon the Company's ability to meet these covenants. At December 31, 2011, the financial covenants included a minimum daily availability of $250,000, a fixed charge coverage ratio of 1.1 to 1.0, and a capital expenditure limitation for fiscal year 2012 of $750,000. At December 31, 2011 and June 30, 2011, the Company had a sublimit for standby letters of credit under its $25.0 million line of credit of $1.75 million, on both dates. At December 31, 2011 and June 30, 2011, $900,000 and $1.2 million, respectively, had been issued in standby letters of credit. The Line of Credit was not limited at any time during either period by these covenants.

The amended loan agreement with the Company's principal lender (the "Loan Agreement") for the Line of Credit, the Term Loan and the Mortgage Loan (together, the "Loan and Credit Facility") continues to require the Company to obtain the consent of the lender prior to incurring additional debt, paying any cash dividends or distributions, repurchasing shares of its capital stock or entering into mergers, consolidations or sales of assets outside the ordinary course of business. Failure to comply with one or more of these covenants could affect the amount the Company can borrow and thereby adversely affect the Company's liquidity and financial condition. The lender previously granted its consent to the stock repurchase program that was in effect during fiscal year 2011. That repurchase program ended on August 4, 2011 when the lender consented to the commencement of the Company's currently ongoing Dividend Program. See Note 7, Shareholders' Equity. At December 31, 2011, the Company was in compliance with its covenants under the Loan Agreement. See Note 6, Long-Term Debt, for further details on the Term Loan and the Mortgage Loan, which balances were $2.583 million and $1.057 million at December 31, 2011, respectively.

SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

6. LONG-TERM DEBT

Long-term debt consists of the following (in thousands):

	As of December 31, 2011	June 30, 2011
June 2009 Term Loan, fully amortized, 60 monthly principal payments of approximately $83,333 commencing on August 1, 2009; variable interest due monthly, 3.08% at December 31, 2011; secured by substantially all Company assets and subject to co-terminus provisions under the Line of Credit or matures July 1, 2014 whichever occurs first, and is cross collateralized and cross defaulting with the rest of the Loan and Credit Facility.	$ 2,583	$ 3,083
June 2009 Unsecured convertible subordinated promissory note (the "June 2009 Note") (5.5% interest due semi-annually, January 15 and July 15, beginning January 15, 2011; interest accrued for first 13 months was deferred and paid on August 12, 2010); matures July 1, 2014 in its entirety.	800	800
November 2011 fifteen-year amortization Mortgage Loan; 180 monthly principal payments of approximately $6,000 commencing on January 1, 2012; variable interest due monthly, 3.08% at December 31, 2011; subject to co-terminus provisions under the Line of Credit. Secured by its respective real estate and is cross-collateralized and cross defaulting with the rest of the Loan and Credit Facility.	1,057	-
September 2011 Line of Credit (interest is based on pricing matrix plus LIBOR 90 day floating rate, the line matures September 27, 2016, if not renewed). Secured by substantially all Company assets and is cross-collateralized and cross defaulting with the rest of the Loan and Credit Facility.	7,223	7,921
Total long-term debt	11,663	11,804
Less: current portion	(1,070)	(1,000)
Long-term debt, net of current portion	$ 10,593	$ 10,804

At December 31, 2011, the Company had $2.583 million outstanding on the Term Loan, and a $1.057 million outstanding on the Mortgage Loan as part of the $28.7 million Loan and Credit Facility. The Term Loan, which originally had a 60 month term, matures on July 1, 2014, subject, however, to earlier termination in the event of termination of the revolving line. As a result of the September 27, 2011 amendment of the Loan Agreement and extension of the Loan and Credit Facility, the interest rates of the Term Loan were reduced. At December 31, 2011, the variable interest rate on the Term Loan was 3.08%, which consisted of 2.50% plus LIBOR 90 day rate. The LIBOR 90 day rate at December 31, 2011 was 0.58%.

The Company has a 5.5%, interest only, unsecured, convertible subordinated promissory note in the principal amount of $800,000 which matures July 1, 2014 (the “June 2009 Note”). The June 2009 Note is subordinated to all other existing debt of the Company, including any amounts owed now or in the future to our principal lender. The holder of the June 2009 Note entered into a debt subordination agreement (the “Subordination Agreement”) with the Company and its principal lender, whereby it expressly subordinated its rights under the June 2009 Note to its principal lender. The June 2009 Note is subject to the limitations in the Subordination Agreement, interest is paid semi-annually, except that the interest payment for the first thirteen months was paid on August 12, 2010. Thereafter, semi-annual interest payments are scheduled on or about each January 15th and July 15th. All required interest payments have been paid timely. Unpaid amounts under the June 2009 Note will become due and payable upon the occurrence of customary events of default, provided, however, that the deferral of any payment in accordance with the Subordination Agreement will not constitute an event of default. If permitted under the Subordination Agreement, the Company may pre-pay the June 2009 Note, in whole or in part, without prepayment penalty or premium.

SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

Twenty-five percent (25%) of the original principal amount of the June 2009 Note, or $200,000, may be converted into shares of the Company's Common Stock at $2.25 per share (the "Conversion Price") at the option of the noteholder. The number and kind of securities purchasable upon conversion and the Conversion Price remain subject to additional adjustments for stock dividends, stock splits and other similar events. As of December 31, 2011, there have been no conversions.

In connection with a June 2011 litigation settlement, the Company received land and a building in Lufkin, Texas, that the Company had previously leased from the conveying party. As part of the conveyance in September 2011, the Company paid off the then existing mortgage on the property with funds from its revolving line of credit. The Company's principal lender provided the Mortgage Loan on the property for $1.057 million, in November of 2011, which provides for repayment in 180 monthly principal payments of approximately $6,000. At December 31, 2011, the variable interest rate on the mortgage was 3.08%, which consisted of 2.50% plus LIBOR 90 day rate of 0.58%.

7. SHAREHOLDERS' EQUITY

The following reflects the change in shareholders' equity for the six months ended December 31, 2011 (in thousands, except share data):

	Preferred Stock Series D		Common Stock		Additional Paid-in	Accumulated	
	Shares	Amount	Shares	Amount	Capital	Deficit	Total
Balance at June 30, 2011	599	$ -	8,366,578	$ 84	$ 36,341	$ (28,424)	$ 8,001
Net income	-	-	-	-	-	3,728	3,728
Issuance of common shares as share-based compensation	-	-	13,000	-	33	-	33
Issuance of unvested restricted shares as share-based compensation	-	-	162,000	1	216	-	217
Issuance of vested restricted shares as share-based compensation	-	-	31,500	1	77	-	78

Share-based compensation amortization expense	-	-	-	-	14	-	14
Conversion of preferred shares to common shares	(65)	-	14,445	-	-	-	-
Common shares dividends	-	-	-	-	(234)	-	(234)
Balance at December 31, 2011	534	$ -	8,587,523	$ 86	$ 36,447	$ (24,696)	$ 11,837

Shared-Based Compensation

Shared-based compensation includes stock options or common shares that have been issued to employees, directors, or for retirement compensation, and are shown in the table above under the appropriate classification whether vested, unvested, issued or amortized.

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SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

The Company is authorized to grant stock options and other equity awards to employees and other eligible persons under the 2009 Equity Incentive Plan (the “2009 Plan”), which currently has 2,004 stock options and 263,000 other stock awards outstanding. The Company no longer grants stock options under the 2000 Employee Stock Option Plan (the “2000 Plan”) but stock options to purchase 161,897 shares of Common Stock remain outstanding under the 2000 Plan. Options granted under the 2000 Plan generally vest over three years of continuous service and expire no later than ten years from the date of grant. As of December 31, 2011, all outstanding options under the 2009 Plan and the 2000 Plan are vested and exercisable.

The Company also no longer grants stock options under its Directors Stock Options Plan but options to purchase 53,272 shares of Common Stock remain outstanding under that plan. All outstanding stock options under the Directors Stock Option Plan are fully vested and presently exercisable.

In September 2011 and December 2011, the Company issued 7,000 and 6,000 fully vested shares, respectively, of its common stock to the non-employee members of its Board of Directors from the 2009 Plan, which were valued at $2.45 and $2.85 per share, respectively, the market closing price on the last trading day prior to their issuance. The aggregate fair value of those two grants was $33,000 and was recognized as stock-based compensation expense during the six months ended December 31, 2011.

Restricted Stock Grants. On September 26, 2011, the Compensation Committee of the Company’s Board of Directors (the “Committee”) granted 93,500 unvested restricted shares of the Company’s common stock to the Company’s then President and Chief Executive Officer (the “Executive”) under the 2009 Plan. The September 2011 restricted shares were to vest in three tranches: 31,500 shares on November 1, 2011, 31,000 on November 1, 2012 and 31,000 shares on November 1, 2013. On November 16, 2011, in connection with the retirement of the Executive, the Company modified the vesting date of the remaining 62,000 non vested shares to 31,000 vesting on July 31, 2012 and 31,000 vesting on January 31, 2013, subject to the Executive’s compliance with various restrictive covenants originally contained in the Executive’s employment agreement until the time of vesting. The 31,500 shares that vested on November 1, 2011 were valued at $2.47 per share, the market closing price on the last trading day prior to their issuance for an aggregate value of $78,000. The 62,000 non vested shares were valued at $2.92 per share, the market closing price on the last day prior to the modification for an aggregate value of $181,000. In the quarter ended December 31, 2011, the Company has recorded these restricted shares in Shareholders’ Equity with a corresponding expense recorded as executive retirement and related transition expense. Per the terms of the original grant, in November 2011, the Company paid the Executive $47,000 in connection with the shares that vested on November 1, 2011, based on 50% of the value of the stock on that date. This payment was made to mitigate the tax impact of such grants.

On September 26, 2011, the Committee also granted 60,000 shares of unvested restricted stock to eleven other officers under the 2009 Plan. All of these grants vest over a three year period, with 33% vesting on each anniversary date of the September 26, 2011 grants. These shares were valued at $2.47 per share, the market closing price on the last trading day prior to their issuance.

On November 30, 2011, the Company awarded 40,000 shares of unvested restricted stock to its new President and Chief Executive Officer under the 2009 Plan pursuant to his employment agreement. These shares were valued at $2.64 per share, the market closing price on the last trading day prior to their issuance, and will vest after a year of employment.

During the three months ended December 31, 2011 and 2010, the Company recorded amortization of share-based compensation expense related to the various stock option plans of $14,000 and $49,000, respectively.

Preferred Stock Conversion

On October 20, 2011, 65 shares of preferred stock were converted into 14,445 shares of common stock.

SMF ENERGY CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)

Common Stock Dividend

On August 9, 2011, the Company's Board of Directors (the "Board") approved a quarterly cash dividend program (the "Dividend Program"), starting with a dividend of $0.0125 per share, which was paid on October 14, 2011, to shareholders of record as of the close of business on September 28, 2011. On October 3, 2011, the Board declared a second quarterly cash dividend of $0.015, which was paid on December 2, 2011, to shareholders of record on November 14, 2011. On January 12, 2012, the Board declared a quarterly cash dividend of $0.01725 per share payable to shareholders of record at the close of business on February 14, 2012, to be paid on March 9, 2012. The timing and amount of future dividends remain subject to Board of Directors approval. The Dividend Program replaced the Company's open market stock repurchase program, which was terminated in August of 2011. The Company's principal lender has granted its consent to the Dividend Program, which consent is required by the Loan Agreement, so long as (a) the Company maintains a ratio of EBITDA to Fixed Charges for the most recent twelve-month period, giving pro forma effect to any dividend payments to be made or already made that are not reflected therein, of at least 1.3 to 1.0, (b) at all times during the 90-day period preceding each dividend payment and after giving pro forma effect to any proposed payments, the Company maintains Excess Availability of not less than $2,250,000 under the Loan Agreement, (c) aggregate dividends do not exceed $600,000 per annum or $150,000 per quarter, and (d) no Default or Event of Default exists under the Loan Agreement. Capitalized terms are defined in the Loan Agreement.

8. DEFERRED TAX ASSET VALUATION ALLOWANCE

As of June 30, 2011, the Company had a valuation allowance against its net deferred tax asset of approximately $9.4 million as the Company believed it was more likely than not that some or all of the deferred tax assets would not be realized. This assessment was based on the Company's cumulative historical losses and uncertainties as to the amount of taxable income that would be generated in future years. During the second quarter of fiscal 2012, the Company determined that it was more likely than not that a portion of the deferred tax assets would be realized and reversed $3.7 million of the valuation allowance. This resulted in the Company recording an income tax benefit of $3.7 million in the quarter ended December 31, 2011. This benefit has resulted in increased earnings per share for basic earnings per share purposes of $0.44 for both the three and six months periods ended December 31, 2011, and has resulted in an increase in earnings per share for diluted earnings per share purposes of $0.42 and $0.43 for the three and six month periods ended December 31, 2011, respectively. The determination to reduce the valuation allowance as of December 31, 2011, was based primarily on the Company's continued profitability. The estimated realizable net deferred tax asset of approximately $3.7 million recorded as of December 31, 2011, is an estimate that is subject to adjustment in the future based on the Company's continuing evaluation of its potential ability to maximize the asset under IRC Section 382.

9. EXECUTIVE RETIREMENT AND RELATED TRANSITION EXPENSES

In November 2011, the Company reported that Richard E. Gathright retired from his positions as President and Chief Executive Officer, and Steven R. Goldberg, a member of our Board of Directors since 2005, assumed those duties. Mr. Gathright also retired from his position as Chairman of the Board of Directors and another longstanding Board member, Larry S. Mulkey, assumed those duties.

As a result of Mr. Gathright's retirement in November 2011, we recorded a $1.2 million Executive retirement and related transition expense, consisting of $286,000 of non-cash stock-based compensation, and $872,000 in severance and retirement benefits and other transition costs, of which $103,000 was paid in the second quarter of fiscal 2012, with the remainder payable over the next 18 months.

10. SETTLEMENT RECEIVABLE

As a result of a settlement agreement effectuated on June 30, 2011, the Company recorded a net receivable settlement of $693,000 in other assets as reflected in the accompanying June 30, 2011 Condensed Consolidated Balance Sheet. The net receivable of $693,000 represented land valued at $500,000, a building valued at $1.28 million, which were received in September 2011, less a related mortgage liability of $1.057 million. As part of the settlement in June 2011, the Company relieved a prior receivable due of $632,000, and relieved an asset retirement obligation liability of $171,000. During fiscal 2012, we received the land and the building, paid off the existing mortgage on the property with funds from our revolving line of credit, and relieved the receivable of $693,000 that we had recorded in June 2011. As fully described in Note 6, Long-term Debt, the Company obtained a new mortgage loan on the property in November 2011.

SMF ENERGY CORPORATION AND SUBSIDIARIES

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11. CONTINGENCIES

The Company and its subsidiaries are from time to time parties to legal proceedings, lawsuits and other claims incident to their business activities. Such matters may include, among other things, assertions of contract breach, claims for indemnity arising in the course of the business and claims by persons whose employment with us has been terminated. Such matters are subject to many uncertainties, and outcomes are not predictable with assurance. Consequently, management is unable to ascertain the ultimate aggregate amount of monetary liability, amounts which may be covered by insurance or recoverable from third parties, or the financial impact with respect to these matters as of December 31, 2011. Therefore, no contingency gains or losses have been recorded as of December 31, 2011. However, management believes that the final resolution of such matters pending at the time of this report, individually and in the aggregate, will not have a material adverse effect upon the Company’s consolidated financial position, results of operations or cash flows.

12. RECENT ACCOUNTING PRONOUNCEMENTS

In December 2010, the FASB issued ASU No. 2010-28 related to goodwill and intangible assets. Under current guidance, testing for goodwill impairment is a two-step test. When a goodwill impairment test is performed, an entity must assess whether the carrying amount of a reporting unit exceeds its fair value (Step 1). If it does, an entity must perform an additional test to determine whether goodwill has been impaired and to calculate the amount of that impairment (Step 2). The objective of ASU No 2010-28 is to address circumstances in which
e> **Description Balance Sheet Location Fair Value**

Derivatives designated as hedging instruments under FAS133:

Commodity Contracts
Other Current Assets $205
Commodity Contracts
Other Long Term Assets $81
Commodity Contracts
Other Current Liabilities $12,124
Commodity Contracts
Other Long Term Liabilities $5,222
Foreign Exchange Contracts
Other Current Assets $591
Foreign Exchange Contracts
Other Current Liabilities $19

Derivatives not designated as hedging instruments under FAS133:

Foreign Exchange Contracts
Other Current Assets $434
Foreign Exchange Contracts
Other Current Liabilities $259

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The following table sets forth the effect of the Company s derivative instruments on financial performance for the three months ended June 28, 2009:

Description	Amount of Gain or (Loss) Recognized in OCI on Derivative (Effective Portion)	Location of Gain or (Loss) Reclassified from Accumulated OCI Into Income (Effective Portion)	Amount of Gain or (Loss) Reclassified from Accumulated OCI Into Income (Effective Portion)	Location of Gain or (Loss) Recognized in Income on Derivative (Ineffective Portion)	Amount of Gain or (Loss) Recognized in Income on Derivative (Ineffective /ePortion)
Derivatives in FAS133 Cash Flow Hedging Relationships:					
Foreign Exchange Contracts	$ 2,133	Net sales	$ 894	Net sales	$
		Cost of sales	$ (583)	Cost of sales	$
Commodity Contracts	$ (433)	Cost of sales	$ (8,941)	Cost of sales	$ (1)

Derivatives not designated as hedging instruments under FAS133:	Location of Gain or (Loss) Recognized in Income Statement	Gain or (Loss) Recognized
Foreign Exchange Contracts	Cost of sales	$ 1,184

The following table sets forth the effect of the Company s derivative instruments on financial performance for the six months ended June 28, 2009:

	Amount of Gain or (Loss) Recognized in OCI on Derivative	Location of Gain or (Loss) Reclassified from Accumulated OCI Into Income	Amount of Gain or (Loss) Reclassified from Accumulated OCI Into Income	Location of Gain or (Loss) Recognized in Income on Derivative	Amount of Gain or (Loss) Recognized in Income on Derivative

Description	(Effective Portion)	(Effective Portion)	(Effective Portion)	(Ineffective Portion)	(Ineffective Portion)
Derivatives in FAS133 Cash Flow Hedging Relationships:					
Foreign Exchange Contracts	$ 1,549	Net sales	$ 354	Net sales	$
		Cost of sales	$ (380)	Cost of sales	$
Commodity Contracts	$ (11,950)	Cost of sales	$ (14,882)	Cost of sales	$ 453

Derivatives not designated as hedging instruments under FAS133:	Location of Gain or (Loss) Recognized in Income Statement	Gain or (Loss) Recognized
Foreign Exchange Contracts	Cost of sales	$ 901

Note 8: Dividend Declarations

On April 15, 2009, the Board of Directors declared a regular quarterly dividend of $0.27 per share. This dividend was paid June 10, 2009 to all shareholders of record as of May 15, 2009.

On July 15, 2009, the Board of Directors declared a regular quarterly dividend of $0.27 per share. This dividend is payable September 10, 2009 to all shareholders of record as of August 21, 2009.

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Note 9: Employee Benefit Plans

Retirement Plans and Retiree Health and Life Insurance Plans

The Company provides non-contributory defined benefit pension plans for a majority of its employees in the United States and certain of its employees in Mexico and Belgium. Effective December 31, 2003, the Company froze participation for newly hired salaried and non-union hourly U.S. employees in its traditional defined benefit plan. The Company adopted a defined contribution plan, the Sonoco Investment and Retirement Plan (SIRP), covering its non-union U.S. employees hired on or after January 1, 2004. The Company also sponsors contributory pension plans covering the majority of its employees in the United Kingdom, Canada, and the Netherlands, as well as postretirement healthcare and life insurance benefits to the majority of its retirees and their eligible dependents in the United States and Canada.

On February 4, 2009, the U.S. qualified defined benefit pension plan was amended to freeze plan benefits for all active participants effective December 31, 2018. At that time, remaining active participants in the U.S. qualified plan will become participants of the SIRP effective January 1, 2019. Current participants of the U.S. qualified plan have a one-time option to transfer into the SIRP effective January 1, 2010. The choice for this one-time election must be made prior to August 28, 2009.

The plan amendment referred to above required a remeasurement of the U.S. qualified plan s assets and liabilities as of February 4, 2009. The following table reconciles the U.S. qualified plan s beginning of year obligations and assets to their values on the remeasurement date:

	U.S Qualified Defined Benefit Pension Plan
Change in Benefit Obligation	
Benefit obligation at January 1, 2009	$ 860,247
Service cost	1,633
Interest cost	4,268
Liability gain due to curtailment	(18,493)
Actuarial gain	(43,800)
Benefits paid	(3,330)
Benefit obligation at February 4, 2009	$ 800,525
Change in Plan Assets	
Fair value of Plan assets at January 1, 2009	$ 593,988
Actual return on Plan assets	(30,290)
Benefits paid	(3,330)
Expenses paid	(258)
Fair value of Plan assets at February 4, 2009	$ 560,110
Funded Status of the Plan	$ (240,415)

The discount rate used to determine the benefit obligation of the U.S. qualified defined benefit plan was 6.52% and 6.10% at February 4, 2009 and December 31, 2008, respectively.

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The components of net periodic benefit cost include the following:

	Three Months Ended		Six Months Ended	
	June 28, 2009	June 29, 2008	June 28, 2009	June 29, 2008
Retirement Plans				
Service cost	$ 5,646	$ 6,546	$ 11,333	$ 13,069
Interest cost	18,114	18,914	35,362	37,710
Expected return on plan assets	(14,770)	(22,586)	(29,050)	(45,024)
Amortization of net transition obligation	98	58	188	123
Amortization of prior service cost	243	398	514	961
Amortization of net actuarial loss	10,009	3,530	19,846	7,179
Effect of curtailment loss		2,289	2,344	2,289
Effect of settlement loss	838	297	838	297
Net periodic benefit cost	$ 20,178	$ 9,446	$ 41,375	$ 16,604
Retiree Health and Life Insurance Plans				
Service cost	$ 349	$ 516	$ 687	$ 1,028
Interest cost	1,014	1,127	1,994	2,244
Expected return on plan assets	(287)	(481)	(565)	(956)
Amortization of prior service credit	(2,781)	(2,593)	(5,470)	(5,159)
Amortization of net actuarial loss	831	776	1,635	1,543
Net periodic benefit income	$ (874)	$ (655)	$ (1,719)	$ (1,300)

As a result of the amendment to the U.S. qualified defined benefit pension plan, the Company recognized a $2,344 curtailment loss in the first quarter of 2009. Approximately 75% of this charge is included in Cost of sales in the Condensed Consolidated Statements of Income; the remainder is included in Selling, general and administrative expenses. The closure of a paper mill in Canada in 2008 resulted in the recognition of a $2,289 curtailment loss in the second quarter of 2008 and a settlement loss of $838 in the second quarter of 2009. These charges are included in Restructuring/Asset impairment charges in the Condensed Consolidated Statements of Income.

During the six months ended June 28, 2009, the Company made contributions of $9,279 to its defined benefit retirement and retiree health and life insurance plans. The Company anticipates that it will make additional contributions of approximately $8,100 in 2009. The Company also contributed $4,847 to the SIRP during this same six-month period. No additional SIRP contributions are expected during the remainder of 2009. Funding of the Company s U.S. qualified defined benefit pension plans, although not required in 2009, is currently expected to be approximately $60 million in 2010. However, if actual returns on plan assets in 2009 are lower than the expected rate of return of 8.5%, the required funding could be higher. Conversely, if actual returns are higher than the expected rate, the required funding could be lower.

Sonoco Savings Plan

The Company sponsors the Sonoco Savings Plan, a defined contribution retirement plan, for its U.S. employees. The plan provides for participant contributions of 1% to 30% of gross pay. The plan provides 100% Company matching on the first 3% of pre-tax contributions, 50% Company matching on the next 2% of pre-tax contributions and 100% immediate vesting. On April 15, 2009, Sonoco s Board of Directors approved an amendment to the Sonoco Savings Plan temporarily suspending the Company s matching contribution effective as of June 1, 2009. The Board intends to reevaluate matching contributions once business conditions allow.

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Note 10: Income Taxes

The Company adopted the provisions of Financial Accounting Standards Board Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), on January 1, 2007. There have been no significant changes in the Company s liability for uncertain tax positions since December 31, 2008.

The Company s effective tax rate for the three and six-month periods ending June 28, 2009 was 31.9% and 32.2%, respectively. These rates varied from the U.S. statutory rate primarily due to the favorable effect of international operations that are subject to tax rates generally lower than the U.S. rate, state taxes and the effect of the manufacturer s deduction and other U.S. tax adjustments. The Company s effective tax rate for the three and six-month periods ending June 29, 2008 was 26.0% and 29.5%, respectively. The rate for the second quarter of 2008 varied from the U.S. statutory rate primarily due to the favorable effect of international operations that are subject to tax rates generally lower than the U.S. rate, a tax benefit associated with a change in Italian tax law, state taxes and the effect of the manufacturer s deduction and other U.S. tax adjustments. The rate for the six months ended June 29, 2008 varied from the U.S. statutory rate due to these same factors as well as a valuation allowance recorded against the capital loss carryovers created by the impairment of financial assets discussed in Note 3 and certain restructuring charges for which tax benefits could not be recognized.

The Company and/or its subsidiaries file federal, state and local income tax returns in the United States and various foreign jurisdictions. The Company is no longer subject to U.S. federal income tax examination by tax authorities for years before 2005. With few exceptions, the Company is no longer subject to examination prior to 2004 with respect to U.S. state and local and non-U.S. income taxes.

The Company s estimate for the potential outcome for any uncertain tax issue is highly judgmental. Management believes that any reasonably foreseeable outcomes related to these matters have been adequately provided for. However, future results may include favorable or unfavorable adjustments to estimated tax liabilities in the period the assessments are made or resolved or when statutes of limitation on potential assessments expire. Additionally, the jurisdictions in which earnings or deductions are realized may differ from current estimates. As a result, the Company s effective tax rate may fluctuate significantly on a quarterly basis.

Note 11: New Accounting Pronouncements

In April 2009, the FASB issued FSP FAS 141(R)-1, Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies. This FASB Staff Position (FSP) modifies FAS 141(R) to provide that contingent assets acquired or liabilities assumed in a business combination be recorded at fair value if the acquisition-date fair value can be determined during the measurement period. If not, such items would be recognized at the acquisition date if they meet the recognition requirements of FAS 5. In periods after the acquisition date, an acquirer shall account for contingent assets and liabilities that were not recognized at the acquisition date in accordance with other applicable GAAP, as appropriate. Items not recognized as part of the acquisition but recognized subsequently would be reflected in that subsequent period s income. This FSP, which was effective for the Company when issued, has no impact on the Company s current financial statements, but will apply to any future acquisitions.

In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1, Interim Disclosures about Fair Value of Financial Instruments which requires publicly traded companies to provide disclosure about the fair value of financial instruments whenever interim summarized financial information is reported. Previously, disclosures about the fair value of financial instruments were only required on an annual basis. Disclosure shall include the method(s) and significant assumptions used to estimate the fair value of financial instruments and shall describe changes in method(s) and significant assumptions, if any, during the period. This FSP is effective for interim and annual periods ending after June 15, 2009, and, as such, the Company began including this disclosure with its second quarter 2009 financial statements.

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In May 2009, the Financial Accounting Standards Board (FASB) issued Financial Accounting Statement (FAS) No. 165, Subsequent Events. This FAS makes no changes to current accounting but does add required disclosure regarding the date through which the Company has evaluated subsequent events and whether that evaluation date is the date of financial statement issuance or the date the financial statements were available to be issued. This Statement is effective for interim and annual periods ending after June 15, 2009.

In June 2009, the FASB issued FAS No.167, Amendments to FASB Interpretation No. 46(R). This FAS changes the approach used to determine the primary beneficiary of a variable interest entity, requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity, amends certain guidance in Interpretation 46(R) for determining whether an entity is a variable interest entity, and adds as a reconsideration event any change in facts and circumstances where the holders of the equity investment at risk, as a group, lose the power to direct the activities of the entity that most significantly impact the entity s economic performance. In addition, this Statement amends Interpretation 46(R) to require enhanced disclosures regarding an enterprise s involvement in a variable interest entity. This FAS is effective for the Company beginning January 1, 2010. The adoption of this FAS is not expected to have a material impact on the Company s financial statements

In June 2009, the FASB issued FAS No.168, The FASB Accounting Standards Codification™ and the Hierarchy of Generally Accepted Accounting Principles - a replacement of FASB Statement No. 162. This FAS establishes the FASB Accounting Standards Codification as the source of authoritative U.S. generally accepted accounting standards (GAAP) and, once in effect, will supersede FAS No. 162. This FAS is effective for financial statements issued for interim and annual periods ending after September 15, 2009. Adoption of this FAS will not have a material effect on the Company s financial statements.

Note 12: Financial Segment Information

Sonoco reports its results in three segments, Consumer Packaging, Tubes and Cores/Paper and Packaging Services. The remaining operations are reported as All Other Sonoco.

The Consumer Packaging segment includes the following products: round and shaped rigid packaging (both composite and plastic); printed flexible packaging; and metal and peelable membrane ends and closures.

The Tubes and Cores/Paper segment includes the following products: high-performance paper and composite paperboard tubes and cores; fiber-based construction tubes and forms; pallet components; recycled paperboard, linerboard, recovered paper and other recycled materials.

The Packaging Services segment provides the following products and services: designing, manufacturing, assembling, packing and distributing temporary, semipermanent and permanent point-of-purchase displays; brand artwork management; and supply chain management services, including contract packing, fulfillment and scalable service centers.

All Other Sonoco represents the Company s businesses that do not meet the aggregation criteria outlined in Statement of Financial Accounting Standards No. 131, Disclosures about Segments of an Enterprise and Related Information, and therefore are not included in any of the above reportable segments. All Other Sonoco includes the following products: wooden, metal and composite wire and cable reels; molded and extruded plastics; custom-designed protective packaging; and paper amenities such as coasters and glass covers.

The following table sets forth net sales, intersegment sales and operating profit for the Company s three reportable segments and All Other Sonoco. Operating profit at the segment level is defined as Income before interest and income taxes on the Company s Condensed Consolidated Statements of Income, adjusted for restructuring/asset impairment charges, which are not allocated to the reporting segments.

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FINANCIAL SEGMENT INFORMATION

	Three Months Ended		Six Months Ended	
	June 28, 2009	June 29, 2008	June 28, 2009	June 29, 2008
Net Sales:				
Consumer Packaging	$ 372,770	$ 398,160	$ 724,704	$ 785,530
Tubes and Cores/Paper	323,391	455,417	611,731	891,604
Packaging Services	98,531	138,095	194,366	262,526
All Other Sonoco	69,539	94,895	134,059	184,903
Consolidated	$ 864,231	$ 1,086,567	$ 1,664,860	$ 2,124,563
Intersegment Sales:				
Consumer Packaging	$ 593	$ 777	$ 1,098	$ 1,169
Tubes and Cores/Paper	18,342	25,651	36,693	50,156
Packaging Services	183		262	91
All Other Sonoco	8,694	10,576	17,405	21,805
Consolidated	$ 27,812	$ 37,004	$ 55,458	$ 73,221
Income Before Income Taxes:				
Operating Profit				
Consumer Packaging	$ 38,906	$ 32,490	$ 78,303	$ 68,767
Tubes and Cores/Paper	20,239	40,045	26,985	74,609
Packaging Services	1,144	8,892	1,779	14,871
All Other Sonoco	7,406	12,353	12,542	23,786
Restructuring/Asset impairment charges	(10,386)	(10,770)	(17,596)	(72,308)
Interest, net	(10,071)	(12,097)	(19,702)	(25,325)
Consolidated	$ 47,238	$ 70,913	$ 82,311	$ 84,400

Note 13: Commitments and Contingencies

The Company is a party to various legal proceedings incidental to its business and is subject to a variety of environmental and pollution control laws and regulations in all jurisdictions in which it operates. The Company is also currently a defendant in a purported class action by persons who bought Company stock between February 7, 2007 and September 18, 2007. That suit alleges that the market price of the stock had been inflated by allegedly false and misleading earnings projections published by the Company. As is the case with other companies in similar industries, the Company faces exposure from actual or potential claims and legal proceedings. Some of these exposures have the potential to be material. Information with respect to these and other exposures appears in Part I Item 3 Legal Proceedings and Part II Item 8 Financial Statements and Supplementary Data (Note 15 Commitments and Contingencies) in the Company s Annual Report on Form 10-K for the year ended December 31, 2008, and in Part II Item 1 Legal Proceedings of this report. The Company cannot currently estimate the final outcome of many of the items described or the ultimate amount of potential losses.

Pursuant to Statement of Financial Accounting Standards No. 5, Accounting for Contingencies, accruals for estimated losses are recorded at the time information becomes available indicating that losses are probable and that the amounts are reasonably estimable. Amounts so accrued are not discounted. While the ultimate liabilities relating to claims and proceedings may be significant to profitability in the period recognized, it is management s opinion that such liabilities, when finally determined, will not have an adverse material effect on Sonoco s consolidated financial position or liquidity.

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Environmental Matters

During the fourth quarter of 2005, the U. S. Environmental Protection Agency (EPA) notified U.S. Paper Mills Corp. (U.S. Mills), a wholly owned subsidiary of the Company, that U.S. Mills and NCR Corporation (NCR), an unrelated party, would be jointly held responsible to undertake a program to remove and dispose of certain PCB-contaminated sediments at a particular site on the lower Fox River in Wisconsin (the Site) which is now labeled by the EPA as Phase 1. U.S. Mills and NCR reached an agreement between themselves that each would fund 50% of the costs of remediation. The Company has expensed a total of $17,650 for its estimated share of the total cleanup cost. Of the total expensed, $12,500 was recorded in 2005, and $5,150 was recorded in 2007. Through June 28, 2009, a total of $14,436 has been spent on remediation of the Site, including a settlement with a contractor who had claimed additional compensation. The Company currently estimates its share of the remaining cost of completing the Site project to be between $1,900 and $4,900. The remaining accrual of $3,214 represents the Company s estimate of what it is likely to pay to complete the Site project. However, the actual costs associated with cleanup of the Site are dependent upon many factors and it is reasonably possible that remediation costs could be higher than the current estimate of project costs. The Company acquired U.S. Mills in 2001, and the alleged contamination predates the acquisition.

In February 2007, the EPA and Wisconsin Department of Natural Resources (WDNR) issued a general notice of potential liability under the Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) and a request to participate in remedial action implementation negotiations relating to a stretch of the lower Fox River, including the bay at Green Bay, (Operating Units 2 5) to eight potentially responsible parties, including U.S. Mills. Operating Units 2 5 include but also comprise a vastly larger area than the Site. Although it has not accepted any liability, U.S. Mills is reviewing this information and discussing possible remediation scenarios, and the possible allocation of responsibility therefor, with other potentially responsible parties. On April 9, 2007, U.S. Mills, in conjunction with other potentially responsible parties, presented to the EPA and the WDNR a proposed schedule to mediate the allocation issues among eight potentially responsible parties, including U.S. Mills. Non-binding mediation began in May 2007 and continued as bilateral/multilateral negotiations until mid 2008. To date, no agreement among the parties has occurred.

On November 13, 2007, EPA issued a unilateral Administrative Order for Remedial Action pursuant to Section 106 of CERCLA. The order requires U.S. Mills and the seven other respondents to jointly take various actions to clean up Operating Units 2 5. The order establishes two phases of work. The first phase consists of planning and design work as well as preparation for dredging and other remediation work and initially was required to be completed by December 31, 2008. The second phase consists primarily of dredging and disposing of contaminated sediments and capping of the dredged and less contaminated areas of the river bottom. The second phase is required to begin in 2009 and is expected to continue for several years. The order also provides for a $32.5 per day penalty for failure by a respondent to comply with its terms as well as exposing a non-complying respondent to potential treble damages. Although U.S. Mills has reserved its rights to contest liability for any portion of the work, it is cooperating with the other respondents to comply with the first phase of the order, although its financial contribution will likely be determined by the lawsuit commenced in June 2008.

On June 12, 2008, NCR and Appleton Papers, Inc., as plaintiffs, commenced a lawsuit against U.S. Mills, as one of a number of defendants, seeking a declaratory judgment allocating among all the parties the costs and damages associated with the pollution and cleanup of the Lower Fox River. The suit also seeks damages from the defendants for amounts already spent by the plaintiffs, including natural resource damages, and future amounts to be spent by all parties with regard to the pollution and cleanup of the Lower Fox River. The Company believes that this suit will have a minimal, if any, impact on the total of the potential remediation costs associated with Operating Units 2 5.

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SONOCO PRODUCTS COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Dollars in thousands except per share data)
(unaudited)

As of June 28, 2009, U.S. Mills had accrued a total of $60,825 for potential liabilities associated with the Fox River contamination (not including amounts accrued for remediation at the Site). In two separate actions during 2008, U.S. Mills increased its reserve for all Fox River related liabilities (other than the Site) from $20,000 to $60,825. Accordingly, U.S. Mills recognized additional pre-tax charges of $40,825 in 2008 for such potential liabilities. Also during 2008, settlements totaling $40,825 were reached on certain of the insurance policies covering the Fox River contamination. The recognition of these insurance settlements offset the impact to earnings of the additional charges in 2008. Through June 28, 2009, a total of $1,419, primarily legal fees, has been spent against this reserve. Although the Company lacks a reasonable basis for identifying any amount within the range of possible loss as a better estimate than any other amount, as has previously been disclosed, the upper end of the range may exceed the net worth of U.S. Mills. However, because the discharges of hazardous materials into the environment occurred before the Company acquired U.S. Mills, and U.S. Mills has been operated as a separate subsidiary of the Company, the Company does not believe that it bears financial responsibility for these legacy environmental liabilities of U.S. Mills. Therefore, the Company continues to believe that the maximum additional exposure to its consolidated financial position is limited to the equity position of U.S. Mills, which was approximately $80,000 at June 28, 2009.

The Company has been named as a potentially responsible party at several other environmentally contaminated sites. All of the sites are also the responsibility of other parties. The potential remediation liabilities are shared with such other parties, and, in most cases, the Company s share, if any, cannot be reasonably estimated at the current time.

As of June 28, 2009 and December 31, 2008, the Company (and its subsidiaries) had accrued $65,606 and $70,542, respectively, related to environmental contingencies. Of these, a total of $62,620 and $67,411 relate to U.S. Mills at June 28, 2009 and December 31, 2008, respectively. These accruals are included in Accrued expenses and other on the Company s Condensed Consolidated Balance Sheets. As discussed above, U.S. Mills also recognized a $40,825 benefit from settlements reached on certain insurance policies covering the Fox River contamination. U.S Mills received all of the cash proceeds from these settlements in 2008. U.S. Mills two remaining insurance carriers are in liquidation. It is possible that U.S. Mills may recover from these carriers a small portion of the costs it ultimately incurs. U.S. Mills may also be able to reallocate some of the costs it incurs among other parties. There can be no assurance that such claims for recovery would be successful and no amounts have been recognized in the consolidated financial statements of the Company for such potential recovery or reallocation.

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Report of Independent Registered Public Accounting Firm

To the Shareholders and Directors of Sonoco Products Company:

We have reviewed the accompanying condensed consolidated balance sheet of Sonoco Products Company as of June 28, 2009, and the related condensed consolidated statements of income for the three- and six-month periods ended June 28, 2009 and June 29, 2008 and the condensed consolidated statements of cash flows for each of the six-month periods ended June 28, 2009 and June 29, 2008. These interim financial statements are the responsibility of the Company s management.

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

Based on our review, we are not aware of any material modifications that should be made to the accompanying condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2008, and the related consolidated statements of income, shareholders equity and of cash flows for the year then ended (not presented herein), and in our report dated February 27, 2009, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2008, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/PricewaterhouseCoopers LLP

Charlotte, North Carolina

July 28, 2009

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SONOCO PRODUCTS COMPANY

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations.

Statements included in this report that are not historical in nature, are intended to be, and are hereby identified as forward-looking statements for purposes of the safe harbor provided by Section 21E of the Securities Exchange Act of 1934, as amended. The words estimate, project, intend, expect, believe, consider, plan, anticipate, obj guidance, outlook, forecasts, future, will, would and similar expressions identify forward-looking statements. Forward-looking statements include, but are not limited to, statements regarding offsetting high raw material costs; improved productivity and cost containment; adequacy of income tax provisions; refinancing of debt; adequacy of cash flows; anticipated amounts and uses of cash flows; effects of acquisitions and dispositions; adequacy of provisions for environmental liabilities; financial strategies and the results expected from them; continued payments of dividends; stock repurchases; producing improvements in earnings, financial results for future periods, and creation of long-term value for shareholders. Such forward-looking statements are based on current expectations, estimates and projections about our industry, management s beliefs and certain assumptions made by management. Such information includes, without limitation, discussions as to guidance and other estimates, expectations, beliefs, plans, strategies and objectives concerning our future financial and operating performance. These statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to predict. Therefore, actual results may differ materially from those expressed or forecasted in such forward-looking statements. The risks and uncertainties include, without limitation:

Availability and pricing of raw materials;

Success of new product development and introduction;

Ability to maintain or increase productivity levels and contain or reduce costs;

International, national and local economic and market conditions;

Availability of credit to us, our customers and/or our suppliers in needed amounts and/or on reasonable terms;

Fluctuations in obligations and earnings of pension and postretirement benefit plans;

Ability to maintain market share;

Pricing pressures and demand for products;

Strength of our paperboard-based tubes and cores and composite can operations;

Anticipated results of restructuring activities;

Resolution of income tax contingencies;

Ability to successfully integrate newly acquired businesses into the Company s operations;

Rate of growth in foreign markets;

Foreign currency, interest rate and commodity price risk and the effectiveness of related hedges;

Actions of government agencies and changes in laws and regulations affecting the Company;

Liability for and anticipated costs of environmental remediation actions;

Ability to weather the current economic downturn;

Loss of consumer or investor confidence; and

Economic disruptions resulting from terrorist activities.

The Company undertakes no obligation to publicly update or revise forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks, uncertainties and assumptions, the forward-looking events discussed in this report might not occur.

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SONOCO PRODUCTS COMPANY

COMPANY OVERVIEW

Sonoco is a leading manufacturer of industrial and consumer packaging products and provider of packaging services, with more than 300 locations in 35 countries.

Sonoco competes in multiple product categories with the majority of its operations organized and reported in three segments: Consumer Packaging, Tubes and Cores/Paper and Packaging Services. Various other operations are reported as All Other Sonoco. The majority of the Company s revenues are from products and services sold to consumer and industrial products companies for use in the packaging of their products for sale or shipment. The Company also manufactures paperboard, primarily from recycled materials, for both internal use and open market sale. Each of the Company s operating units has its own sales staff and maintains direct sales relationships with its customers.

Second Quarter 2009 Compared with Second Quarter 2008

RESULTS OF OPERATIONS

The following discussion provides a review of results for the three months ended June 28, 2009 versus the three months ended June 29, 2008.

OVERVIEW

Sales for the second quarter were 21% below last year s levels primarily due to lower volumes companywide, but most significantly in the industrial-focused businesses. Although lower volumes and a significant increase in pension costs led to reduced overall gross profit, gross profit margins for the second quarter increased to 18.3% compared to last year s 17.9%. Margins were favorably impacted by a positive selling price/material cost relationship, as well as cost containment actions and productivity initiatives. Net income attributable to Sonoco for the second quarter of 2009 was $33.6 million compared to $58.0 million reported for the same period of 2008. 2009 earnings include $7.0 million of higher after-tax pension expenses as well as after-tax restructuring charges of $7.3 million. Second quarter 2008 results were impacted by after-tax restructuring charges of $4.6 million.

As stated above, the Company experienced significant volume declines as a result of global economic conditions, primarily in the Tubes and Cores/Paper and Packaging Services segments. In order to manage the impact of these declines, the Company continues to control its costs by implementing additional initiatives aimed at simplifying its business structure, scaling itself for profitable growth, improving innovation and creating sustainable operating efficiencies. Given the current economic environment, it is uncertain when and at what rate volume will begin to significantly recover. However, management believes the Company s strong cash flow, liquidity position and competitive cost structure leave it well positioned to manage any further economic weakness and capitalize on any improvement.

OPERATING REVENUE

Net sales for the second quarter of 2009 were $864 million, compared to $1,086 million for the second quarter of 2008, a decrease of $222
million.

The components of the sales change were:

($ in millions)	
Volume/Mix	$(134)
Foreign Currency Translation	(68)
Selling Prices	(19)
Other	(1)
Total Sales Decrease	$(222)

Volume/mix accounted for a 12% decrease in sales from 2008 levels as each of the Company s reporting segments experienced volume declines across nearly every geographic region, with the greatest volume declines occurring in businesses serving industrial markets, which tend to be more economically sensitive. Although average selling prices were higher in several businesses within the Consumer Packaging segment, they were more than offset by significantly lower selling prices within the Tubes and Cores/Paper segment. The higher selling prices in the Consumer Packaging segment were initiated in response to higher metal and converting costs while the lower selling prices in the Tubes and

SONOCO PRODUCTS COMPANY

Cores/Paper segment were in response to significantly lower recovered paper prices. The strong dollar, relative to last year s levels, also contributed significantly to the sales decline.

COSTS AND EXPENSES

Cost of sales in the second quarter of 2009 was lower year over year primarily due to the significant declines in volume discussed above. Last year s decline in the value of plan assets has resulted in a significant increase in current year pension and retirement plan costs. In total, these costs were up approximately $11 million in the second quarter, most of which is reflected in cost of sales. Lower recovered paper prices had the corresponding effect of lowering costs in our converted paper operations. However, other cost components, including metal, energy, labor and other converting costs, experienced price increases over last year s second quarter. Productivity initiatives and cost containment activities were able offset some of the above cost increases. In an attempt to partially offset the negative impact of lower volume and rising costs, the Company initiated several contingency actions, including freezing salaries, temporarily suspending 401(k) matches and restricting discretionary spending.

Selling, general and administrative costs are down primarily due to cost containment activities, lower management incentive expenses, and the impact of foreign currency translation. These reductions were partially offset by higher pension costs.

Restructuring and related asset impairment charges totaled $10.4 million and $10.8 million for the second quarters of 2009 and 2008, respectively. Additional information regarding restructuring and impairment actions is provided in Note 3 to the Consolidated Financial Statements.

Net interest expense for the second quarter of 2009 decreased to $10.1 million, compared with $12.1 million during the same period in 2008. The decrease was due to lower debt levels and lower interest rates.

This year s second quarter effective tax rate of 31.9% was significantly higher than the 26.0% rate recorded in the 2008 quarter. The lower rate last year was primarily a result of non-recurring tax benefits recognized in 2008 related to a tax law change in Italy.

REPORTABLE SEGMENTS

The following table recaps net sales for the second quarter of 2009 and 2008 ($ in thousands):

	Three Months Ended	
	June 28, 2009	June 29, 2008
Net Sales:		
Consumer Packaging	$ 372,770	$ 398,160
Tubes and Cores/ Paper	323,391	455,417
Packaging Services	98,531	138,095
All Other Sonoco	69,539	94,895
Consolidated	$ 864,231	$ 1,086,567

Consolidated operating profits, also referred to as Income before income taxes on the Condensed Consolidated Statements of Income, are comprised of the following ($ in thousands):

	Three Months Ended	
	June 28, 2009	June 29, 2008
Income Before Income Taxes:		
Segment Operating Profit		
Consumer Packaging	$ 38,906	$ 32,490
Tubes and Cores/ Paper	20,239	40,045
Packaging Services	1,144	8,892

All Other Sonoco	7,406	12,353
Restructuring/Asset Impairment Charges	(10,386)	(10,770)
Interest, net	(10,071)	(12,097)
Consolidated	$ 47,238	$ 70,913

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Segment results are used by Company management to evaluate segment performance and do not include restructuring, impairment and net interest charges. Accordingly, the term segment operating profit is defined as the segment s portion of Income before income taxes excluding those items. All other general corporate expenses have been allocated as operating costs to each of the Company s reportable segments and All Other Sonoco.

Consumer Packaging

Sonoco s Consumer Packaging segment includes the following products: round and shaped rigid packaging (both composite and plastic); printed flexible packaging; and metal and peelable membrane ends and closures.

Sales in the Consumer Packaging segment during the second quarter of 2009 decreased $25 million, or 6%, compared with the second quarter of 2008. This was primarily due to an overall volume decline of 8%. In addition, an unfavorable $12 million effect of foreign currency translation offset a large part of the benefit from selling price increases.

Segment operating profit was up 20% in the second quarter as selling price increases were implemented to offset rising metal and other costs, the negative impacts of which were not fully felt until later in the second quarter. The delay in the cost of sales impact of metal cost increases, along with productivity improvements and lower resin and film costs, were the major contributors to improved operating profit. Higher pension costs partially offset this favorable price/cost relationship.

Tubes and Cores/Paper

The Tubes and Cores/Paper segment includes the following products: high-performance paper and composite paperboard tubes and cores; fiber-based construction tubes and forms; recycled paperboard, linerboard, recovered paper and other recycled materials.

Second quarter 2009 sales for the segment dropped $132 million, or 29%, compared with the same period in 2008, due to a 12% decline in volume resulting from significantly lower global demand and a $39 million unfavorable effect from foreign currency translation. Selling prices declined year over year, particularly those associated with recovered paper.

Segment operating profit fell nearly 50% from last year s levels due to lower volume and higher pension costs. Lower fixed costs resulting from restructuring and other cost containment actions offset some of the impact. The benefit of lower recovered paper costs was nearly completely offset by reduced selling prices for those products associated with recovered paper.

Packaging Services

The Packaging Services segment includes the following products and services: designing, manufacturing, assembling, packing and distributing temporary, semipermanent and permanent point-of-purchase displays; brand artwork management; and supply chain management services, including contract packing, fulfillment and scalable service centers.

Second quarter 2009 sales for the segment decreased 29%, or $40 million, from the second quarter of 2008. The decrease was due to lower volume and a $15 million unfavorable effect of foreign currency translation.

Segment operating profit declined 87% in the second quarter, compared with the same period in 2008. Lower volume in point-of-purchase displays, fulfillment and contract packing were the primary reasons for the steep decline in earnings.

All Other Sonoco

All Other Sonoco includes businesses that are not aggregated in a reportable segment and includes the following products: wooden, metal and composite wire and cable reels, molded and extruded plastics, custom-designed protective packaging and paper amenities such as coasters and glass covers.

Second quarter 2009 sales in All Other Sonoco dropped nearly 27% from the same period in 2008. Continued weak volumes in wire and cable reels, protective packaging and molded plastics was the primary reason for the decline, although lower prices and foreign currency translation also contributed to the lower sales.

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Operating profit was down 40% from last year s second quarter due to lower volumes and higher pension costs, partially offset by productivity improvements and lower fixed costs.

Six Months Ended June 28, 2009 Compared with Six Months Ended June 29, 2008

RESULTS OF OPERATIONS

The following discussion provides a review of results for the six months ended June 28, 2009 versus the six months ended June 29, 2008.

OVERVIEW

Results for the first half of 2009 were affected by many of the same factors impacting the second quarter. Lower volumes companywide drove sales 22% below last year s levels, most significantly in the industrial-focused businesses. These lower volumes primarily resulted from lower activity for the Company s customers in served markets, and do not, in management s opinion, represent any significant loss of market share. Despite these volume declines and a $26 million increase in pension costs, of which approximately 75% is included in cost of sales, gross profit margins increased slightly to 18.0% from 17.9% in 2008. Net income attributable to Sonoco for the first half of 2009 was $56.7 million compared to $71.2 million reported for the same period of 2008. 2009 earnings include after-tax restructuring charges of $13.3 million. First half 2008 results were impacted by a $31.0 million after-tax non-cash impairment charge for the Company s remaining financial interest related to the 2003 sale of its high density film business as well as after-tax restructuring charges of $14.4 million.

OPERATING REVENUE

Net sales for the first six months of 2009 were $1,665 million, compared to $2,125 million for the first half of 2008, a decrease of $460 million.

The components of the sales change were:

($ in millions)	
Volume/Mix	$(292)
Foreign Currency Translation	(134)
Selling Prices	(27)
Other	(7)
Total Sales Decrease	$(460)

As discussed earlier, volume/mix and the impact of unfavorable foreign exchange translation were the major drivers in the decrease in sales from 2008 levels. Lower recovered paper costs were partially offset by higher average selling prices in several businesses initiated in response to higher metal and converting costs.

COSTS AND EXPENSES

Restructuring related charges totaled $17.6 million and $29.7 million for the first six months of 2009 and 2008, respectively. In addition, the first six months of 2008 included a non-cash impairment charge of $42.7 million for the Company s remaining financial interest related to the 2003 sale of its high density film business. Additional information regarding restructuring actions is provided in Note 3 to the Consolidated Financial Statements. None of these charges are allocated to the reporting segments.

Volume declines were the largest driver of the year over year decrease in cost of sales for the first six months, while total pension and retirement plan costs increased approximately $26 million, of which approximately 75% is included in cost of sales. As noted above, gross profit margin improved slightly as the benefits of restructuring actions taken over the last 12 months, cost containment activities and productivity improvements were able to partially offset the negative impacts of lower volume and higher pension costs.

Selling, general and administrative costs were lower than 2008 levels primarily due to aggressive cost containment activities, lower management incentive expenses and the impact of foreign currency translation. These reductions were partially offset by higher pension costs.

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Net interest expense for the first half of 2009 decreased to $19.7 million, compared with $25.3 million during the same period in 2008. The decrease was due to lower debt levels and lower interest rates.

The effective tax rate in the first six months of 2009 was 32.2%, versus 29.5% recorded in 2008. The lower rate last year was primarily a result of non-recurring tax benefits recognized in 2008 related to a tax law change in Italy.

REPORTABLE SEGMENTS

The following table recaps net sales for the first six months of 2009 and 2008 ($ in thousands):

	Six Months Ended	
	June 28, 2009	June 29, 2008
Net Sales:		
Consumer Packaging	$ 724,704	$ 785,530
Tubes and Cores/ Paper	611,731	891,604
Packaging Services	194,366	262,526
All Other Sonoco	134,059	184,903
Consolidated	$ 1,664,860	$ 2,124,563

Consolidated operating profits, also referred to as Income before income taxes on the Condensed Consolidated Statements of Income, are comprised of the following ($ in thousands):

	Six Months Ended	
	June 28, 2009	June 29, 2008
Income Before Income Taxes:		
Segment Operating Profit		
Consumer Packaging	$ 78,303	$ 68,767
Tubes and Cores/ Paper	26,985	74,609
Packaging Services	1,779	14,871
All Other Sonoco	12,542	23,786
Restructuring/Asset Impairment Charges	(17,596)	(72,308)
Interest, net	(19,702)	(25,325)
Consolidated	$ 82,311	$ 84,400

Consumer Packaging

Sales in the Consumer Packaging segment during the first six months of 2009 decreased $61 million, or 8%, compared with the first half of 2008, as a result of a 9% decline in volume and the unfavorable impact of foreign exchange. Increased selling prices partially offset these negative factors.

A 14% increase in segment operating profits was a result of a favorable price/cost relationship and productivity improvements that more than offset the impact of volume declines and higher pension costs.

Tubes and Cores/Paper

First half 2009 sales for the segment dropped $280 million, or 31%, compared with the same period in 2008. A volume decline of approximately 15% was the most significant driver, but the unfavorable effect of foreign currency translation also contributed notably. In addition, recovered paper prices have been lower than 2008 levels throughout the first six months of 2009.

Segment operating profit fell nearly 64% during the first half of 2009, compared to last year s levels. As has been the case throughout 2009, lower volume, higher pension costs and the unfavorable impact of foreign currency translation were the major factors in the decline. The benefits of several plant shutdowns along with other fixed cost control measures and a favorable price/cost relationship helped mitigate the impact of the volume shortfall.

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Packaging Services

First half 2009 sales for the segment decreased 27% or $68 million from 2008 levels. This decrease was due to significantly lower volume and the unfavorable effect of foreign currency translation.

Compared to the same period in 2008, segment operating profit declined 88% in the first half of 2009. Lower volume was the most significant factor in this decline, but was somewhat offset by the benefit of several fixed cost reduction initiatives.

All Other Sonoco

First half 2009 sales in All Other Sonoco dropped 27% from the same period in 2008. Continued weak volumes in wire and cable reels, protective packaging and molded plastics were the primary reasons for the decline.

Operating profit was down 47% from last year s first half due to lower volumes and higher pension costs, partially offset by productivity improvements.

Financial Position, Liquidity and Capital Resources

The Company s financial position remained strong during the second quarter of 2009. Cash flows from operations totaled $181.9 million in the first six months of 2009, compared with $143.9 million in the same period last year. Improvements in working capital, primarily inventory and accounts payable, accounted for the majority of the year-over-year increase in operating cash flow. Cash flows for the second half of 2009 are expected to remain strong, but lower than the levels generated in the first half of the year.

During the first six months of 2009, the Company utilized cash from operations to fund capital expenditures of $57.4 million, pay dividends of $53.9 million, and reduce outstanding debt by a net $43.9 million to $645.9 million at June 28, 2009. Cash on hand increased from $101.7 million at December 31, 2008, to $111.5 million at June 28, 2009.

During the latter part of 2008, the Internal Revenue Service issued a temporary rule extending to 60 days the period that U.S. Corporations may borrow funds from foreign subsidiaries without unfavorable tax consequences. The Company utilized this rule during the final two months of 2008 to access approximately $72 million of offshore cash on hand, which was used to reduce outstanding commercial paper. These short-term lending arrangements were settled early in 2009. In June, the Company again utilized this rule to access approximately $49 million of offshore cash on hand, which was used to reduce outstanding commercial paper. This short-term lending arrangement will be settled during the third quarter of 2009, resulting in equivalent increases in commercial paper and cash on hand. Depending on its immediate offshore cash needs, the Company may choose to again access such funds in the future as allowed by the temporary rule. Commercial paper, a component of the Company s long-term debt, had a balance of $54.0 million at June 28, 2009.

Certain of the Company s debt agreements impose restrictions with respect to the maintenance of financial ratios and the disposition of assets. The most restrictive covenant currently requires the Company to maintain a minimum level of net worth, as defined. As of June 28, 2009, the Company s defined net worth was approximately $412 million above the minimum level required under this covenant.

Funding of the Company s U.S. qualified defined benefit pension plans, although not required in 2009, is currently expected to be approximately $60 million in 2010. However, if actual returns on plan assets in 2009 are lower than the expected rate of return of 8.5%, the required funding could be higher. Conversely, if actual returns are higher than the expected rate, the required funding could be lower.

Certain assets and liabilities are reported in the Company s financial statements at fair value, the fluctuation of which can impact the Company s financial position and results of operations. Items reported by the Company on a recurring basis at fair value include derivative contracts and pension and deferred compensation related assets. The valuation of the vast majority of these items is based either on quoted prices in active and accessible markets or on other observable inputs.

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At June 28, 2009, the Company had commodity contracts outstanding to fix the cost of a portion of anticipated raw materials and natural gas purchases. The total net fair market value of these instruments was an unfavorable position of $17.1 million at June 28, 2009, and an unfavorable position of $20.5 million at December 31, 2008. Natural gas and aluminum contracts covering an equivalent of 6.5 million MMBtu and 5,228 metric tons, respectively, were outstanding at June 28, 2009. Additionally, the Company had various currency contracts outstanding to fix the exchange rate on certain anticipated foreign currency cash flows. The total market value of these instruments was a net favorable position of $0.6 million at June 28, 2009 compared with a net unfavorable position of $0.7 million at December 31, 2008. These contracts qualify as cash flow hedges under FAS 133 and mature within twelve months of their respective reporting date.

In addition, at June 28, 2009, the Company had various currency contracts outstanding to fix the exchange rate on certain foreign currency assets and liabilities. Although placed as an economic hedge, the Company has chosen not to apply hedge accounting to these contracts. The fair value of these currency contracts, all of which mature within twelve months, was a net favorable position of $0.2 million at the end of the quarter and $6.6 million at December 31, 2008.

Restructuring and Impairment

Information regarding restructuring charges and restructuring-related asset impairment charges is provided in Note 3 to the Company s Condensed Consolidated Financial Statements.

New Accounting Pronouncements

Information regarding new accounting pronouncements is provided in Note 11 to the Company s Condensed Consolidated Financial Statements.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

Information about the Company s exposure to market risk is discussed under Part I, Item 2 in this report and was disclosed in its Annual Report on Form 10-K for the year ended December 31, 2008, which was filed with the Securities and Exchange Commission on February 27, 2009. There have been no other material quantitative or qualitative changes in market risk exposure since the date of that filing.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

Under the supervision, and with the participation, of our management, including our principal executive officer and principal financial officer, we conducted an evaluation pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934 of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934). Based on this evaluation, our principal executive officer and principal financial officer concluded that such controls and procedures, as of the end of the period covered by this Quarterly Report on Form 10-Q, were effective.

Changes in Internal Controls

During the second quarter of 2009, the Company implemented a new general ledger and related shared services modules (accounts receivable, accounts payable and fixed assets) at the majority of its operations in the United States and Canada. The underlying processes and internal controls were not changed; therefore, we believe the Company s internal control over financial reporting is, and will continue to be, effective under the new systems. There have been no other changes in the Company s internal control over financial reporting (as defined in Rule 13a-15(f) under the Securities Exchange Act of 1934) during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1. Legal Proceedings.

Information with respect to legal proceedings and other exposures appears in Part I Item 3 Legal Proceedings and Part II Item 8 Financial Statements and Supplementary Data (Note 15 - Commitments and Contingencies) in the Company s Annual Report on Form 10-K for the year ended December 31, 2008, and in Part I Item 1 Financial Statements (Note 13 Commitments and Contingencies) of this report. In April 2006, the United States and the State of Wisconsin (plaintiffs) sued U.S. Paper Mills Corp. (U.S. Mills), a wholly owned subsidiary of the Company, and NCR Corporation (NCR), an unrelated company, to recover certain costs incurred for response activities undertaken regarding the release and threatened release of hazardous substances in specific areas of elevated concentrations of polychlorinated biphenyls (PCBs) in sediments in the Lower Fox River and Green Bay in northeastern Wisconsin (hereinafter the Site). Pursuant to a Consent Decree agreed to by NCR and U.S. Mills as a consequence of the litigation, the Site is to be cleaned up on an expedited basis and NCR and U.S. Mills started removing contaminated sediment in May 2007. The remediation involves removal of sediment from the riverbed, dewatering of the sediment and storage at an offsite landfill. U.S. Mills and NCR reached an agreement between themselves that each would fund 50% of the costs of remediation, which the Company currently estimates to be between $32.7 million and $38.7 million for the project as a whole. The actual costs associated with cleanup of this particular site are dependent upon many factors and it is reasonably possible that remediation costs could be higher than the current estimate of project costs. Under the terms of the agreement, the parties reserved their rights to make claims against each other, as well as third parties, to reallocate the costs of remediating the Site. Accordingly, the Company s ultimate share of the liability for remediating the Site could be greater or less than 50% of the total cost.

In addition to the Site discussed above, as previously disclosed in its Annual Report on Form 10-K for the year ended December 31, 2008, U.S. Mills faces additional exposure related to potential natural resource damage and environmental remediation costs for a larger stretch of the lower Fox River, including the bay at Green Bay, which includes the Site discussed above (Operating Units 2 5). On April 9, 2007, U.S. Mills, in conjunction with other potentially responsible parties (PRPs), presented to the U.S. Environmental Protection Agency and the Wisconsin Department of Natural Resources a proposed schedule to mediate the allocation issues among eight PRPs, including U.S. Mills. Non-binding mediation began in May 2007 and continued as bilateral/multilateral negotiations although no agreement among the parties occurred. On June 12, 2008, NCR and Appleton Papers, Inc., as plaintiffs, commenced suit in the United States District Court for the Eastern District of Wisconsin (No. 08-CV-0016-WCG) against U.S. Mills, as one of a number of defendants, seeking a declaratory judgment allocating among all the parties the costs and damages associated with the pollution and clean up of the Lower Fox River. The suit also seeks damages from the defendants for amounts already spent by the plaintiffs, including natural resource damages, and future amounts to be spent by all parties with regard to the pollution and cleanup of the Lower Fox River. The court has initially limited discovery to information regarding when each party knew, or should have known, that recycling NCR-brand carbonless paper would result in the discharge of PCBs to a water body and what action, if any, each party took to avoid the risk of further contamination. The court has set a trial date for those issues only for December 1, 2009. U.S. Mills plans to vigorously defend the suit.

As of June 28, 2009, U.S. Mills had accrued a total of $60.8 million for potential liabilities associated with the Fox River contamination (not including amounts accrued for remediation at the Site). In two separate actions during 2008, U.S. Mills increased its reserve for all Fox River related liabilities (other than the Site) from $20.0 million to $60.8 million. Accordingly, U.S. Mills recognized additional pre-tax charges of $40.8 million in 2008 for such potential liabilities. Also during 2008, settlements totaling $40.8 million were reached on certain of the insurance policies covering the Fox River contamination. The recognition of these insurance settlements effectively offset the impact to earnings of the additional charges in 2008. Although the Company lacks a reasonable basis for identifying any amount within the range of possible loss as a better estimate than any other amount, as has previously been disclosed, the upper end of the range may exceed the net worth of U.S. Mills. However, because the discharges of hazardous materials into the environment occurred before the Company acquired U.S. Mills, and U.S. Mills has been operated as a separate subsidiary of the Company, the Company does not believe that it bears financial responsibility for these legacy environmental liabilities of U.S. Mills. Therefore, the Company continues to believe that the maximum additional exposure to its consolidated financial position is limited to the equity position of U.S. Mills, which was approximately $80 million at June 28, 2009.

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SONOCO PRODUCTS COMPANY

On July 7, 2008, the Company was served with a complaint filed in the United States District Court for South Carolina by the City of Ann Arbor Employees Retirement System, individually and on behalf of others similarly situated. The suit purports to be a class action on behalf of those who purchased the Company s common stock between February 7, 2007 and September 18, 2007, except officers and directors of the Company. The complaint alleges that the Company issued press releases and made public statements during the class period that were materially false and misleading because the Company allegedly had no reasonable basis for the earnings projections contained in the press releases and statements, and that such information caused the market price of the Company s common stock to be artificially inflated. The complaint also names certain Company officers as defendants and seeks an unspecified amount of damages plus interest and attorneys fees. The Company believes that the claims are without merit and intends to vigorously defend itself against the suit.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

ISSUER PURCHASES OF EQUITY SECURITIES

Period	(a) Total Number of Shares Purchased[1]	(b) Average Price Paid per Share	(c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs[2]	(d) Maximum Number of Shares that May Yet be Purchased under the Plans or Programs[2]
3/30/09 5/03/09	1,812	$ 24.16		5,000,000
5/04/09 5/31/09				5,000,000
6/01/09 6/28/09				5,000,000
Total	1,812	$ 24.16		5,000,000

1 All of the share purchases in the second quarter of 2009 relate to shares withheld to satisfy employee tax withholding obligations in association with the exercise of performance-based stock awards, deferred compensation and

restricted stock. These shares were not repurchased as part of a publicly announced plan or program.

2 On April 19, 2006, the Company s Board of Directors authorized the repurchase of up to 5,000,000 shares of the Company s common stock. This authorization rescinded all previous existing authorizations and does not have a specific expiration date. No shares have been repurchased under this authorization during 2009. At June 28, 2009, a total of 5,000,000 shares remain available for repurchase.

Item 4. Submission of Matters to a Vote of Security Holders.

Incorporated by reference to Part II, Item 4 of the Company s Quarterly Report on Form 10-Q for the quarter ended March 29, 2009.

Item 6. Exhibits.

Exhibit 15	Letter re: unaudited interim financial information
Exhibit 31	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and 17 C.F.R. 240.13a-14(a)
Exhibit 32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and 17 C.F.R. 240.13a-14(b)

SONOCO PRODUCTS COMPANY

SIGNATURE

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.

SONOCO PRODUCTS COMPANY
(Registrant)

Date: July 28, 2009

By: /s/ Charles J. Hupfer
Charles J. Hupfer
Senior Vice President and Chief Financial Officer
(principal financial officer)

By: /s/ Barry L. Saunders
Barry L. Saunders
Vice President and Corporate Controller
(principal accounting officer)

SONOCO PRODUCTS COMPANY
EXHIBIT INDEX

Exhibit Number	Description
15	Letter re: unaudited interim financial information
31	Certifications of Chief Executive Officer and Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 and 17 C.F.R. 240.13a-14(a)
32	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 and 17 C.F.R. 240.13a-14(b)