FORM 10-K

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

(Mark One)

/X/ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (FEE REQUIRED)

For the fiscal year ended: December 31, 1998

or

/ / TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

For the transition period from __________ to __________

Commission File Number: 1-7677

LSB INDUSTRIES, INC.

(Exact Name of Registrant as Specified in its Charter)

Delaware	73-1015226
(State of Incorporation)	(I.R.S. Employer Identification No.)
16 South Pennsylvania Avenue Oklahoma City, Oklahoma	73107
(Address of Principal Executive Offices)	(Zip Code)

Registrant's Telephone Number, Including Area Code:

(405) 235-4546

Securities Registered Pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange On Which Registered
Common Stock, Par Value $.10	New York Stock Exchange
$3.25 Convertible Exchangeable Class C Preferred Stock, Series 2	New York Stock Exchange
Preferred Share Purchase Rights	New York Stock Exchange

(Facing Sheet Continued)

Securities Registered Pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the Registrant (1) has filed all reports required by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for the shorter period that the Registrant has had to file the reports), and (2) has been subject to the filing requirements for the past 90 days. YES X NO
______ _____.

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

As of February 28, 1999, the aggregate market value of the 7,650,412 shares of voting stock of the Registrant held by non-affiliates of the Company equaled approximately $22,951,236 based on the closing sales price for the Company's common stock as reported for that date on the New York Stock Exchange. That amount does not include the 1,463 shares of voting Convertible Non-Cumulative Preferred Stock (the "Non-Cumulative Preferred Stock") held by non-affiliates of the Company. An active trading market does not exist for the shares of Non-Cumulative Preferred Stock.

As of February 28, 1999, the Registrant had 11,866,486 shares of common stock outstanding (excluding 3,242,190 shares of common stock held as treasury stock).

TABLE OF CONTENTS

PART I

PART II

PART I

Item 1. BUSINESS

General

LSB Industries, Inc. (the "Company") was formed in 1968 as an Oklahoma corporation, and in 1977 became a Delaware corporation. The Company is a diversified holding company which is engaged, through its subsidiaries, in (i) the manufacture and sale of chemical products for the explosives, agricultural and industrial acids markets (the "Chemical Business"), (ii) the manufacture and sale of a broad range of hydronic fan coils and water source heat pumps as well as other products used in commercial and residential air conditioning systems (the "Climate Control Business"), and (iii) the manufacture or purchase and sale of certain automotive and industrial products, including automotive bearings and other automotive replacement parts (the "Automotive Products Business") and the purchase and sale of machine tools (the "Industrial Products Business").

As previously announced, the Company is continuing with its evaluation of the spin-off of the Automotive Products Business ("Automotive") to its shareholders as a dividend. The spin-off of Automotive will require, among other things, commitment to a formal plan, receipt by the Company from the Internal Revenue Service of a favorable ruling or an opinion of counsel confirming tax-free treatment, certain Securities and Exchange Commission filings, arrangement for lines of credit for Automotive, and LSB Board of Directors' approval. Subject to completion of the above conditions, management believes there is a strong likelihood that the spin-off will be completed during 1999. However, there are no assurances that the Company will spin-off Automotive.

Segment Information and Foreign and Domestic Operations and Export Sales

Schedules of the amounts of sales, operating profit and loss, and identifiable assets attributable to each of the Company's lines of business and of the amount of export sales of the Company in the aggregate and by major geographic area for each of the Company's last three fiscal years appear in Note 13 of the Notes to Consolidated Financial Statements included elsewhere in this report.

A discussion of any risks attendant as a result of a foreign operation or the importing of products from foreign countries appears below in the discussion of each of the Company's business segments.

Chemical Business

General

The Company's Chemical Business manufactures three principal product lines that are derived from anhydrous ammonia: (1) fertilizer grade ammonium nitrate for the agricultural industry, (2) explosive grade ammonium nitrate for the mining industry and (3) concentrated, blended and mixed nitric acid for industrial applications. In addition, the Company also produces sulfuric acid for commercial applications primarily in the paper industry. The Chemical Business' products are sold in niche markets where the

Company believes it can establish a position as a market leader. See "Special Note Regarding Forward-Looking Statements".

The Chemical Business' principal manufacturing facility is located in El Dorado, Arkansas ("El Dorado Facility"), and its other manufacturing facilities are located in Hallowell, Kansas, Wilmington, North Carolina, and four locations in Australia.

For each of the years 1998, 1997 and 1996, approximately 26% of the sales of the Chemical Business consisted of sales of fertilizer and related chemical products for agricultural purposes, which represented approximately 12%, 13% and 14% of the Company's consolidated sales for each respective year, and approximately 52%, 61% and 61% of the sales of the Chemical Business consisted of sales of ammonium nitrate and other chemical-based blasting products for the mining industry, which represented approximately 23%, 31% and 33% of the Company's 1998, 1997 and 1996 consolidated sales, respectively. The Chemical Business accounted for approximately 45%, 50% and 54% of the Company's 1998, 1997 and 1996 consolidated sales, respectively.

Agricultural Products

The Chemical Business produces ammonium nitrate, a nitrogen-based fertilizer, at the El Dorado Facility. In 1998, the Company sold approximately 143,000 tons of ammonium nitrate fertilizer to farmers, fertilizer dealers and distributors located primarily in the south central United States.

Ammonium nitrate is one of several forms of nitrogen-based fertilizers which include anhydrous ammonia and urea. Although, to some extent, the various forms of nitrogen-based fertilizers are interchangeable, each has its own characteristics which produce agronomic preferences among end users. Farmers decide which type of nitrogen-based fertilizer to apply based on the crop planted, soil and weather conditions, regional farming practices and relative nitrogen fertilizer prices.

The Chemical Business is a major manufacturer of fertilizer grade ammonium nitrate, which it markets primarily in Texas, Arkansas and the surrounding regions. This market, which is in close proximity to its El Dorado Facility, includes a high concentration of pasture land and row crops which favor ammonium nitrate over other nitrogen-based fertilizers. The Company has developed the leading market position in Texas by emphasizing high quality products, customer service and technical advice. Using a proprietary prilling process, the Company produces a high performance ammonium nitrate fertilizer that, because of its uniform size, is easier to apply than many competing nitrogen-based fertilizer products. The Company believes that its "E-2" brand ammonium nitrate fertilizer is recognized as a premium product within its primary market. In addition, the Company has developed long term relationships with end users through its network of 22 owned and operated wholesale and retail distribution centers.

In 1998, the Chemical Business has been adversely affected by the extreme drought conditions in the mid-south market during the primary fertilizer season, followed by excess wet conditions and floods in the fall season, resulting in substantially lower volume and lower sales prices for certain of its products sold in its agricultural markets. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Special Note Regarding Forward-Looking Statements".

Explosives

The Chemical Business manufactures low density ammonium nitrate-based explosives including bulk explosives used in surface mining. In addition, the Company manufactures and sells a branded line of packaged explosives used in construction, quarrying and other applications, particularly where controlled explosive charges are required. The Company's bulk explosives are marketed primarily through five Company-owned distribution centers, three of which are located in close proximity to the customers' surface mines in the coal producing states of Kentucky, Missouri, and West Virginia. Additionally, the Company, through its Australian subsidiary, manufactures and distributes bulk and packaged explosives in Australia. The Company emphasizes value-added customer services and specialized product applications for its bulk explosives. Most of the sales of bulk explosives are to customers who work closely with the Company's technical representatives in meeting their specific product needs. In addition, the Company sells bulk explosives to independent wholesalers and to other explosives companies. Packaged explosives are used for application requiring controlled explosive charges and typically command a premium price and produce higher margins. The Company believes its Slurry packaged explosive products are among the most widely recognized in the industry. Slurry packaged explosive products are sold nationally and internationally to other explosive companies and end-users.

The Company has received an offer in 1999, the terms of which it is presently negotiating with the company that made the offer, to sell the Australian subsidiary; however, there are no assurances that the Company will sell the Australian subsidiary.

Industrial Acids

The Chemical Business manufactures and sells industrial acids, primarily to the food, paper, chemical and electronics industries. The Company is the leading supplier to third parties of concentrated nitric acid which is a special grade of nitric acid used in the manufacture of plastics, pharmaceuticals, herbicides, explosives, and other chemical products. In addition, the Company produces and sells regular, blended and mixed nitric acid and a variety of grades of sulfuric acid. The Company competes on the basis of price and service, including on-time reliability and distribution capabilities. The Company operates the largest fleet of tankcars in the concentrated nitric acid industry which provides it with a significant competitive advantage in terms of distribution costs and capabilities. In addition, the Company provides inventory management as part of the value-added services it offers to its customers.

The Company has identified concentrated nitric acid as a strategic product line for its Chemical Business due to attractive levels of profitability, increased diversity of end markets and the ability to compete on a value added service basis. To support further growth in its nitric acid business, the Company constructed the DSN Plant located at the El Dorado Facility. The DSN Plant uses a newer and more efficient process to produce concentrated nitric acid directly from anhydrous ammonia, in contrast to the conventional process which requires the input of regular nitric acid, an intermediate step to produce concentrated nitric acid.

DSN Plant

During the four years commencing January 1, 1994, the Chemical Business spent approximately $32.0 million to construct and install the DSN Plant. The DSN Plant began limited operations in 1995, and such limited operations continued due to certain mechanical and design problems associated with the plant's construction and installation. As a result of such problems, production at the DSN Plant was limited to approximately 170 and 223 tons per day for the years ended December 31, 1997 and 1998, respectively. These production rates approximate 60% and 80%, respectively, of the stated capacity of 285 tons per day assuming 338 days of annual production. In October, 1998, management completed certain corrective actions at the DSN Plant. As a result of these corrective actions, the DSN Plant has since produced at rates equal to or above the stated capacity of 285 tons per day. While the Company will seek to market the additional capacity of concentrated nitric acid output to commercial markets, there can be no assurance that the Company will be able to sell all of the additional capacity in this market. However, to the extent that there is insufficient demand for concentrated nitric acid, the Company believes it can profitably use the concentrated nitric acid in the production of mixed and blended acids and ammonium nitrate based fertilizer and explosives (although at lower margins than if the production were sold as concentrated nitric acid). See "Special Note Regarding Forward-Looking Statements".

EDNC Baytown Plant

In June, 1997, two wholly owned subsidiaries of the Company, El Dorado Chemical Company ("EDC") and El Dorado Nitrogen Company ("EDNC"), entered into a series of agreements with Bayer Corporation ("Bayer")(collectively, the "Bayer Agreement"). Under the Bayer Agreement, EDNC will act as an agent to construct and, upon completion of construction, will operate a nitric acid plant (the "EDNC Baytown Plant") at Bayer's Baytown, Texas chemical facility. EDC has guaranteed the performance of EDNC's obligations under the Bayer Agreement.

Under the terms of the Bayer Agreement, EDNC is to lease the EDNC Baytown Plant pursuant to a leveraged lease from an unrelated third party with an initial lease term of ten years from the date on which the EDNC Baytown Plant becomes fully operational. Bayer will purchase from EDNC all of its requirements for nitric acid to be used by Bayer at its Baytown, Texas facility for ten years from the date on which the EDNC Baytown Plant becomes fully operational. EDNC will purchase from Bayer its requirements for anhydrous ammonia for the manufacture of nitric acid as well as utilities and other services. Subject to certain conditions, EDNC will be entitled to sell the amount of nitric acid manufactured at the EDNC Baytown Plant which is in excess of Bayer's requirements to third parties. The Bayer Agreement provides that Bayer will make certain net monthly payments to EDNC which will be sufficient for EDNC to recover all of its costs plus a profit. The Company estimates that, after the initial start-up phase of operations of the EDNC Baytown Plant, at full production capacity based on terms of the

Bayer Agreement and subject to the price of anhydrous ammonia, the EDNC Baytown Plant is anticipated to generate approximately $35 million to $50 million in annual gross revenues. Unlike the Chemical Business' regular sales volume, the market risk on this additional volume is much less since the contract provides for recovery of costs, as defined, plus a profit. See "Special Note Regarding Forward-Looking Statements". Upon expiration of the initial ten-year term from the date the EDNC Baytown Plant becomes operational, the Bayer Agreement may be renewed for up to six renewal terms of five years each; however, prior to each renewal period, either party to the Bayer Agreement may opt against renewal.

Under the original Bayer Agreement, if operations at the EDNC Baytown Plant were not commenced by February 1, 1999, or upon a change in control of LSB, EDC or EDNC, Bayer had an option to terminate the Bayer Agreement. EDNC has an option to terminate the Bayer Agreement upon the occurrence of certain events of default which remain uncured. Bayer retains the right of first refusal with respect to any bona fide third-party offer to purchase any voting stock of EDNC or any portion of the EDNC Baytown Plant.

In January, 1999, the contractor constructing the EDNC Baytown Plant informed the Company that it could not complete construction alleging a lack of financial resources. The Company and certain other parties involved in this project have demanded the contractor's bonding company to provide funds necessary for subcontractors to complete construction. The Company, the contractor, the bonding company and Bayer have entered into an agreement which provides that the bonding company will pay $12.9 million for payments to subcontractors for work performed prior to February 1, 1999. In addition, the contractor has agreed to provide, on a no cost basis, labor and to incur certain other additional costs through the completion of the contract. Because of this delay, an amendment was entered into in connection with the Bayer Agreement. The amendment extended the requirement date that the plant be in production by May 31, 1999, and fully operational by June 30, 1999. The amendment also requires the Company to reimburse Bayer for certain increased costs incurred by Bayer due to the failure to complete the construction of the EDNC Baytown Plant by February 1, 1999. The anticipated construction cost of the EDNC Baytown Plant, not including the $12.9 million paid to subcontractors by the bonding company, is currently anticipated to be approximately $69 million. The Company anticipates that construction of the EDNC Baytown Plant will be mechanically complete and making acid by April 15, 1999, and, after completion of certain performance tests, be fully operational by June 1, 1999. Construction financing of the EDNC Baytown Plant is being provided by an unaffiliated lender up to $75 million. Neither the Company nor EDC has guaranteed any of the lending obligations for the EDNC Baytown Plant. See "Special Note Regarding Forward-Looking Statements".

Raw Materials

Anhydrous ammonia represents the primary component in the production of most of the products of the Chemical Business. See "Management's Discussion and Analysis of Financial Condition and Results of Operations." The Chemical business currently purchases approximately 220,000 tons of anhydrous ammonia per year for use in its manufacture of its products. The Company has contracts with three suppliers of anhydrous ammonia. One contract expires in

April, 2000, one expires in June, 2000, and the other expires in December, 2000. The Chemical Business is required to buy at least 120,000 tons of its annual requirements of anhydrous ammonia under the contract expiring in April, 2000, at least 24,000 tons of its annual requirements of anhydrous ammonia under the contract expiring in June, 2000, and at least 60,000 tons of its annual requirements of anhydrous ammonia under the contract expiring in December, 2000, with additional quantities of anhydrous ammonia available under each contract. Anhydrous ammonia is not being currently supplied under the contract expiring in December, 2000, due to that supplier's declaration of an event of force majeure as a result of a temporary shut down of its plant caused by mechanical problems. The Company has been able to, on a temporary basis, obtain anhydrous ammonia from other sources on similar terms as provided in the contract expiring in December, 2000.

During 1995, 1996, 1997, and the first half of 1998, there were substantial increases in the price for anhydrous ammonia. During each of these periods, the Chemical Business was unable to increase its sales prices to cover all of the higher anhydrous ammonia costs incurred by the Company, and in the future the Chemical Business may not be able to pass along to its customers the full amount of increases in anhydrous ammonia costs. Accordingly, the Company's results of operations and financial condition have in the past been adversely affected by cost increases of raw materials, including anhydrous ammonia. During the second half of 1998, cost for anhydrous ammonia decreased. The ammonia industry added an additional one million tons of capacity of anhydrous ammonia in the western hemisphere in 1998, and the Company believes there is approximately one million tons of additional annual capacity of anhydrous ammonia being constructed in the western hemisphere scheduled for completion in 1999. The Company believes this additional capacity may contribute to a decline in the future market price of anhydrous ammonia. See "Special Note Regarding Forward-Looking Statements".

The Company believes that it could obtain anhydrous ammonia from other sources in the event of a termination of the above-referenced contracts, but such may not be obtainable on as favorable terms.

Seasonality

The Company believes that the only seasonal products of the Chemical Business are fertilizer and related chemical products sold to the agricultural industry. The selling seasons for those products are primarily during the spring and fall planting seasons, which typically extend from February through May and from September through November in the geographical markets in which the majority of the Company's agricultural products are distributed. As a result, the Chemical Business increases its inventory of ammonium nitrate prior to the beginning of each planting season. Sales to the agricultural markets depend upon weather conditions and other circumstances beyond the control of the Company.

Patents

The Company believes that the Chemical Business does not depend upon any patent or license; however, the Chemical Business does own certain patents that it considers important in connection with the manufacture of certain blasting agents and high explosives. These patents will expire in 1999.

Regulatory Matters

Each of the Chemical Business' domestic blasting product distribution centers are licensed by the Bureau of Alcohol, Tobacco and Firearms in order to manufacture and distribute blasting products. The Australian distribution centers are subject to comparable licensing requirements imposed by their controlling government authorities. The Chemical Business is also subject to extensive federal, state and local environmental laws, rules and regulations. See "Environmental Compliance", "Environmental Matters" and "Legal Proceedings".

Competition

The Chemical business competes with other chemical companies in its markets, many of whom have greater financial and other resources than the Company. The Company believes that competition within the markets served by the Chemical Business is primarily based upon price, service, warranty and product performance. The Company believes that the Chemical Business is the leader in the Texas ammonium nitrate market and is the leading producer of concentrated nitric acid in the United States for third party sales. See "Special Note Regarding Forward-Looking Statements".

Developments in Asia

The Chemical Business' Australian subsidiaries' results of operations have been adversely affected during 1997 and 1998 due to economic developments in certain countries in Asia. These economic developments in Asia have had a negative impact on the mining industry in Australia which the Chemical Business services. The Company received in 1999 an offer for the purchase of the Australian subsidiary, and, as of the date of this report, the Company is negotiating with the company that made the offer. There are no assurances that the Company will sell the Australian subsidiary.

Climate Control Business

General

The Company's Climate Control Business manufactures and sells a broad range of standard and custom designed hydronic fan coils and water source heat pumps as well as other products for use in commercial and residential heating ventilation and air conditioning ("HVAC") systems. Demand for the Climate Control Business' products is driven by the construction of commercial, institutional and residential buildings, the renovation of existing buildings and the replacement of existing systems. The Climate Control Business' commercial products are used in a wide variety of buildings, such as: hotels, motels, office buildings, schools, universities, apartments, condominiums, hospitals, nursing homes, extended care facilities, supermarkets and superstores. Many of the Company's products are targeted to meet increasingly stringent indoor air quality and energy efficiency standards. The Climate Control Business accounted for approximately 37%, 34% and 29% of the Company's 1998, 1997 and 1996 consolidated sales, respectively.

Hydronic Fan Coils

The Climate Control Business is the leading provider of hydronic fan coils targeted to the commercial and institutional markets in the U.S. Hydronic fan coils use heated or chilled water, provided by a centralized chiller or boiler through a water pipe system, to condition the air and allow individual room control. Hydronic fan coil systems are quieter and have longer lives and lower maintenance costs than comparable systems used where individual room control is required. The Company believes that its product line of hydronic fan coils is the most extensive offered by any domestic producer. The breadth of this product line coupled with customization capability provided by a flexible manufacturing process are important components of the Company's strategy for competing in the commercial and institutional renovation and replacement markets. See "Special Note Regarding Forward-Looking Statements".

Water Source Heat Pumps

The Company is a leading U.S. provider of water source heat pumps to the commercial construction and renovation markets. These are highly efficient heating and cooling units which enable individual room climate control through the transfer of heat through a water pipe system which is connected to a centralized cooling tower or heat injector. Water source heat pumps enjoy a broad range of commercial applications, particularly in medium to large sized buildings with many small, individually controlled spaces. The Company believes the market for commercial water source heat pumps will continue to grow due to the relative efficiency and long life of such systems as compared to other air conditioning and heating systems, as well as to the emergence of the replacement market for those systems. See "Special Note Regarding Forward-Looking Statements".

Geothermal Products

The Climate Control Business is a pioneer in the use of geothermal water source heat pumps in residential and commercial applications. Geothermal systems, which circulate water or antifreeze through an underground heat exchanger, are among the most energy efficient systems available. The Company believes that an aging installed base of residential HVAC systems, coupled with the longer life, lower cost to operate, and relatively short payback periods of geothermal systems will continue to increase demand for its geothermal products, particularly in the residential replacement market. See "Special Note Regarding Forward-Looking Statements".

Hydronic Fan Coil and Water Source Heat Pump Market

The Company has pursued a strategy of specializing in hydronic fan coils and water source heat pump products. The annual U.S. market for hydronic fan coils and water source heat pumps is approximately $273 million. Demand in these markets is generally driven by levels of repair, replacement, and new construction activity. The U.S. market for fan coils and water source heat pump products has grown on average 14% per year over the last 4 years. This growth has been fueled by new construction, the aging of the installed base of units, the introduction of new energy efficient systems, upgrades to central air conditioning and increased governmental regulations restricting the use of ozone depleting refrigerants in HVAC systems.

Production and Backlog

Most of the Climate Control Business' production of the above-described products occurs on a specific order basis. The Company manufactures the units in many sizes and configurations, as required by the purchaser, to fit the space and capacity requirements of hotels, motels, school, hospitals, apartment buildings, office buildings and other commercial or residential structures. As of December 31, 1998, the backlog of confirmed orders for the Climate Control Business was approximately $21.1 million as compared to approximately $28.8 million at December 31, 1997. A customer generally has the right to cancel an order prior to the order being released to production. Past experience indicates that customers generally do not cancel orders after the Company receives them. As of March 31, 1999, the Climate Control Business had released substantially all of the December 31, 1998 backlog to production. All of the December 31, 1998 backlog is expected to be filled by December 31, 1999. See "Special Note Regarding Forward-Looking Statements".

Marketing and Distribution

Distribution

The Climate Control Business sells its products to mechanical contractors, original equipment manufacturers and distributors. The Company's sales to mechanical contractors primarily occur through independent manufacturer's representatives, who also represent complementary product lines not manufactured by the Company. Original equipment manufacturers generally consist of other air conditioning and heating equipment manufacturers who resell under their own brand name the products purchased from the Climate Control Business in competition with the Company. Sales to original equipment manufacturers accounted for approximately 25% of the sales of the Climate Control Business in 1998 and approximately 9% of the Company's 1998 consolidated sales.

Market

The Climate Control Business depends primarily on the commercial construction industry, including new construction and the remodeling and renovation of older buildings. In recent years this Business has introduced geothermal products designed for residential markets for both new and replacement markets.

Raw Materials

Numerous domestic and foreign sources exist for the materials used by the Climate Control Business, which materials include aluminum, copper, steel, electric motors and compressors. The Company does not expect to have any difficulties in obtaining any necessary materials for the Climate Control Business. See "Special Note Regarding Forward-Looking Statements".

Competition

The Climate Control Business competes with approximately eight companies, some of whom are also customers of the Company. Some of the competitors have greater financial and other resources than the Company. The Climate Control Business manufactures a broader line of fan coil and water source heat pump products than any other manufacturer in the United States, and the Company believes that it is competitive as to price, service, warranty and product performance.

Joint Ventures and Options to Purchase

The Company has obtained an option to acquire 80% of the issued and outstanding stock of an Entity ("Entity") that performs energy savings contracts, primarily on US government facilities (the "Option"). For the Option, the Company has paid $1.3 million as of the date of this report. The term of the Option expires May 4, 1999. The Company is currently negotiating to extend the expiration date of its Option. As of the date of this report, the Company has not decided whether it will exercise the Option. If the Company is unsuccessful in negotiating an extension of the Option exercise date, and, if the Company decides to exercise the Option, the Company may pay an exercise price of $4.0 million, less the amount already paid toward the Option ("Option Price"), with a portion of the unpaid exercise price being payable in cash and the balance over a certain period of time. The grantors of the Option have entered into an employment agreement with the Entity. Under the terms of the employment agreements, each of the three grantors will receive, among other things, 12 1/2% of the net profits of the Entity for a period of three to five years following the date of exercise of the Option. If the Company is unsuccessful in negotiating an extension of the Option exercise date, and, if the Company decides not to exercise the Option, the grantors of the Option have agreed to repay to the Company the amounts paid by the Company in connection with the Option up to a total of $1.0 million, which obligation is secured by the stock of the Entity and other affiliates of the Entity. There is no assurance that the grantors of the Option will have funds necessary to repay to the Company the amount paid for the Option in the event they are required to pay such amounts. See "Management's Discussion and Analysis of Financial Condition and Results of Operations". Through the date of this report, the Company has loaned the Entity approximately $1.4 million. The Company has recorded reserves of approximately $1.3 million against the loans and option payments. For its year ended June 30, 1998, the Entity reported an audited net income of approximately $.9 million.

During 1994, a subsidiary of the Company obtained an option to acquire all of the stock of a French manufacturer of air conditioning and heating equipment. The Company's subsidiary was granted the option as a result of the subsidiary loaning to the parent company of the French manufacturer approximately $2.1 million. Subsequent to the loan of $2.1 million, the Company's subsidiary has loaned to the parent of the French manufacturer an additional $1.7 million. The amount loaned is secured by the stock and assets of the French manufacturer. The Company's subsidiary may exercise its option to acquire the French manufacturer by converting approximately $150,000 of the amount loaned into equity. The option is currently exercisable and will expire June 15, 2005. As of the date of this report, the Company has not decided whether it will exercise the option.

For 1998 and 1997, the French manufacturer had revenues of $17.2 million and $14.3 million, respectively, and reported net income in 1998 and 1997 of approximately $100,000 and $300,000, respectively. As a result of cumulative losses by the French manufacturer, the Company established reserves against the loans aggregating approximately $1.5 million through December 31, 1998. See "Management's Discussion and Analysis of Financial Condition and Results of Operations".

Automotive Products Business

General

The Automotive Products Business is primarily engaged in the manufacture and sale of a line of anti-friction bearings, which includes straight-thrust and radial-thrust ball bearings, angular contact ball bearings, and certain other automotive replacement parts (including universal joints, motor mounts, and clutches). This Business also manufactures power train and drive line parts for original equipment manufacturers. These products are used in automobiles, trucks, trailers, tractors, farm and industrial machinery, and other equipment. The Automotive Products Business accounted for approximately 13% and 11% of the Company's 1998 and 1997 sales, respectively. In 1998, the Automotive Products Business manufactured approximately 44% of the products it sold, and approximately 40% in 1997, and purchased the balance of its products from other sources, including foreign sources.

As discussed in "Item 1 - Business - General", the Company is continuing with its evaluation of the spin-off of Automotive to its shareholders as a dividend. The spin-off of Automotive will require, among other things, commitment to a formal plan, receipt by the Company from the Internal Revenue Service of a favorable ruling or an opinion of counsel confirming tax-free treatment, certain Securities and Exchange Commission filings, arrangement for lines of credit for Automotive, and LSB Board of Directors' approval. Subject to completion of the above conditions, management believes there is a strong likelihood that the spin-off will be completed during 1999. However, there are no assurances that the Company will spin-off Automotive.

Distribution and Market

The automotive, truck and agricultural equipment replacement markets serve as the principal markets for the Automotive Products Business. This Business sells its products domestically and for export, principally through independent manufacturers' representatives who also sell other automotive products. Those manufacturers' representatives sell to retailers (including major chain stores), wholesalers, distributors and jobbers. The Automotive Products Business also sells its products directly to original equipment manufacturers and certain major chain stores.

Inventory

The Company generally produces or purchases the products sold by the Automotive Products Business in quantities based on a general sales forecast, rather than on specific orders from customers. The Company fills most orders for the automotive replacement market from inventory. The Company generally produces products for original equipment manufacturers after receiving an order from the manufacturer.

Raw Materials

The principal materials that the Automotive Products Business needs to produce its products consist of high alloy steel tubing, steel bars, flat strip coil steel and bearing components produced to specifications. The Company acquires those materials from a variety of domestic and foreign suppliers at competitive prices. The Company does not anticipate having any difficulty in obtaining those materials in the near future. See "Special Note Regarding Forward-Looking Information".

Foreign Risk

By purchasing a significant portion of the bearings and other automotive replacement parts that it sells from foreign manufacturers, the Automotive Products Business must bear certain import duties and international economic risks, such as currency fluctuations and exchange controls, and other risks from political upheavals and changes in United States or other countries' trade policies. Contracts for the purchase of foreign-made bearings and other automotive replacement parts provide for payment in United States dollars. Circumstances beyond the control of the Company could eliminate or seriously curtail the supply of bearings or other automotive replacement parts from any one or all of the foreign countries involved.

Competition

The Automotive Products Business engages in a highly competitive business. Competitors include other domestic and foreign bearing manufacturers, which sell in the original equipment and replacement markets. Many of those manufacturers have greater financial and other resources than the Company.

Industrial Products Business

General

The Industrial Products Business purchases and markets a proprietary line of machine tools. The current line of machine tools distributed by the Industrial Products Business includes milling, drilling, turning and fabricating machines. The Industrial Products Business purchases most of the machine tools marketed by it from foreign companies, which manufacture the machine tools to the Company's specifications. This Business manufactures CNC bed mills and electrical control panels for machine tools. The Company has eliminated in the past, and continues to eliminate, certain categories of machinery from its product line by not replacing them when sold. The Industrial Products Business accounted for approximately 5% of the Company's consolidated sales in each of the years 1998 and 1997.

Distribution and Market

The Industrial Products Business distributes its machine tools in the United States, Mexico, Canada and certain other foreign markets. The Industrial Products Business also sells its machine tools through independent machine tool dealers throughout the United States and Canada, who purchase the machine tools for resale to end users. The principal markets for machine tools, other than machine tool dealers, consist of manufacturing and metal working companies, maintenance facilities, and utilities.

Foreign Risk

By purchasing a majority of the machine tools from foreign manufacturers, the Industrial Products Business must bear certain import duties and international economic risks, such as currency fluctuations and exchange controls, and other risks from political upheavals and changes in United States or other countries' trade policies. Contracts for the purchase of foreign-made machine tools provide for payment in United States dollars. Circumstances beyond the control of the Company could eliminate or seriously curtail the supply of machine tools from any one or all of the foreign countries involved.

Competition

The Industrial Products Business competes with manufacturers, importers, and other distributors of machine tools many of whom have greater financial resources than the Company. The Company's machine tool business generally is competitive as to price, warranty and service, and maintains personnel to install and service machine tools.

Employees

As of December 31, 1998, the Company employed 1,723 persons. As of that date, (a) the Chemical Business employed 578 persons, with 133 represented by unions under agreements expiring in August, 2001 and February, 2002, (b) the Climate Control Business employed 686 persons, none of whom are represented by a union, and (c) the Automotive Products Business employed 344 persons, with 21 represented by unions under an agreement expiring in July, 2000.

Research and Development

The Company incurred approximately $409,000 in 1998, $394,000 in 1997, and $532,000 in 1996 on research and development relating to the development of new products or the improvement of existing products. All expenditures for research and development related to the development of new products and improvements are expensed by the Company.

Environmental Matters

The Company and its operations are subject to numerous Environmental Laws and to other federal, state and local laws regarding health and safety matters ("Health Laws"). In particular, the manufacture and distribution of chemical products are activities which entail environmental risks and impose obligations under the Environmental Laws and the Health Laws, many of which provide for substantial fines and criminal sanctions for violations, and there can be no assurance that material costs or liabilities will not be incurred by the Company in complying with such laws or in paying fines or penalties for violation of such laws. The Environmental Laws and Health Laws and enforcement policies thereunder relating to the Chemical Business have in the past resulted, and could in the future result, in penalties, cleanup costs, or other liabilities relating to the handling, manufacture, use, emission, discharge or disposal of pollutants or other substances at or from the Company's facilities or the use or disposal of certain of its chemical products. Significant expenditures have been incurred by the Chemical Business at the El Dorado Facility in order to comply with the Environmental Laws and Health Laws. The Chemical Business may be required to make additional significant site or operational modifications at the El Dorado Facility, potentially involving substantial expenditures and reduction, suspension or cessation of certain operations. See "Special Note Regarding Forward-Looking Statements"; "Management's Discussion and Analysis of Financial Condition and Results of Operations-Chemical Business" and "Legal Proceedings."

Due to a consent order entered into with the Arkansas Department of Pollution Control & Ecology ("ADPC&E"), the Chemical Business has installed additional monitoring wells at the El Dorado Facility in accordance with a workplan approved by the ADPC&E, and submitted the test results to ADPC&E. The results indicated that a risk assessment should be conducted on nitrates present in the shallow groundwater. The Chemical Business' consultant has completed this risk assessment, and has forwarded it to the ADPC&E for approval. The risk assessment concludes that, although there are contaminants at the El Dorado Facility and in the groundwater, the levels of such contaminants at the El Dorado Facility and in the groundwater do not present an unacceptable risk to human health and the environment. Based on this conclusion, the Chemical Business' consultant has recommended continued monitoring at the site for five years.

A second consent order was entered into with ADPC&E in August, 1998 (the "Wastewater Consent Order"), which required installation of an interim groundwater treatment system (which is now operating) and certain improvements in the wastewater collection and treatment system (discussed below). Twelve months after all improvements are in place, the risk will be reevaluated, and a final decision will be made on what additional groundwater remediation, if any, is required. There can be no assurance that the risk assessment will be approved by the ADPC&E, or that further work will not be required.

In addition, in accordance with the consent order, the Chemical Business currently plans to upgrade the El Dorado Facility's wastewater treatment plant. Current estimates of the cost of the planned upgrade are that approximately $4.6 million in future capital expenditures will be incurred to complete this project. Furthermore, the El Dorado Facility's new wastewater permit currently is being reviewed for renewal by the ADPC&E. The new permit may impose additional or more stringent limitations on the plant's wastewater discharges. The Company believes, although there can be no assurance, that any such new limitations would not have a material adverse effect on the Company. See "Special Note Regarding Forward-Looking Statements."

During May, 1997, approximately 2,300 gallons of caustic material spilled when a valve in a storage vessel located at the El Dorado Facility failed, resulting in a release of such material to a stormwater drain, and according to ADPC&E records, a minor fish kill in a creek near the El Dorado Facility. In 1998, the Chemical Business entered into a Consent Administrative Order (the "Wastewater Consent Order") with the ADPC&E to resolve this event, as well as certain violations of the facility's NPDES permit for wastewater discharge. The Wastewater Consent Order also resolved several issues relating to a Consent Administrative Order that the Chemical Business had entered into in May, 1995, which ordered closure of a solid waste landfill. The Wastewater Consent Order requires the Chemical Business to complete a waste minimization plan and characterize the wastewater before obtaining a new NPDES permit, which is expected to have more restrictive effluent limits, to install additional treatment to meet the new effluent limits by August 1, 2001, and achieve compliance with the new effluent limits by February 1, 2002. The Chemical Business is currently undertaking the waste minimization activities. The Wastewater Consent Order recognizes the presence of nitrate contamination in the groundwater and requires the Chemical Business to undertake on-site bioremediation, which is currently underway. Upon completion of the waste minimization activities referenced above, a final remedy for groundwater contamination will be selected, based on an evaluation of risk. There are no known users of groundwater in the area, and preliminary risk assessments have not identified any risk that would require additional remediation. The Wastewater Consent Order included a $183,700 penalty assessment, of which $125,000 will be satisfied over five years at expenditures of $25,000 per year for waste minimization activities. The Chemical Business has documented in excess of $25,000 on expenditures for the first year, 1998. An additional $57,000 of the assessed penalty was satisfied by funding approved supplemental environmental projects and the $1,700 required monetary civil penalty has been paid.

The El Dorado Facility's air permit required it to cease operation of certain older nitric acid concentrators (the "Older Nitric Acid Concentrators") within a certain period of time after the initiation of operations of the DSN Plant. Due to certain start-up problems with the DSN Plant, including excess emissions from various emission sources, the Chemical Business and the ADPC&E entered into certain agreements, including an administrative consent order (the "Air Consent Order") in 1995 to resolve certain of the Chemical Business' past violations and to permit the Chemical Business to operate the Older Nitric Acid Concentrators until the ADPC&E has made a final decision regarding the El Dorado Facility's air permit, including whether the Older Nitric Acid Concentrators may continue to operate. Although the Company expects that the Chemical Business will be able to continue to operate the Older Nitric Acid Concentrators, there can be no assurance that the ADPC&E will allow it to continue to do so. The Air Consent Order also provides for payment of a civil penalty of $50,000, which the Chemical Business has paid, and requires installation of certain pollution control equipment and completion of certain maintenance activities at the El Dorado Facility to eliminate certain off-site hazing problems. The Air Consent Order was amended in 1996 and 1997. The second amendment to the Air Consent Order (the "1997 Amendment") provided for certain stipulated penalties of $1,000 per hour to $10,000 per day for continued off-site emission events and deferred enforcement for other alleged air permit violations. The 1997 Amendment acknowledges that the Chemical Business has completed the installation of the pollution control equipment and maintenance activities required under the Air Consent Order. Nonetheless, the Chemical Business was assessed an additional penalty of $150,000, as well as a payment of an additional $50,000 to fund certain environmental projects, with respect to a number of alleged permit violations relating to off-site emissions and other air permit conditions. The Chemical Business has paid both the penalty and the additional sums required by the 1997 Amendment. Since the 1997 Amendment and as of the date of this report, the Chemical Business has been assessed stipulated penalties of approximately $67,000 by the ADPC&E for violations of certain provisions of the 1997 Amendment. In 1998, a third amendment to the Air Consent Order provided for the stipulated penalties to be reset at $1,000 per hour after ninety (90) days without any confirmed events. The Chemical Business believes that the El Dorado Facility has made progress in controlling certain off-site emissions; however, such off-site emissions have occurred, and may continue, from time to time, which could result in the assessment of additional penalties against the Chemical Business by the ADPC&E and could have a material adverse effect on the Company. In addition, prior to 1998, the El Dorado Facility was identified as one of 33 significant violators of the federal Clean Air Act in a review of Arkansas air programs by the EPA Office of Inspector General. The Company is unable to predict the impact, if any, of such designation. See "Special Note Regarding Forward-Looking Statements."

During 1997 and 1998, the Chemical Business expended approximately $1.1 million and $.7 million, respectively, in connection with capital expenditures relating to compliance with federal, state and local Environmental Laws at its El Dorado Facility, including, but not limited to, compliance with the Air Consent Order, as amended. The Company anticipates that the Chemical Business will spend approximately $4.6 million for capital expenditures relating to environmental control facilities at its El Dorado Facility to comply with Environmental Laws, including, but not limited to, the Air Consent Order, as amended, with $2.4 million being spent in 1999 and the balance being spent in 2000. No assurance can be made that the actual expenditures of the Chemical Business for such matters will not exceed the estimated amounts by a substantial margin, which could have a material adverse effect on the Company and its financial condition. The amount to be spent during 1999 for capital expenditures related to compliance with Environmental Laws is dependent upon a variety of factors, including, but not limited to, the occurrence of additional releases or threatened releases (particularly air emissions) into the environment, or changes in the Environmental Laws (or in the enforcement or interpretation by any federal or state agency or court of competent jurisdiction). See "Special Note Regarding Forward-Looking Statements." Failure to satisfactorily resolve the pending noncompliance issues with the ADPC&E, or additional orders from the ADPC&E imposing penalties, or requiring the Chemical Business to spend more for environmental improvements or curtail production activities at the El Dorado Facility, could have a material adverse effect on the Company.

Item 2. PROPERTIES

Chemical Business

The Chemical Business primarily conducts manufacturing operations (i) on 150 acres of a 1,400 acre tract of land located in El Dorado, Arkansas (the "El Dorado Facility"), (ii) in a facility of approximately 60,000 square feet located on ten acres of land in Hallowell, Kansas ("Kansas Facility") and (iii) in a mixed acid plant in Wilmington, North Carolina ("Wilmington Plant"). The Chemical Business owns all of its manufacturing facilities, with the El Dorado Facility and the Wilmington Plant subject to mortgages. In addition, the Chemical Business has four manufacturing facilities in Australia that produce bulk and packaged explosives.

As of December 31, 1998, the El Dorado Facility was utilized at approximately 74% of capacity, based on continuous operation.

The Chemical Business operates its Kansas Facility from buildings located on an approximate ten acre site in southeastern Kansas, and a research and testing facility comprising approximately ten acres, including buildings and equipment thereon, located in southeastern Kansas, which it owns.

In addition, the Chemical Business distributes its products through 32 agricultural and explosive distribution centers. The Chemical Business currently operates 22 agricultural distribution centers, with 16 of the centers located in Texas (13 of which the Company owns and three of which it leases); one center located in Oklahoma which the Company owns; two centers located in Missouri (one of which the Company owns and one of which it leases); and three centers located in Tennessee (all of which the company owns). The Chemical Business currently operates six domestic explosives distribution centers located in Hallowell, Kansas (owned); Bonne Terre, Missouri (owned); Poca, West Virginia (leased); Owensboro and Combs, Kentucky (leased); and Pryor, Oklahoma (leased). The Chemical Business also has four explosives distribution centers in Australia, all of which are leased.

Climate Control Business

The Climate Control Business conducts its fan coil manufacturing operations in a facility located in Oklahoma City, Oklahoma, consisting of approximately 265,000 square feet. The Company owns this facility subject to a mortgage. As of December 31, 1998, the Climate Control Business was using the productive capacity of the above referenced facilities to the extent of approximately 87%, based on three, eight-hour shifts per day and a five-day week in one department and one and one half eight-hour shifts per day and a five-day week in all other departments.

The Climate Control Business manufactures most of its heat pump products in a leased 270,000 square foot facility in Oklahoma City, Oklahoma, which it leases from an unrelated party. The lease term began March 1, 1988, after renewal in October 1997, and expires February 28, 2003, with options to renew for additional five-year periods, and currently provides for the payment of rent in the amount of $52,389 per month. The Company also has an option to acquire the facility at any time in return for the assumption of the then outstanding balance of the lessor's mortgage. As of December 31, 1998, the productive capacity of this manufacturing operation was being utilized to the extent of approximately 81%, based on two twelve-hour shifts per day and a seven-day week in one department and one eight-hour shift per day and a five-day week in all other departments.

All of the properties utilized by the Climate Control Business are considered by the Company management to be suitable and adequate to meet the current needs of that Business.

Automotive Products Business

The Automotive Products Business conducts its operations in plant facilities principally located in Oklahoma City, Oklahoma which are considered by Company management to be suitable and adequate to meet its needs. One of the manufacturing facilities occupies a building owned by the Company, subject to mortgages, totaling approximately 178,000 square feet. The Automotive Products Business also uses additional manufacturing facilities located in Oklahoma City, Oklahoma, owned and leased by the Company totaling approximately 158,000 square feet. During 1998, the Automotive Products Business under utilized the productive capacity of its facilities.

International Bearings, Inc. ("IBI"), a subsidiary of the Company operating as a separate entity within the Automotive Products Division, operates from a Company owned warehouse of approximately 45,000 square feet in an industrial park section of Memphis, Tennessee.

Industrial Products Business

The Company owns several buildings, some of which are subject to mortgages, totaling approximately 360,000 square feet located in Oklahoma City and Tulsa, Oklahoma, which the Industrial Products Business uses for showrooms, offices, warehouse and manufacturing facilities. The Company also owns real property located near or adjacent to the above-referenced buildings in Oklahoma City, Oklahoma, which the Industrial Products Business uses for parking and storage. The Company also leases facilities in Middletown, New York containing approximately 25,000 square feet for manufacturing operations.

The Industrial Products Business also leases a facility from an entity owned by the immediate family of the Company's President, which facility occupies approximately 30,000 square feet of warehouse and shop space in Oklahoma City, Oklahoma. The Industrial Products Business also leases an office in Europe to coordinate its European activities.

All of the properties utilized by the Industrial Products Business are considered by Company management to be suitable and adequate to meet the needs of the Industrial Products Business.

Item 3. LEGAL PROCEEDINGS

In 1987, the U.S. Environmental Protection Agency ("EPA") notified one of the Company's subsidiaries, along with numerous other companies, of potential responsibility for clean-up of a waste disposal site in Oklahoma. In 1990, the EPA added the site to the National Priorities List. Following the remedial investigation and feasibility study, in 1992 the Regional Administrator of the EPA signed the Record of Decision ("ROD") for the site. The ROD detailed EPA's selected remedial action for the site and estimated the cost of the remedy at $3.6 million. In 1992, the Company made settlement proposals which would have entailed a collective payment by the subsidiaries of $47,000. The site owner rejected this offer and proposed a counteroffer of $245,000 plus a reopener for costs over $12.5 million. The EPA rejected the Company's offer, allocating 60% of the cleanup costs to the potentially responsible parties and 40% to the site operator. The EPA estimated the total cleanup costs at $10.1 million as of February 1993. The site owner rejected all settlements with the EPA, after which the EPA issued an order to the site owner to conduct the remedial design/remedial action approved for the site. In August, 1997, the site owner issued an "invitation to settle" to various parties, alleging the total cleanup costs at the site may exceed $22 million.

No legal action has yet been filed. The amount of the Company's cost associated with the cleanup of the site is unknown due to continuing changes in the estimated total cost of cleanup of the site and the percentage of the total waste which was alleged to have been contributed to the site by the Company. As of December 31, 1998, the Company has accrued an amount based on a recent preliminary settlement proposal by the alleged potential responsible parties; however, there is no assurance such proposal will be accepted. Such amount is not material to the Company's financial position or results of operations. This estimate is subject to material change in the near term as additional information is obtained. The subsidiary's insurance carriers have been notified of this matter; however, the amount of possible coverage, if any, is not yet determinable.

Arch Mineral Corporation, et al. v. ICI Explosives USA, Inc., et al. On May 24, 1996, the plaintiffs filed this civil cause of action against EDC and five other unrelated commercial explosives manufacturers alleging that the defendants allegedly violated certain federal and state antitrust laws in connection with alleged price fixing of certain explosive products. This cause of action is pending in the United States District Court, Southern District of Indiana. The plaintiffs are suing for an unspecified amount of damages, which, pursuant to statute, plaintiffs are seeking be trebled, together with costs. Plaintiffs are also seeking a permanent injunction enjoining defendants from further alleged anti-competitive activities. Based on the information presently available to EDC, EDC does not believe that EDC conspired with any party, including, but not limited to, the five other defendants, to fix prices in connection with the sale of commercial explosives. This action has been consolidated, for discovery purposes only, with several other actions in a multi-district litigation proceeding in Utah. Discovery in this litigation is in process. EDC intends to vigorously defend itself in this matter. See "Special Note Regarding Forward-Looking Statements."

ASARCO v. ICI, et al. The U. S. District Court for the Eastern District of Missouri has granted ASARCO and other plaintiffs in a lawsuit originally brought against various commercial explosives manufacturers in Missouri, and consolidated with other lawsuits in Utah, leave to add EDC as a defendant in that lawsuit. This lawsuit alleges a national conspiracy, as well as a regional conspiracy, directed against explosive customers in Missouri and seeks unspecified damages. EDC has been included in this lawsuit because it sold products to customers in Missouri during a time in which other defendants have admitted to participating in an antitrust conspiracy, and because it has been sued in the Arch case discussed above. Based on the information presently available to EDC, EDC does not believe that EDC conspired with any party, to fix prices in connection with the sale of commercial explosives. EDC intends to vigorously defend itself in this matter. See "Special Note Regarding Forward-Looking Statements."

Eugene Lowe, et al. v. Teresa Trucking, Inc., pending in the Circuit Court of Lincoln County, West Virginia. During the third quarter of 1997, EDC was served with this lawsuit in which approximately 27 plaintiffs have sued approximately 13 defendants, including EDC, alleging personal injury and property damage for undifferentiated compensatory and punitive damages of approximately $7,000,000. Specifically, the plaintiffs assert property damage to their residence and wells, annoyance and inconvenience, and nuisance as a result of daily blasting and round-the-clock mining activities. The plaintiffs are residents living near the Heartland Coal Company ("Heartland") strip mine in Lincoln County, West Virginia, and an unrelated mining operation operated by Pen Coal Inc. During the first quarter of 1999, the plaintiffs withdrew all personal injury claims previously asserted in this litigation. Heartland employed EDC to provide blasting materials and personnel to load and shoot holes drilled by employees of Heartland. Down hole blasting services were provided by EDC at Heartland's premises from approximately August 1991, until approximately August 1994. Subsequent to August 1994, EDC supplied blasting materials to the reclamation contractor at Heartland's mine. In connection with EDC's activities at Heartland, EDC has entered into a contractual indemnity to Heartland to indemnify Heartland under certain conditions for acts or actions taken by EDC or for which EDC failed to take, and Heartland is alleging that EDC is liable thereunder for Heartland's defense costs and any losses to, or damages sustained by, the plaintiffs in this lawsuit as a result of EDC's operations.

Discovery in this litigation is in process. The Company intends to vigorously defend itself in this matter. EDC has provided notification of this lawsuit to its two insurance carriers providing primary insurance coverage to EDC during the period covered by the plaintiff's allegations. Based on information provided to EDC by its counsel handling this matter, the Company does not believe that this matter will have a material adverse effect on the Company.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Not applicable.

Item 4A. EXECUTIVE OFFICERS OF THE COMPANY

Identification of Executive Officers

The following table identifies the executive officers of the Company.

Name	Age	Position and Offices with the Company	Served as an Officer from
Jack E. Golsen	70	Board Chairman and President	December, 1968
Barry H. Golsen	48	Board Vice Chairman and President of the Climate Control Business	August, 1981
David R. Goss	58	Senior Vice President of Operations and Director	March, 1969
Tony M. Shelby	57	Senior Vice President - Chief Financial Officer, and Director	March, 1969
Jim D. Jones	57	Vice President - Treasurer and Corporate Controller	April, 1977
David M. Shear	39	Vice President and General Counsel	March, 1990

The Company's officers serve one-year terms, renewable on an annual basis by the Board of Directors. All of the individuals listed above have served in substantially the same capacity with the Company and/or its subsidiaries for the last five years. In March 1996, the Company executed an employment agreement (the "Agreement") with Jack E. Golsen for an initial term of three years followed by two additional three year terms. The Agreement automatically renews for each successive three year term unless terminated by either the Company or Jack E. Golsen giving written notice at least one year prior to the expiration of the then three year term.

Family Relationships

The only family relationship that exists among the executive officers of the Company is that Jack E. Golsen is the father of Barry H. Golsen.

PART II

Item 5. MARKET FOR THE COMPANY'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Market Information

The Company's Common Stock trades on the New York Stock Exchange, Inc. ("NYSE"). The following table shows, for the periods indicated, the high and low closing sales prices for the Company's Common Stock.

	Fiscal Year Ended December 31,			
	1998		1997	
Quarter	High	Low	High	Low
First	4 1/2	3 13/16	5 1/4	4 1/8
Second	4 9/16	3 13/16	5	4
Third	4 3/8	3 1/8	5	3 5/8
Fourth	3 9/16	2 15/16	5 13/16	3 5/8

Stockholders

As of February 28, 1999, the Company had 981 record holders of its Common Stock.

Other Information

The Company's Common Stock and its $3.25 Convertible Exchangeable Class C Preferred Stock, Series 2 (the "Series 2 Preferred") are currently listed for trading on the New York Stock Exchange ("NYSE"). The Company recently fell below the NYSE continued listing criteria for net tangible assets available to the holders of the Company's Common Stock and the three year average net income. Based on a business plan submitted to the NYSE, the NYSE has agreed to continue the listing of the Company's Common Stock and Series 2 Preferred subject to certain quarterly reviews. There are no assurances that the Company will be able to comply with the business plan presented to the NYSE and that the Company's Common Stock and Series 2 Preferred will continue to be listed on the NYSE.

Dividends

Under the terms of a loan agreement between the Company and its lender, the Company may, so long as no event of default has occurred and is continuing under the loan agreement, make currently scheduled dividends and pay dividends on its outstanding Preferred Stock and pay annual dividends on its Common Stock equal to $.06 per share. In addition, the loan agreement with the lender includes as an event of default an ownership change if any Person (except Jack E. Golsen or members of his Immediate Family, as defined below, and any entity controlled by Jack E. Golsen or members of his Immediate Family together with such Person's affiliates and associates), is or becomes the beneficial owner, directly or indirectly, of more than fifty percent (50%) of the outstanding Common Stock of the Company. The term "Immediate Family" of any Person means the spouse, siblings, children, mothers and mothers-in-law, fathers and fathers-in-law, sons and daughters-in-law, daughters and sons-in-law, nieces, nephews, brothers and sisters-in-law, and sisters and brothers-in-law.

The Company is a holding company and, accordingly, its ability to pay dividends on its Preferred Stock and its Common Stock is dependent in large part on its ability to obtain funds from its subsidiaries. The ability of the Company's wholly-owned subsidiary ClimaChem, Inc. ("ClimaChem") (which owns substantially all of the companies comprising the Chemical Business and the Climate Control Business) and its wholly-owned subsidiaries to pay dividends and to make distributions to the Company is restricted by certain covenants contained in the Indenture to which they are parties.

Under the terms of the Indenture, ClimaChem cannot transfer funds to the Company in the form of cash dividends or other distributions or advances, except for (i) the amount of taxes that ClimaChem would be required to pay if they were not consolidated with the Company and (ii) an amount not to exceed fifty percent (50%) of ClimaChem's cumulative net income from January 1, 1998, through the end of the period for which the calculation is made for the purpose of proposing a payment and (iii) the amount of direct and indirect costs and expenses incurred by the Company on behalf of ClimaChem pursuant to a certain services agreement and a certain management agreement to which ClimaChem and the Company are parties. For 1998, ClimaChem had a net loss of $2.6 million. See Note 5 of Notes to Consolidated Financial Statements and Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations".

Under the loan agreement, the Company and its subsidiaries, other than ClimaChem and its subsidiaries, have the right to borrow on a revolving basis up to $24 million, based on eligible collateral. At December 31, 1998, the Company and its subsidiaries, except ClimaChem and its subsidiaries, had availability for additional borrowings of $2.7 million. See Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" for a discussion of the financial covenants which the Company's failure to maintain could result in an event of default.

Holders of the Company's Common Stock are entitled to receive dividends only when, as, and if declared by the Board of Directors. No dividends may be paid on the Company's Common Stock until all required dividends are paid on the outstanding shares of the Company's Preferred Stock, or declared and amounts set apart for the current period, and, if cumulative, prior periods. The Company has issued and outstanding as of December 31, 1998, 915,000 shares of $3.25 Convertible Exchangeable Class C Preferred Stock, Series 2 ("Series 2 Preferred"), 1,463 shares of a series of Convertible Non Cumulative Preferred Stock ("Non Cumulative Preferred Stock") and 20,000 shares of Series B 12% Convertible, Cumulative Preferred Stock ("Series B Preferred"). Each share of Preferred Stock is entitled to receive an annual dividend, if, as and when declared by the Board of Directors, payable as follows: (i) Series 2 Preferred at the rate of $3.25 a share payable quarterly in arrears on March 15, June 15, September 15 and December 15, which dividend is cumulative, (ii) Non Cumulative Preferred Stock at the rate of $10.00 a share payable April 1, and (iii) Series B Preferred at the rate of $12.00 a share payable January 1, which dividend is cumulative. The Company has a policy as to the payment of annual cash dividends on its outstanding Common Stock of an amount per share to be determined by the Board of Directors from time to time. The Company paid a cash dividend of $.01 a share on its outstanding Common Stock on July 1, 1998, and January 1, 1999; however, there are no assurances that this policy will not be terminated or changed by the Board of Directors. As of the date of this report, management is considering, but has not made its final decision, recommending to the Board of Directors that the Company discontinue payments of cash dividends on its Common Stock for periods subsequent to January 1, 1999. Due to ClimaChem's net loss for 1998, the restrictions contained in the Indenture and certain borrowing limitations upon the Company, other than ClimaChem and its subsidiaries, under the Company's loan agreements, management has not, as of the date of this report, determined whether the Company will have adequate liquidity to declare and pay each of the quarterly dividends on its outstanding Preferred Stock during 1999. See Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources" for further discussion of the Company's payment of cash dividends. Also see Notes 7, 8 and 9 of Notes to Consolidated Financial Statements.

On February 17, 1989, the Company's Board of Directors declared a dividend to its stockholders of record on February 27, 1989, of one Preferred Stock purchase right on each of the Company's outstanding shares of Common Stock (the "Preferred Shares Purchase Rights Plan"). The rights expire on February 27, 1999. On January 5, 1999, the Company's Board of Directors approved the renewal of the Company's existing Preferred Share Purchase Rights Plan (with certain exceptions) through the execution and delivery of a Renewed Rights Agreement, dated January 6, 1999, which expires January 6, 2009 ("Renewed Rights Plan"). The Company issued the rights, among other reasons, in order to assure that all of the Company's stockholders receive fair and equal treatment in the event of any proposed takeover of the Company and to guard against partial tender abusive tactics to gain control of the Company. The rights under the Renewed Rights Plan (the "Renewed Rights") will become exercisable only if a person or group acquires beneficial ownership of 20% or more of the Company's Common Stock or announces a tender or exchange offer the consummation of which would result in the ownership by a person or group of 20% or more of the Common Stock, except pursuant to a tender or exchange offer which is for all outstanding shares of Common Stock at a price and on terms which a majority of outside directors of the Board of Directors determines to be adequate and in the best interest of the Company in which the Company, its stockholders and other relevant constituencies, other than the party triggering the rights (a "Permitted Offer"), except acquisitions by the following excluded persons (collectively, the "Excluded Persons"): (i) the Company, (ii) any subsidiary of the Company, (iii) any employee benefit plan of the Company or its subsidiaries, (iv) any entity holding Common Stock for or pursuant to the employee benefit plan of the Company or its subsidiary, (v) Jack E. Golsen, Chairman of the Board and President of the Company, his spouse and children and certain related trusts and entities, (vi) any party who becomes the beneficial owner of 20% or more of the Common Stock solely as a result of the acquisition of Common Stock by the Company, unless such party shall, after such share purchase by the Company, become the beneficial owner of additional shares of Common Stock constituting 1% or more of the then outstanding shares of Common Stock, and (vii) any party whom the Board of Directors of the Company determines in good faith acquired 20% or more of the Common Stock inadvertently and such person divests within 10 business days after such determination, a sufficient number of shares of Common Stock and no longer beneficially own 20% of the Common Stock.

Each Renewal Rights, when triggered, (other than the Renewal Rights, owned by the acquiring person or members of a group that causes the Renewal Rights to become exercisable, which became void) will entitle the stockholder to buy one one-hundredth of a share of a new series of participating Preferred Stock at an exercise price of $20.00 per share. Each one one-hundredth of a share of the new Preferred Stock purchasable upon the exercise of a right has economic terms designed to approximate the value of one share of the Company's Common Stock. If another person or group acquires the Company in a merger or other business combination transaction, each Renewal Right will entitle its holder (other than Renewal Rights owned by the person or group that causes the Renewal Rights to become exercisable, which become void) to purchase at the Renewal Right's then current exercise price, a number of the acquiring company's common shares which at the time of such transaction would have a market value two times the exercise price of the Renewal Right. In addition, if a person or group (with certain exceptions) acquires 20% or more of the Company's outstanding Common Stock, each Renewal Right will entitle its holder (other than the Renewal Rights owned by the acquiring person or members of the group that results in the Renewal Rights becoming exercisable, which become void) to purchase at the Renewal Right's then current exercise price, a number of shares of the Company's Common Stock having a market value of twice the Renewal Right's exercise price in lieu of the new Preferred Stock.

Following the acquisition by a person or group of beneficial ownership of 20% or more of the Company's outstanding Common Stock (with certain exceptions) and prior to an acquisition of 50% or more of the Company's Common Stock by the person or group, the Board of Directors may exchange the Renewal Rights (other than Renewal Rights owned by the acquiring person or members of the group that results in the Renewal Rights becoming exercisable, which become void), in whole or in part, for shares of the Company's Common Stock. That exchange would occur at an exchange ratio of one share of Common Stock, or one one-hundredth of a share of the new series of participating Preferred Stock, per Renewal Right.

Prior to the acquisition by a person or group of beneficial ownership of 20% or more of the Company's Common Stock (with certain exceptions) the Company may redeem the Renewal Rights for one cent per Renewal Right at the option of the Company's Board of Directors. The Company's Board of Directors also has the authority to reduce the 20% thresholds to not less than 10%.

Item 6. SELECTED FINANCIAL DATA

	Years ended December 31, 1998	1997	1996	1995	1994
	(Dollars in Thousands, except per share data)				
Selected Statement of Operations Data:					
Net sales	$310,037	$313,929	$307,160	$267,391	$245,025
Total revenues	$324,320	$319,096	$313,425	$274,115	$249,969
Interest expense	$ 17,327	$ 14,740	$ 10,017	$ 10,131	$ 6,949
Income (loss) from continuing operations before extraordinary charge	$ (1,920)	$(18,446)	$ (3,845)	$ (3,732)	$ 983
Net income (loss)	$ (1,920)	$(23,065)	$ (3,845)	$ (3,732)	$ 24,467
Net income (loss) applicable to common stock	$ (5,149)	$(26,294)	$ (7,074)	$ (6,961)	$ 21,232
Basic and diluted earnings (loss) per common share:					
Loss from continuing operations before extraordinary charge	$ (.42)	$ (1.68)	$ (.55)	$ (.54)	$ (.17)
Net income (loss)	$ (.42)	$ (2.04)	$ (.55)	$ (.54)	$ 1.57

Item 6. SELECTED FINANCIAL DATA (Continued)

	Years ended December 31,				
	1998	1997	1996	1995	1994
	(Dollars in Thousands, except per share data)				
Selected Balance Sheet Data:					
Total assets	$248,647	$270,653	$261,560	$238,176	$221,281
Long-term debt, including current portion	$169,642	$180,941	$132,284	$118,280	$ 91,681
Redeemable preferred stock	$ 139	$ 146	$ 146	$ 149	$ 152
Stockholders' equity	$ 35,059	$ 44,496	$ 74,018	$ 81,576	$ 90,599
Selected other data:					
Cash dividends declared per common share	$ .02	$ .06	$ .06	$ .06	$ .06

Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations should be read in conjunction with a review of the Company's December 31, 1998 Consolidated Financial Statements, Item 6 "SELECTED FINANCIAL DATA" and Item 1 "BUSINESS" included elsewhere in this report.

Certain statements contained in this "Management's Discussion and Analysis of Financial Conditions and Results of Operations" may be deemed forward-looking statements. See "Special Note Regarding Forward-Looking Statements".

Overview

General

The Company is pursuing a strategy of focusing on its core businesses and concentrating on product lines in niche markets where the Company has established or believes it can establish a position as a market leader. In addition, the Company is seeking to improve its liquidity and profits through liquidation of selected assets that are on its balance sheet and on which it is not realizing an acceptable return and does not reasonably expect to do so. In this connection, the Company has come to the conclusion that its Automotive and Industrial Products Businesses are non-core to the Company and the Company is exploring various alternatives to maximize shareholder value from these assets. The Company is also considering the sale of other assets that are non-core to its Chemical and Climate Control Businesses.

As discussed in "Item 1 - Business - General", the Company is continuing with its evaluation of the spin-off of Automotive to its shareholders as a dividend. The spin-off of Automotive will require, among other things, commitment to a formal plan, receipt by the Company from the Internal Revenue Service of a favorable ruling or an opinion of counsel confirming tax-free treatment, certain Securities and Exchange Commission filings, arrangement for lines of credit for Automotive, and LSB Board of Directors' approval. Subject to completion of the above conditions, management believes there is a strong likelihood that the spin-off will be completed during 1999. However, there are no assurances that the Company will spin-off Automotive.

Certain statements contained in this Overview are forward-looking statements, and future results could differ materially from such statements.

The following table contains certain of the information from Note 13 of Notes to the Company's Consolidated Financial Statements about the Company's operations in different industry segments for each of the three years in the period ended December 31, 1998.

	1998	1997	1996
	(In Thousands)		
Sales:			
Chemical	$139,942	$ 156,949	$ 166,163
Climate Control	115,786	105,909	89,275
Automotive Products	39,994	35,499	37,946
Industrial Products	14,315	15,572	13,776
	$310,037	$ 313,929	$ 307,160
Gross profit: (1)			
Chemical	$ 18,274	$ 19,320	$ 25,885
Climate Control	32,278	29,552	21,961
Automotive Products	8,670	3,299	5,868
Industrial Products	3,731	3,776	3,058
	$ 62,953	$ 55,947	$ 56,772
Operating profit (loss): (2)			
Chemical	$ 3,675	$ 5,479	$ 10,971
Climate Control	10,493	8,895	5,362
Automotive Products	(1,827)	(7,251)	(4,134)
Industrial Products	(403)	(993)	(2,685)
	11,938	6,130	9,514
General corporate expenses, net	(9,424)	(9,786)	(3,192)
Interest expense	(17,327)	(14,740)	(10,017)
Gain on sale of the Tower	12,993	-	-
Loss from continuing operations before provision for income taxes and extra-ordinary charge	$ (1,820)	$ (18,396)	$ (3,695)
Total assets:			
Chemical	$124,577	$ 137,570	$ 132,718
Climate Control	49,516	49,274	50,623
Automotive Products	41,967	42,718	43,212
Industrial Products	11,662	9,929	13,614
	227,722	239,491	240,167
Corporate assets and other	20,925	31,162	21,393
Total assets	$248,647	$ 270,653	$ 261,560

(1) Gross profit by industry segment represents net sales less cost of sales.
(2) Operating profit by industry segment represents revenues less operating expenses before deducting general corporate expenses, interest expense and income taxes and, in 1998, before gain on sale of the Tower.

Chemical Business

Although sales in the Chemical Business have declined from $156.9 million in the twelve months ended December 31, 1997, to $139.9 million in the twelve months ended December 31, 1998 (a decrease of 10.8%) and the gross profit has decreased from $19.3 million in 1997 to $18.3 million in 1998, the gross profit percentage has increased from 12.3% in 1997 to 13.1% in 1998.

In 1998, the Chemical Business was adversely affected by the extreme drought conditions in the mid-south market during the primary fertilizer season, followed by excess wet conditions and floods in the fall season, resulting in substantially lower volume and lower sales prices for certain of its products sold in its agricultural markets. The operating profit of the Chemical Business decreased from $5.5 million in 1997 to $3.7 million in 1998 (a decrease of 32.9%). The decline in sales volume explains approximately $1.0 million of this decrease. The remaining $800,000 decrease is primarily attributable to a provision for possible loss on a note receivable recorded in the fourth quarter of 1998.

During 1997, limitations on production, as a result of certain mechanical and design problems relating to the construction and start-up of a concentrated nitric acid plant, resulted in significant fixed costs being expended as period costs rather than being absorbed as cost of product being produced and sold. In addition, significant amounts were expended for engineering, consulting, and other costs to bring the nitric acid plant up to its stated capacity.

Additionally, the cost of the Chemical Business' primary raw material, anhydrous ammonia, averaged approximately $184 per ton in 1997, compared to approximately $154 per ton in 1998. The Chemical Business purchases approximately 220,000 tons of anhydrous ammonia per year under three contracts expiring in April, 2000, June, 2000, and December, 2000, respectively. The Company's purchase price of anhydrous ammonia under these contracts can be higher or lower than the current market spot price of anhydrous ammonia. Pricing is subject to variations due to numerous factors contained in these contracts. Based on the price calculations contained in the contracts, one contract is presently priced above the current market spot price. The Chemical Business is required to purchase 120,000 tons of its requirements under the contract expiring in April, 2000, at least 24,000 tons of its requirements under the contract expiring in June, 2000, and 60,000 tons of its requirements under the contract expiring in December, 2000, with additional quantities of anhydrous ammonia available under each contract. Anhydrous ammonia is not being currently supplied under the contract expiring in December, 2000, due to that supplier's declaration of an event of force majeure as a result of a temporary shut down of its plant due to mechanical problems. The Company has been able to, on a temporary basis, obtain anhydrous ammonia from other sources on similar terms as provided in the contract expiring in December, 2000.

The anhydrous ammonia industry added an additional one million tons of capacity of anhydrous ammonia in the western hemisphere in 1998, and the Company believes there is approximately one million tons of additional annual capacity of anhydrous ammonia being constructed in the western hemisphere scheduled for completion in 1999. The Company believes this additional capacity may contribute to a decline in the future market price of anhydrous ammonia. See "Special Note Regarding Forward-Looking Statements".

In June, 1997, a subsidiary of the Company entered into an agreement with Bayer Corporation ("Bayer") whereby one of the Company's subsidiaries is acting as agent to construct a nitric acid plant located within Bayer's Baytown, Texas chemical plant complex. This plant, when constructed, will be operated by the Company's subsidiary and will supply nitric acid for Bayer's polyurethane business under a long-term supply contract. Management estimates that, after the initial startup phase of operations at the plant, at full production capacity based on terms of the Bayer Agreement and dependent upon the price of anhydrous ammonia, based on the price of anhydrous ammonia as of the date of this report, the plant should generate approximately $35 million to $50 million in annual gross revenues. Unlike the Chemical Business' regular sales volume, the market risk on this additional volume is much less since the contract provides for recovery of costs, as defined, plus a profit. It is anticipated that the construction of the nitric acid plant at Bayer's facility in Baytown, Texas, will cost approximately $69 million and construction is scheduled to be completed in the second quarter of 1999. The Company's subsidiary is to lease the nitric acid plant pursuant to a leverage lease from an unrelated third party for an initial term of ten (10) years from the date that the plant becomes fully operational, and the construction financing of this plant is being provided by an unaffiliated lender. (See Item 1 - "Business - - - Chemical Business" for a further discussion of the Baytown, Texas nitric acid plant facility.)

The results of operation of the Chemical Business' Australian subsidiary have been adversely affected due to the recent economic developments in certain countries in Asia. These economic developments in Asia have had a negative impact on the mining industry in Australia which the Company's Chemical Business services. As these adverse economic conditions in Asia have continued, such have had an adverse effect on the Company's consolidated results of operations in 1998. The Company received an offer in 1999 to purchase its Australian subsidiary. As of the date of this report, the Company is negotiating with the company that offered to buy the Australian subsidiary. During 1998, TES had net sales of $14.2 million, and reported a net loss of $2.9 million. There are no assurances that the Company will sell the Australian subsidiary.

Climate Control

The Climate Control Business manufactures and sells a broad range of hydronic fan coil, air handling, air conditioning, heating, water source heat pump, and dehumidification products targeted to both commercial and residential new building construction and renovation.

The Climate Control Business focuses on product lines in the specific niche markets of hydronic fan coils and water source heat pumps and has established a significant market share in these specific markets.

As indicated in the above table, the Climate Control Business reported improved sales (an increase of 9.3%) and improved operating profit (an increase of 18.0%) for 1998, as compared to 1997.

Automotive and Industrial Products Businesses

As indicated in the above table, during 1998, 1997, and 1996, the Automotive and Industrial Products Businesses recorded combined sales of $54.3 million, $51.1 million, and $51.7 million, respectively, and reported operating losses (as defined above) of $2.2 million, $8.2 million, and $6.8 million in 1998, 1997, and 1996, respectively. The net investment in assets of these Businesses was $53.6 million, $52.6 million, and $56.8 million at year end 1998, 1997, and 1996, respectively. While the Company's investment in the assets of these businesses has declined from $56.8 million in 1996 to $53.6 million in 1998, the Company expects to realize further reductions in future periods as it implements its proposed plan to dispose of non-core and non-earning assets. See "Overview - General" for a discussion of the Company's intent to spin-off the Automotive Business, subject to numerous conditions precedent. During 1998, the Automotive Business had net sales of $40.0 million, and an operating loss (as defined) of approximately $1.8 million. The Company continues to eliminate certain categories of machinery from the Industrial Products' product line by not replacing machines when sold.

Results of Operations

Year Ended December 31, 1998 compared to Year Ended December 31, 1997

Revenues

Total revenues for 1998 and 1997 were $324.3 million and $319.1 million, respectively (an increase of $5.2 million). Sales decreased $3.9 million and other income decreased $3.9 million. Additionally, in March, 1998, a subsidiary of the Company closed the sale of an Oklahoma City office building (the "Tower"). The Company recognized a pre-tax gain on the sale of the Tower of approximately $13.0 million in the first quarter of 1998. The decrease in other income of $3.9 million was primarily due to non-recurring operations of the Tower, which was sold in March, 1998, and certain valuation reserve adjustments recorded against specifically identified investments in the fourth quarter of 1998.

Net Sales

Consolidated net sales included in total revenues for 1998 were $310.0 million, compared to $313.9 million for 1997, a decrease of $3.9 million. This decrease in sales resulted principally from: (i) decreased sales in the Industrial Products Business of $1.3 million due to decreased sales of machine tools, and (ii) decreased sales in the Chemical Business of $17.0 million primarily due to lower sales volume in the U.S. of agricultural and blasting products and decreased business volume of its Australian subsidiary. Sales were lower in the Chemical Business during 1998, compared to 1997, as a result of adverse weather conditions in its agricultural markets during the spring and fall planting seasons. Blasting sales in the Chemical Business declined as a result of elimination of certain low profit margin sales and decreased volume in the Australian subsidiary resulting from adverse economic developments in Asia. These decreases were offset by (i) increased sales in the Climate Control Business of $9.9 million, primarily due to increased volume and price increases in both the heat pump and fan coil product lines, and (ii) increased sales in the Automotive Products Business of $4.5 million primarily due to increased volume of units being shipped to original equipment manufacturers and new customers.

Gross Profit

Gross profit increased $7.0 million and was 20.3% of net sales for 1998, compared to 17.8% of net sales for 1997. The gross profit percentage improved in the Chemical, Automotive Products and Industrial Products Businesses. It was consistent from 1997 to 1998 in the Climate Control Business.

The increase in the gross profit percentage was due primarily to (i) increased absorption of costs due to higher production volumes and improved experience with returns and allowances in the Automotive Products Business, (ii) lower production costs in the Chemical Business due to the effect of lower prices of anhydrous ammonia in 1998, (iii) lower unabsorbed overhead costs caused by excessive downtime related to problems associated with mechanical failures at the Chemical Business' primary manufacturing plant in the first half of 1997, and (iv) higher gross profit product mix of machine tools sold in the Industrial Products Business.

Selling, General and Administrative Expense

Selling, general and administrative expenses ("SG&A"), as a percent of net sales, were 19.9% in 1998, and 20.6% in 1997. SG&A, as a percent of sales, was approximately 11.5% in 1998, compared to 9.8% in 1997 for the Chemical Business; 20.3% in 1998, compared to 21.0% in 1997 for the Climate Control Business; 26.5% in 1998, compared to 32.1% in 1997 for the Automotive Products Business; and 33.3% in 1998, compared to 33.4% in 1997 for the Industrial Products Business.

The increase in the Chemical Business was the result of lower sales in 1998 with relatively constant SG&A expenses. Within SG&A of the Chemical Business, higher provisions for uncollectible accounts receivable in 1998 were offset by decreased expenses at the Company's Australian subsidiary in anticipation of sustaining a lower level of business activity. The decrease in the Climate Control Business' SG&A as a percentage of sales was the result of increases in sales. The Climate Control Business' amount of SG&A increased in 1998 due to additional information technology personnel to support management information systems changes and higher variable costs due to a change in sales mix toward greater domestic sales which carry a higher SG&A percent. The decrease in the Automotive Products Business was due to higher sales and decreased expenses pursuant to a comprehensive cost reduction program implemented by the Company.

In addition to the variances described above, approximately $1.7 million of the total SG&A decrease of $3.0 million is due to the reduction of costs associated with the Tower which was sold in March of 1998 compared to a full year in 1997 and approximately $1.0 million is due to legal fees in 1997 over 1998 to assert the Company's position in various legal proceedings.

Interest Expense

Interest expense for the Company, before deducting capitalized interest, was $17.3 million during 1998, compared to $15.9 million during 1997. During 1997, $1.1 million of interest expense was capitalized in connection with construction of the DSN Plant. The increase of $1.4 million before the effect of capitalization primarily resulted from increased borrowings. The increased borrowings were necessary to support capital expenditures, higher accounts receivable balances and to meet the operational requirements of the Company. See "Liquidity and Capital Resources" of this Management's Discussion and Analysis.

Extraordinary Charge

In 1997, in connection with the issuance of the 10 3/4% unsecured senior notes due 2007 by a subsidiary of the Company, a subsidiary of the Company retired the outstanding principal associated with a certain financing arrangement and incurred a prepayment fee. The prepayment fee and loan origination costs expensed in 1997 related to the financing arrangement aggregated approximately $4.6 million.

Net Loss

The Company had a net loss of $1.9 million in 1998, compared to a net loss of $23.1 million in 1997. The decreased loss of $21.2 million was primarily due to the gain on the sale of the Tower in 1998, increased gross profit in 1998, decreased SG&A in 1998, and the extraordinary charge in 1997 offset by increased interest expense in 1998, as discussed above.

Year Ended December 31, 1997 compared to Year Ended December 31, 1996

Revenues

Total revenues for 1997 and 1996 were $319.1 million and $313.4 million, respectively (an increase of $5.7 million or 1.8%). Sales increased $6.8 million or 2.2%.

Net Sales

Consolidated net sales for 1997 were $313.9 million, compared to $307.2 million for 1996, an increase of $6.8 million or 2.2%. This sales increase resulted principally from: (i) increased sales in the Climate Control Business of $16.6 million, primarily due to increased sales of heat pumps; and (ii) increased sales of $1.8 million in the Industrial Products Business due to increased machine tool sales; partially offset by (iii) decreased sales of $2.4 million in the Automotive Products Business due to less units being shipped and product mix; and (iv) decreased sales in the Chemical Business of $9.2 million primarily due to reduced sales of the Company's wholly-owned Australian subsidiary, because of the expiration of certain customer contracts and recent economic developments in Asia.

Gross Profit

Gross profit decreased $.8 million and was 17.8% of net sales for 1997, compared to 18.5% of net sales for 1996. The gross profit percentage declined in the Automotive Products and Chemical Businesses, but improved in the Climate Control and Industrial Products Businesses.

The gross profit of the Chemical Business was adversely affected by higher production costs due to (i) the higher cost of anhydrous ammonia which was only partially passed on in the form of higher selling prices, (ii) unabsorbed overhead costs caused by down time related to modifications made to resolve problems associated with mechanical failures, and (iii) environmental matters at the Chemical Business' primary manufacturing plant. These increased costs in 1997 were partially offset by a reduction in cost of sales of $2.1 million through recapture of manufacturing variances of the Chemical Business in the form of business interruption insurance settlements.

The primary reasons for the decline in gross profit percentage in the Automotive Products Business were (i) less favorable customer mix (i.e., decreased sales to higher margin retail customers, and increased sales to Original Equipment Manufacturer (OEM) customers which are lower margin customers), and (ii) increases in manufacturing expenses in excess of increases in production cost absorption attributable to new product lines that have been developed.

These gross profit declines have been partially offset by gross profit percentage increases due to sales of machine tools carrying a higher gross profit percentage in the Industrial Products Business and increased absorption of costs due to higher production volumes and focus on sales of more profitable product lines in the Climate Control Business.

Selling, General and Administrative Expense

Selling, general and administrative expenses ("SG&A"), as a percent of net sales, were 20.6% in 1997 and 18.5% in 1996. SG&A, as a percent of sales, was approximately 9.8% in 1997 compared to 9.3% in 1996 for the Chemical Business; 21.0% in 1997 compared to 19.8% in 1996 for the Climate Control Business; 32.1% in 1997 compared to 29.5% in 1996 for the Automotive Products Business; and 33.4% in 1997 compared to 44.4% in 1996 for the Industrial Products Business.

The increase in the Chemical Business was the result of lower sales in 1997 with relatively constant SG&A expenses. Within SG&A of the Chemical Business, lower provisions for uncollectible accounts receivable in 1997 were offset by increased expenses at the Company's Australian subsidiary in anticipation of sustaining a higher level of business activity. The increase in the Climate Control Business' SG&A was the result of increases in sales personnel costs to support higher sales in future periods, additional information technology personnel to support management information systems changes and higher freight costs due to a change in sales mix toward greater domestic sales which carry a higher SG&A percent. The increase in the Automotive Products Business was due to lower sales and increased advertising expenses expected to benefit future periods. The decrease in the Industrial Products Business resulted from lower bad debt expenses and lower advertising expenses compounded by higher sales.

In addition to the variances described above, approximately $2.2 million of the total SG&A increase of $8.1 million is due to the operations of the Tower in 1997 as discussed elsewhere in this report and approximately $2.4 million is due to increased legal fees, settlement accruals and loss reserves in 1997 over 1996 to assert the Company's position in various legal proceedings and joint ventures.

Interest Expense

Interest expense for the Company, before deducting capitalized interest, was $15.9 million during 1997, compared to $12.4 million during 1996. During 1997, $1.1 million of interest expense was capitalized in connection with construction of the DSN Plant, compared to $2.4 million in 1996. The increase of $3.5 million before the effect of capitalization primarily resulted from increased borrowings and higher interest rates. The increased borrowings were necessary to support capital expenditures, higher accounts receivable balances and to meet the operational requirements of the Company.

Extraordinary Charge

In 1997, in connection with the issuance of the 10 3/4% unsecured senior notes due 2007 by a subsidiary of the Company, a subsidiary of the Company retired the outstanding principal associated with a certain financing arrangement and incurred a prepayment fee. The prepayment fee and loan origination costs expensed in 1997 related to the financing arrangement aggregated approximately $4.6 million.

Net Loss

The Company had a net loss of $23.1 million in 1997 compared to a net loss of $3.8 million in 1996. The increased loss of $19.3 million was primarily due to decreased gross profit, increased SG&A, increased interest expense and the extraordinary charge as discussed above.

Liquidity and Capital Resources

Cash Flow From Operations

Historically, the Company's primary cash needs have been for operating expenses, working capital and capital expenditures. The Company has financed its cash requirements primarily through internally generated cash flow and borrowings under its revolving credit facilities, and more recently, by issuance of senior unsecured notes by a wholly owned subsidiary.

Net cash used by operations for the year ended December 31, 1998 was $4.2 million, after $13.2 million for noncash depreciation and amortization, $4.9 million in provisions for possible losses on accounts receivable, inventory, notes receivable and a loan guarantee, $1.1 million of increase in cash surrender value on certain life insurance policies and $13.9 million in gains from the sales of real estate and other assets and including the following changes in assets and liabilities: (i) accounts receivable increases of $2.3 million; (ii) inventory decreases of $1.3 million; (iii) increases in supplies and prepaid items of $1.0 million; and (iv) decreases in accounts payable and accrued liabilities of $3.5 million. The increase in accounts receivable is due to increased sales and extended credit terms to new customers in the Automotive Products Business and initial sales under the Bayer Agreement in the Chemical Business. The decrease in inventory was due primarily to measures taken in all of the Company's Businesses to decrease their inventory levels. The increase in supplies and prepaid items resulted primarily from an increase in maintenance and manufacturing supplies in the Chemical Business. The decrease in accounts payable and accrued liabilities was primarily due to timing of payments for inventory purchases in the Chemical Business.

Cash Flow from Investing and Financing Activities

Cash provided by investing activities for the year ended December 31, 1998 included cash proceeds of $29.3 million received on the sale of the Tower (see Note 2 of Notes to the Company's Consolidated Financial Statements) and proceeds from sales of other property of $1.8 million offset by $9.6 million in capital expenditures and $2.1 million used to increase other assets. The capital expenditures took place primarily in the Chemical and Climate Control Businesses to enhance production and product delivery capabilities. The increase in other assets includes approximately $.9 million of cash advances to a start-up aviation company as discussed later in this report under "Debt Guarantee" and approximately $.7 million of deposits made in connection with an interest rate hedge contract related to the agreement with Bayer.

Net cash used by financing activities included: (i) payments on long-term debt of $20.3 million, including the $12.6 million payoff of the mortgage on the Tower, (ii) long-term and other borrowings, net of origination fees, of $.6 million, (iii) net increases in revolving debt of $7.7 million, after application of net proceeds of $16.5 million from the sale of the Tower, (iv) dividends of $3.5 million, and (v) treasury stock purchases of $3.6 million.

Source of Funds

The Company is a diversified holding Company and its liquidity is dependent, in large part, on the operations of its subsidiaries and credit agreements with lenders.

The Company and certain of its subsidiaries are parties to a working capital line of credit evidenced by four separate loan agreements ("Revolving Credit Agreements") with an unrelated lender ("Lender") collateralized by receivables, inventory, and proprietary rights of the Company and the subsidiaries that are parties to the Revolving Credit Agreements and the stock of certain of the subsidiaries that are borrowers under the Revolving Credit Agreements. The Revolving Credit Agreements, as amended, provide for revolving credit facilities ("Revolver") for total direct borrowings up to $65.0 million, including the issuance of letters of credit. The Revolver provides for advances at varying percentages of eligible inventory and trade receivables. The Revolving Credit Agreements, as amended, provide for interest at the lender's prime rate plus .5% per annum or, at the Company's option, on the Lender's LIBOR rate plus 2.875% per annum (which rates are subject to increase or reduction based upon achieving specified availability and adjusted tangible net worth levels). At December 31, 1998, the effective interest rate was 8.11%. The term of the Revolving Credit Agreements is through December 31, 2000, and is renewable thereafter for successive thirteen month terms. At December 31, 1998, the availability for additional borrowings, based on eligible collateral approximated $22 million. Borrowings under the Revolver outstanding at December 31, 1998, were $26.3 million. The Revolving Credit Agreements, as amended, require the Company to maintain certain financial ratios and contain other financial covenants, including tangible net worth requirements and capital expenditure limitations. At December 31, 1998, the Company was not in compliance with certain of these financial covenants. Subsequent to December 31, 1998, the Company obtained waivers of such noncompliance and amendments to reset the financial covenants through maturity. The annual interest on the outstanding debt under the Revolver at December 31, 1998 at the rates then in effect would approximate $2.1 million. The Revolving Credit Agreements also require the payment of an annual facility fee of 0.5% of the unused revolver.

In addition to the Revolving Credit Agreements discussed above, as of December 31, 1998, the Company's wholly-owned subsidiary, DSN Corporation ("DSN"), is a party to several loan agreements with a financial company (the "Financing Company") for three projects. At December 31, 1998, DSN had outstanding borrowings of $11.0 million under these loans. The loans have repayment schedules of 84 consecutive monthly installments of principal and interest through maturity in 2002. The interest rate on each of the loans is fixed and range from 8.2% to 8.9%. Annual interest, for the three notes as a whole, at December 31, 1998, at the agreed to interest rates would approximate $1.0 million. The loans are secured by the various DSN property and equipment. The loan agreements require the Company to maintain certain financial ratios, including tangible net worth requirements.

As previously discussed, the Company is a holding company and, accordingly, its ability to pay dividends on its outstanding Common Stock and Preferred Stocks is dependent in large part on its ability to obtain funds from its subsidiaries. The ability of the Company's wholly owned subsidiary, ClimaChem (which owns all of the stock of substantially all of the Company's subsidiaries comprising the Chemical Business and the Climate Control Business) and its subsidiaries to transfer funds to the Company is restricted by certain covenants contained in the Indenture to which they are parties. Under the terms of the Indenture, ClimaChem and its subsidiaries cannot transfer funds to the Company, except for (i) the amount of income taxes that they would be required to pay if they were not consolidated with the Company, (ii) an amount not to exceed fifty percent (50%) of ClimaChem's consolidated net income for the year in question, and (iii) the amount of direct and indirect costs and expenses incurred by the Company on behalf of ClimaChem and ClimaChem's subsidiaries pursuant to a certain services agreement and a certain management agreement to which the companies are parties. During 1998, ClimaChem reported a consolidated net loss of approximately $2.6 million. Accordingly, ClimaChem and its subsidiaries were unable to transfer funds to the Company in 1998 except for reimbursement of costs and expenses incurred by the Company on their behalf or in connection with certain agreements.

Under the Revolving Credit Agreements discussed above, the Company and its subsidiaries, other than ClimaChem and its subsidiaries, have the right to borrow on a revolving basis up to $24 million, based on eligible collateral. At December 31, 1998, the Company and its subsidiaries, except ClimaChem and its subsidiaries, had availability for additional borrowings based on eligible collateral of approximately $2.7 million (borrowings under the Revolver outstanding at December 31, 1998, were $14.5 million).

Due to ClimaChem's net loss for 1998 and the Company's (other than ClimaChem and its subsidiaries) limited borrowing ability under the Revolver, management is considering, but has not made its final decision, recommending to the Board of Directors that the Company discontinue payment of cash dividends on its Common Stock for periods subsequent to January 1, 1999, until the Board of Directors determines otherwise. In addition, as of the date of this report, management has not determined whether the Company will have adequate liquidity to declare and pay each of the quarterly dividends on its outstanding Preferred Stock during 1999.

Future cash requirements (other than cash dividends) include working capital requirements for anticipated sales increases in all Businesses and funding for future capital expenditures. Funding for the higher accounts receivable resulting from anticipated sales increases will be provided by cash flow generated by the Company and the revolving credit facilities discussed elsewhere in this report. Inventory requirements for the higher anticipated sales activity should be met by scheduled reductions in the inventories of the Industrial Products Business and in the inventories of the Automotive Products Business. In addition, the Company is also considering the sale of certain assets which it does not believe are critical to its Chemical and Climate Control Businesses. In 1999, the Company has planned capital expenditures of approximately $10 million, primarily in the Chemical and Climate Control Businesses, a certain amount of which it anticipates will be financed by equipment finance contracts on a term basis and in a manner allowed under its various loan agreements. Such capital expenditures include approximately $2.4 million, which the Chemical Business anticipates spending related to environmental control facilities at its El Dorado Facility, as previously discussed in this report. The Company currently has no material commitments for capital expenditures.

During the latter part of March 1999, the Company's management is considering the realignment of certain of the Company's overhead to better match its focus on its core businesses. Consistent with this realignment, in April 1999, the Company's Board of Directors approved the sale of certain assets to ClimaChem in accordance with the terms of the Indenture to which ClimaChem and its subsidiaries are parties to and the loan agreement that the Company and subsidiaries of ClimaChem are borrowing under, which assets are materially related to the lines of businesses of the Chemical and Climate Control Businesses. In addition, the Company is negotiating with an asset based lender to provide the Automotive Business with a new credit facility of up to $20.0 million, with a term loan of $2.0 million and a revolving line of credit of up to $18.0 million. If this new credit facility is finalized as currently structured, it would have provided the Automotive Business borrowing ability of approximately $14.3 million as of March 31, 1999, as compared to borrowing ability of $12.7 million under the Automotive Business' current credit facility as of March 31, 1999. Borrowings outstanding under the current credit facility at March 31, 1999, approximated $12.5 million. Such borrowings will be repaid from proceeds of this new credit facility if it is finalized. Further, the Company's Revolver provides for the elimination of its financial covenants upon the sale, disposal or spin-off of the Automotive Business by the Company as long as the Company maintains a minimum aggregate availability under the Revolver of at least $15 million.

Management believes that the Company will have adequate cash flow from operations, its revolving line of credit and other sources to meet its present anticipated working capital and debt service requirements.

If the spin-off of the Automotive Business is to be completed, the Company anticipates that the Company will be required to make a capital contribution to the Automotive Business prior to the spin-off in the form of a reduction of the amount the Automotive Business owes the Company so as to enable the Automotive Business after the spin-off to have a positive stockholders' equity. The balance of the amount the Automotive Business owes the Company is expected to be evidenced by a promissory note.

The spin-off being evaluated by the Company of the Automotive Business would be accomplished in the form of a dividend to the holders of the Company's Common Stock. In order to declare and pay a dividend upon shares of capital stock, the Delaware General Corporation Law ("Delaware Law") requires that such either be declared and paid (1) out of "surplus", as defined under the Delaware Law, or (2) in case there is no "surplus", out of net profits of the Company for the fiscal year in which the dividend is declared or the preceding fiscal year. The Company is presently reviewing with its investment banker as to whether it has sufficient "surplus" to accomplish the spin-off of the Automotive Business to its holders of its Common Stock after the capital contribution by the Company to the Automotive Business as discussed above. The Company does not believe that it will be able to pay such dividend out of net profits. If the Company's investment banker is unable to opine that the Company has sufficient "surplus" to accomplish the spin-off, under Delaware Law the Company could reduce its "capital" (as defined under Delaware Law) represented by issued shares of its capital stock without par value and transfer the amount of such reduction to "surplus", as long as the assets of the Company remaining after such reduction shall be sufficient to pay the Company's debts for which payment has not otherwise been provided. The terms of the Company's Series B 12% Cumulative Convertible Preferred Stock ("Series B Preferred") provides, in part, that "In the event of any voluntary or involuntary liquidation, dissolution or winding up of LSB, or any reduction in its capital resulting in any distribution of assets to its stockholders, the holders of the Series B Preferred Stock shall be entitled to receive in cash out of assets of LSB, whether from capital or from earnings available for distribution to the stockholders, before any amount shall be paid to the holder of Common Stock of LSB the sum of One Hundred & No/100 Dollars ($100) (the par value of the Series B Preferred Stock) per share, plus an amount equal to all accumulated and unpaid cash dividends thereon to the date fixed for payment of such distributive amount". Counsel to the Company has advised the Company that a transfer from "capital" to "surplus" to distribute the stock of the Automotive Business to the holders of the Company's Common Stock would trigger a payment of $100 per outstanding share of Series B Preferred. There are currently outstanding 20,000 shares of Series B Preferred, all of which are owned by Jack E. Golsen or members of his immediate family and/or entities wholly owned by members of Mr. Golsen's immediate family. Mr. Golsen has advised the Company that if the Company is required to transfer from "capital" to "surplus" an amount necessary to complete the spin-off and such triggers the payment under the Series B Preferred, he would not require the Company to pay such in cash but would be willing to receive such amount in a form other than cash, with the form to be determined based on negotiations with independent members of the Company's

Board of Directors. The Series B Preferred was issued by the Company in 1987 in connection with a transaction approved by the Board of Directors and the stockholders of the Company. Accordingly, as of the date of this report, there are no assurances that the Company will ultimately commit to a formal plan to spin-off the Automotive Business.

Pursuant to the Company's previously announced repurchase plan, the Company purchased during 1998, 909,300 shares of Common Stock, for an aggregate purchase price of $3,567,026. From January 1, 1999, through March 31, 1999, the Company has purchased under its repurchase plan a total of 80,400 shares of Common Stock for an aggregate amount of $232,555. As of the date of this report, management and the Board of Directors are considering whether to continue with its repurchase plan to purchase shares of its Common Stock and if so, to what extent for the balance of 1999.

Foreign Subsidiary

The Company's wholly-owned Australian subsidiary, TES, has a revolving credit working capital facility (the "TES Revolving Facility") with Bank of New Zealand, Australia, in the amount of AUS$10.5 million (approximately US$6.5 million). The TES Revolving Facility allows for borrowings based on specific percentages of qualified eligible assets. Based on the effective exchange rate at December 31, 1998, approximately US$5.0 million (AUS$8.1 million approximately) was borrowed at December 31, 1998. Such debt is secured by substantially all the assets of TES, plus an unlimited guarantee and indemnity from LSB and certain subsidiaries of TES. The interest rate on this debt is dependent upon the borrowing option elected by TES and had a weighted average rate of 7.01% at December 31, 1998. TES is in technical noncompliance with a certain financial covenant contained in the loan agreement involving the TES Revolving Facility. However, this covenant was not met at the time of closing of this loan and the Bank of New Zealand, Australia has continued to extend credit under the Facility. The outstanding borrowing under the TES Revolving Facility at December 31, 1998 has been classified as due within one year in the accompanying consolidated financial statements. As previously noted in this report, the Company has received an offer in 1999, the terms of which it is presently negotiating with the company that made the offer, to purchase TES; however, there are no assurances that the Company will sell TES. Under the terms of the Indenture to which ClimaChem is bound by, the net cash proceeds from the sale of TES, if completed, are required (1) within 270 days from the date of the sale to be applied to the redemption of the notes issued under the Indenture or to the repurchase of such notes, or (2) within 240 days from the date of such sale, the amount of the net cash proceeds be invested in a related business of ClimaChem or the Australian subsidiary or used to reduce indebtedness of ClimaChem.

Joint Ventures and Options to Purchase

Prior to 1997, the Company, through a subsidiary, loaned $2.8 million to a French manufacturer of HVAC equipment whose product line is compatible with that of the Company's Climate Control Business in the USA. Under the loan agreement, the Company has the option to exchange its rights under the loan for 100% of the borrower's outstanding common stock. The Company obtained a security interest in the stock of the French manufacturer to secure its loan. During 1997 the Company advanced an additional $1 million to the French manufacturer bringing the total of the loan at December 31, 1997 to $3.8 million. Parties to the option have agreed to extend the exercise date of the option to June 15, 2005. As of the date of this report, the decision has not been made to exercise such option and the $3.8 million loan, less a $1.5 million valuation reserve, is carried on the books as a note receivable in other assets.

In 1995, a subsidiary of the Company invested approximately $2.8 million to purchase a fifty percent (50%) equity interest in an energy conservation joint venture (the "Project"). The Project had been awarded a contract to retrofit residential housing units at a US Army base which it completed during 1996. The completed contract was for installation of energy-efficient equipment (including air conditioning and heating equipment), which would reduce utility consumption. For the installation and management, the Project will receive an average of seventy-seven percent (77%) of all energy and maintenance savings during the twenty (20) year contract term. The Project spent approximately $17.5 million to retrofit the residential housing units at the US Army base. The Project received a loan from a lender to finance approximately $14.0 million of the cost of the Project. The Company is not guaranteeing any of the lending obligations of the Project.

During 1995, the Company executed a stock option agreement to acquire eighty percent (80%) of the stock of a specialty sales organization ("Optioned Company"), which owns the remaining fifty percent (50%) equity interest in the Project discussed above, to enhance the marketing of the Company's air conditioning products. The stock option has a four (4) year term, and a total option granting price of $1.0 million and annual $100,000 payments for yearly extensions of the stock option thereafter for up to three (3) years. The Company is currently negotiating to extend the Option expiration date. Through the date of this report the Company has made option payments aggregating $1.3 million and has loaned the Optioned Company approximately $1.4 million. The Company has recorded reserves of $1.3 million against the loans and option payments. Upon exercise of the stock option by the Company, or upon the occurrence of certain performance criteria which would give the grantors of the stock option the right to accelerate the date on which the Company must elect whether to exercise, the Company shall pay certain cash and issue promissory notes for the balance of the exercise price of the subject shares. The total exercise price of the subject shares is $4.0 million, less the amounts paid for the granting and any extensions of the stock option. As of the date of this report, no decision to exercise this option has been reached by the Company.

Debt Guarantee

At December 31, 1998, the Company and one of its subsidiaries had outstanding guarantees of approximately $2.6 million of indebtedness of a startup aviation company in exchange for an ownership interest. The debt guarantee relates to two note instruments. The subsidiary has guaranteed up to $600,000 on one of the note instruments. The other note in the amount of $2.0 million requires monthly principal payments.

In 1998 and during the first quarter of 1999, the aviation company made capital calls on its shareholders. In 1998 and 1999, in contemplation of a sale of the aviation company and pursuant to such capital calls, the Company invested an additional $1,046,000 in the aviation company. This additional investment increased the Company's ownership interest to approximately 45%. The Company has reserves for losses equal to its direct investment and contingent liabilities under the guarantees.

Subsequent to December 31, 1998, the Company was called upon to perform on both guarantees. The Company paid approximately $600,000 to the lender in satisfaction of the guarantee and assumed the obligation for the $2.0 million note, which is due in equal monthly principal payments, plus interest, through August, 2004. In connection with the demand on the Company to perform under its guarantee, the Company and the other guarantors formed a new company ("KAC") and acquired the assets of the aviation company through foreclosure.

The Company and the other shareholders of KAC are attempting to sell the assets acquired in foreclosure. If they are successful in selling these assets, it is expected that the Company will recover a portion of its investment in and advances to the aviation company which have been previously fully reserved.

Availability of Company's Loss Carry-overs

The Company anticipates that its cash flow in future years will benefit from its ability to use net operating loss ("NOL") carry-overs from prior periods to reduce the federal income tax payments which it would otherwise be required to make with respect to income generated in such future years. Such benefit, if any is dependent on the Company's ability to generate taxable income in future periods, for which there is no assurance. Such benefit if any, will be limited by the Company's reduced NOL for alternative minimum tax purposes which is approximately $31.4 million at December 31, 1998. As of December 31, 1998, the Company had available regular tax NOL carry-overs of approximately $63.8 million based on its federal income tax returns as filed with the Internal Revenue Service for taxable years through 1998. These NOL carry-overs will expire beginning in the year 1999. As of December 31, 1998 and 1997, due to its recent history of reporting net losses, the Company has established a valuation allowance on a portion of its NOLs and thus has not recognized the full benefit of its NOLs in the accompanying Consolidated Financial Statements.

The amount of these carry-overs has not been audited or approved by the Internal Revenue Service and, accordingly, no assurance can be given that such carry-overs will not be reduced as a result of audits in the future. In addition, the ability of the Company to utilize these carry-overs in the future will be subject to a variety of limitations applicable to corporate taxpayers generally under both the Internal Revenue Code of 1986, as amended, and the Treasury Regulations. These include, in particular, limitations imposed by Code Section 382 and the consolidated return regulations.

Year 2000 Issues

The Year 2000 Issue is the result of computer programs being written using two digits rather than four to define the applicable year. Any of the Company's computer programs or hardware that have date-sensitive software or embedded chips may recognize a date using "00" as the Year 1900 rather than the Year 2000. This could result in a system failure or miscalculations causing disruptions of operations, including, among other things, a temporary inability to process transactions, create invoices, or engage in similar normal business activities.

Beginning in 1996, the Company undertook a project to enhance certain of its Information Technology ("IT") systems and install certain other technologically advanced communication systems to provide extended functionality for operational purposes. A major part of the Company's program was to implement a standardized IT system purchased from a national software distributor at all of the Company and subsidiary operations, and to install a Local Area Network ("LAN"). The IT system and the LAN necessitated the purchase of additional hardware, as well as software. The process implemented by the Company to advance its systems to be more "state-of-the-art" had an added benefit in that the software and hardware changes necessary to achieve the Company's goals are Year 2000 compliant.

Starting in 1996 through December 31, 1998, the Company has capitalized approximately $1.0 million in costs to accomplish its enhancement program. The capitalized costs include $425,000 in external programming costs, with the remainder representing hardware and software purchases. The Company anticipates that the remaining cost to complete this IT systems enhancement project will be less than $100,000, and such costs will be capitalized.

The Company's plan to identify and resolve the Year 2000 Issue involved the following phases: assessment, remediation, testing, and implementation. To date, the Company has fully completed its assessment of all systems that could be significantly affected by the Year 2000. Based on assessments, the Company determined that it was required to modify or replace certain portions of its software and hardware so that those systems will properly utilize dates beyond December 31, 1999. For its IT exposures which include financial, order management, and manufacturing scheduling systems, the Company is 100% complete on the assessment and remediation phases. As of the date of this report, the Company has completed its testing and has implemented its remediated systems for all of its businesses except a portion of the Industrial Products Business. The uncompleted testing and remediation procedures represent approximately 2% and 5%, respectively, of the total Year 2000 Program testing and remediation phase. Completion of the remaining testing and implementation phase is expected by August 31, 1999. The assessments also indicated that limited software and hardware (embedded chips) used in production and manufacturing systems ("operating equipment") also are at limited risk. The Company has completed its assessment and identified remedial action which will be completed in the second quarter 1999. In addition, the Company has completed its assessment of its product line and determined that the products it has sold and will continue to sell do not require remediation to be Year 2000 compliant. Accordingly, based on the Company's current assessment, the Company does not believe that the Year 2000 presents a material exposure as it relates to the Company's products.

The Company has queried its significant suppliers, subcontractors, distributors and other third parties (external agents). The Company does not have any direct system interfaces with external agents. To date, the Company is not aware of any external agent with a Year 2000 Issue that would materially impact the Company's results of operations, liquidity, or capital resources. However, the Company has no means of ensuring that external agents will be Year 2000 ready. The inability of external agents to complete their Year 2000 resolution process in a timely fashion could materially impact the Company. The effect of non-compliance by external agents is not determinable at this time.

Management of the Company believes it has an effective program in place to resolve the remaining aspects of the Year 2000 Issue applicable to its businesses in a timely manner. If the Company does not complete the remaining phases of its program, the Year 2000 Issue could have a negative impact on the operations of the Company; however, management does not believe that, under the most reasonably likely worst case scenario, such potential impact would be material.

The Company is creating contingency plans for certain critical applications. These contingency plans will involve, among other actions, manual workarounds, increasing inventories, and adjusting staffing strategies. In addition, disruptions in the economy generally resulting from Year 2000 Issues could also materially adversely affect the Company. See "Special Note Regarding Forward-Looking Statements".

Contingencies

The Company has several contingencies that could impact its liquidity in the event that the Company is unsuccessful in defending against the claimants. Although management does not anticipate that these claims will result in substantial adverse impacts on its liquidity, it is not possible to determine the outcome. The preceding sentence is a forward-looking statement that involves a number of risks and uncertainties that could cause actual results to differ materially, such as, among other factors, the following: the EIL Insurance does not provide coverage to the Company and the Chemical Business for any material claims made by the claimants, the claimants alleged damages are not covered by the EIL Policy which a court may find the Company and/or the Chemical Business liable for, such as punitive damages or penalties, a court finds the Company and/or the Chemical Business liable for damages to such claimants for a material amount in excess of the limits of coverage of the EIL Insurance or a court finds the Chemical Business liable for a material amount of damages in the antitrust lawsuits pending against the Chemical Business in a manner not presently anticipated by the Company. See "Business", "Legal Proceedings" and Note 10 of Notes to Consolidated Financial Statements.

Item 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

General

The Company's results of operations and operating cash flows are impacted by changes in market interest rates and raw material prices for products used in its manufacturing processes. The Company also has a wholly-owned subsidiary in Australia, for which the Company has foreign currency translation exposure. The derivative contracts used by the Company are entered into to hedge these risks and exposures and not for trading purposes. All information is presented in U.S. dollars. See Item 1. - "Business - - - Chemical" for a discussion of an offer to purchase the Australian subsidiary which the Company received in 1999.

Interest Rate Risk

The Company's interest rate risk exposure results from its debt portfolio which is impacted by short-term rates, primarily prime rate-based borrowings from commercial banks, and long-term rates, primarily fixed-rate notes, some if which prohibit prepayment or require substantial prepayment penalties.

The Company is also a party to a series of agreements under which, upon completion of construction, it will lease a nitric acid plant. The minimum lease payments associated therewith until execution will be directly impacted by the change in interest rates. To mitigate a portion of the Company's exposure to adverse market changes related to this leveraged lease, in 1997 the Company entered into a interest rate forward agreement whereby the Company is the fixed rate payor on notional amounts aggregating $25 million, net to its 50% interest, with a weighted average of 7.12%. The Company accounts for this forward under the deferral method, so long as high correlation is maintained, whereby the net gain or loss upon settlement will adjust the item being hedged, the minimum lease rentals, in periods commencing with the lease execution. As of December 31, 1998, the fair value of this interest rate forward agreement represented a liability of approximately $3.3 million, net to the Company's 50% interest. The following table provides information about the Company's interest rate sensitive financial instruments as of December 31, 1998.

	Years Ending December 31, 1999	2000	2001	2002	2003	Thereafter through 2007	Total
Expected maturities of long-term debt:							
Variable rate debt	$ 5,725	$26,969	$ 272	$ 116	$ 126	$ 1,009	$ 34,217
Weighted averages interest rate(1)	8.05%	8.13%	8.28%	8.25%	8.25%	8.25%	8.10%
Fixed rate debt	$ 8,229	$ 9,852	$7,641	$2,813	$ 550	$106,340	$135,425
Weighted average interest rate(2)	10.44%	10.51%	10.61%	10.69%	10.72%	10.74%	10.65%

(1) Interest rate is based on the aggregate rate of debt outstanding as of December 31, 1998. Interest is at floating rate based on the lender's prime rate plus percentages ranging from .5% to 1.5% per annum, or at the Company's option, on its Revolving Credit Agreements on the lender's LIBOR rate plus 2.875% per annum (rates under its Revolving Credit Agreements are subject to change based upon specified availability and adjusted tangible net worth levels).

(2) Interest rate is based on the aggregate rate of debt outstanding as of December 31, 1998.

As of December 31, 1998, the Company's variable rate and fixed rate debt which aggregated $169.6 million approximated their fair value. The fair value of the Company's Senior Notes was determined based on a market quotation for such securities.

Raw Material Price Risk

The Company enters into long-term supply agreements with certain third parties to insure availability of certain raw materials used in its manufacturing processes. To mitigate a portion of its price risk, the Company has entered into swap agreements whereby it receives a floating price and pays a fixed price. As of December 31, 1998, the Company had outstanding natural gas contracts requiring settlement in January and February 1999 involving notional amounts of 590,000 MMBtu for which the fair value represented a liability of approximately $255,000. The Company follows the deferral method of accounting for these swap agreements.

Foreign Currency Risk

The Company has a wholly-owned subsidiary located in Australia, for which the functional currency is the local currency, the Australian dollar. Since the Australian subsidiary accounts are converted into U.S. dollars upon consolidation using the end of the period exchange rate, declines in value of the Australian dollar to the U.S. dollar result in translation loss to the Company. Additionally, any cumulative foreign currency translation loss will impact operating results in the period the Company sells or disposes of substantially all of its investment in the subsidiary. As of December 31, 1998, the Company's net investment in this Australian subsidiary was $5.8 million with the cumulative translation loss not recognized in results of operations aggregating approximately $1.6 million.

Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The Company has included the financial statements and supplementary financial information required by this item immediately following Part IV of this report and hereby incorporates by reference the relevant portions of those statements and information into this Item 8.

Item 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

No disagreements between the Company and its accountants have occurred within the 24-month period prior to the date of the Company's most recent financial statements.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements contained within this report may be deemed "Forward-Looking Statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. All statements in this report other than statements of historical fact are Forward-Looking Statements that are subject to known and unknown risks, uncertainties and other factors which could cause actual results and performance of the Company to differ materially from such statements. The words "believe", "expect", "anticipate", "intend", "will", and similar expressions identify Forward-Looking Statements. Forward-Looking Statements contained herein relate to, among other things, (i) ability to improve operations and become profitable on an annualized basis, (ii) establishing a position as a market leader, (iii) construction costs of the EDNC Baytown Plant will approximate $69 million (excluding the $12.9 million paid to subcontractors by the bonding company) and will be completed by the second quarter of 1999, (iv) ability to continue to operate the DSN Plant at the rate of approximately 285 tons per day, (v) increase demand for, and growth relating to, the Company's products, (vi) certain of the Company's product lines possibly being the most extensive offered, (vii) production of backlog, (viii) amount to be spent in 1999 relating to compliance with federal, state and local Environmental laws at the El Dorado Facility, (ix) Year 2000 issues, (x) improving liquidity and profits through liquidation of assets or realignment of assets, (xi) the Company's ability to develop or adopt new and existing technologies in the conduct of its operations, (xii) anticipated financial performance, (xiii) ability to comply with the Company's general working capital requirements, (xiv) spin-off the Automotive Products Business, (xv) ability to be able to continue to borrow under the Company's revolving line of credit, (xvi) ability to enter into a new line of credit for the Automotive Business, and (xvii) ability of the EDNC Baytown Plant to guarantee $35 to $50 million in gross revenues once operational. While the Company believes the expectations reflected in such Forward-Looking Statements are reasonable, it can give no assurance such expectations will prove to have been correct. There are a variety of factors which could cause future outcomes to differ materially from those described in this report, including, but not limited to, (i) decline in general economic conditions, both domestic and foreign, (ii) material reduction in revenues, (iii) inability to collect in a timely manner a material amount of receivables, (iv) increased competitive pressures, (v) inability to meet the "Year 2000" compliance of the computer system by the Company, its key suppliers, customers, creditors, and financial service organization, (vi) changes in federal, state and local laws and regulations, especially environmental regulations, or in interpretation of such, pending (vii) additional releases (particularly air emissions into the environment), (viii) potential increases in equipment, maintenance, operating or labor costs not presently anticipated by the Company, (ix) inability to retain management or to develop new management, (x) the requirement to use internally generated funds for purposes not presently anticipated, (xi) inability to become profitable, or if unable to become profitable, the inability to secure additional liquidity in the form of additional equity or debt, (xii) the effect of additional production capacity of anhydrous ammonia in the western hemisphere,

(xiii) the cost for the purchase of anhydrous ammonia not reducing or continuing to increase, (xiv) changes in competition, (xv) the loss of any significant customer, (xvi) changes in operating strategy or development plans, (xvii) inability to implement on a permanent basis the corrective actions necessary for the DSN Plant to operate at its stated capacity or inability to produce at the DSN Plant in an efficient manner, (xviii) inability to fund the working capital and expansion of the Company's businesses, (xix) adverse results in any of the Company's pending litigation, on claims described under "Legal Proceedings", (xx) inability to finalize the settlements of the environmental litigation in terms described in "Legal Proceedings", (xxi) inability to obtain necessary raw materials, (xxii) inability to satisfy the NYSE continued listing requirements, (xxiii) the requirement to pay a dividend on the Series B Preferred as a result of the spin-off of the Automotive Products Business, (xxiv) inability to recover the Company's investment in the aviation company, and (xxiv) other factors described in "Business", "Legal Proceedings" or "Management's Discussion and Analysis of Financial Condition and Results of Operation" contained in this report. Given these uncertainties, all parties are cautioned not to place undue reliance on such Forward-Looking Statements. The Company disclaims any obligation to update any such factors or to publicly announce the result of any revisions to any of the Forward-Looking Statements contained herein to reflect future events or developments.

PART III

The Company hereby incorporates by reference the information required by Part III of this report except for the information on the Company's executive officers included under Part 4A of Part I of this report, from the definitive proxy statement which the Company intends to file with the Securities and Exchange Commission on or before April 30, 1999, in connection with the Company's 1999 annual meeting of stockholders.

PART IV

Item 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a)(1) Financial Statements

The following consolidated financial statements of the Company appear immediately following this Part IV:

(a)(2) Financial Statement Schedule

The Company has included the following schedule in this report:

The Company has omitted all other schedules because the conditions requiring their filing do not exist or because the required information appears in the Company's Consolidated Financial Statements, including the notes to those statements.

(a)(3) Exhibits

2.1. Stock Option Agreement dated as of May 4, 1995, between optionee, LSB Holdings, Inc., an Oklahoma Corporation and the shareholders of a specialty sales organization, an option which the Company hereby incorporates hereby by reference from Exhibit 2.1 to the Company's Form 10-K for fiscal year ended December 31, 1995.

2.2. Stock Purchase Agreement and Stock Pledge Agreement between Dr. Hauri AG, a Swiss Corporation, and LSB Chemical Corp., which the Company hereby incorporates by reference from Exhibit 2.2 to the Company's Form 10-K for fiscal year ended December 31, 1994.

3.1. Restated Certificate of Incorporation, the Certificate of Designation dated February 17, 1989, and certificate of Elimination dated April 30, 1993, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Registration Statement, No. 33-61640; Certificate of Designation for the Company's $3.25 Convertible Exchangeable Class C Preferred Stock, Series 2, which the Company hereby incorporates by reference from Exhibit 4.6 to the Company's Registration Statement, No. 33-61640.

3.2. Bylaws, as amended, which the Company hereby incorporates by reference from Exhibit 3(ii) to the Company's Form 10-Q for the quarter ended June 30, 1998.

4.1. Specimen Certificate for the Company's Non-cumulative Preferred Stock, having a par value of $100 per share, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 10-Q for the quarter ended June 30, 1983.

4.2. Specimen Certificate for the Company's Series B Preferred Stock, having a par value of $100 per share, which the Company hereby incorporates by reference from Exhibit 4.27 to the Company's Registration Statement No. 33-9848.

4.3. Specimen Certificate for the Company's Series 2 Preferred, which the Company hereby incorporates by reference from Exhibit 4.5 to the Company's Registration Statement No. 33-61640.

4.4. Specimen Certificate for the Company's Common Stock, which the Company incorporates by reference from Exhibit 4.4 to the Company's Registration Statement No. 33-61640.

4.5. Renewed Rights Agreement, dated January 6, 1999, between the Company and Bank One, N.A., which the Company hereby incorporates by reference from Exhibit No. 1 to the Company's Form 8-A Registration Statement, dated January 27, 1999.

4.6. Indenture, dated as of November 26, 1997, by and among ClimaChem, Inc., the Subsidiary Guarantors and Bank One, NA, as trustee, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 8-K, dated November 26, 1997.

4.7. Form 10 3/4% Series B Senior Notes due 2007 which the Company hereby incorporates by reference from Exhibit 4.3 to the ClimaChem Registration Statement, No. 333-44905.

4.8. Amended and Restated Loan and Security Agreement, dated November 21, 1997, by and between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation which the Company hereby incorporates by reference from Exhibit 10.2 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

4.9. Amended and Restated Loan and Security Agreement, dated November 21, 1997, by and between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.11 to the Company's Form 10-K for the fiscal year ended December 31, 1997. Substantially identical Amended and Restated Loan and Security Agreements dated November 21, 1997, were entered into by each of L&S Bearing Co., and Summit Machine Tool Manufacturing Corp., with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.10. First Amendment to Amended and Restated Loan and Security Agreement, dated March 12, 1998, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation which the Company hereby incorporates by reference from Exhibit 10.53 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

4.11. First Amendment to Amended and Restated Loan and Security Agreement, dated March 12, 1998, between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.13 to the Company's Form 10-K for the fiscal year ended December 31, 1997. Substantially identical First Amendments to Amended and Restated Loan and Security Agreements, dated March 12, 1998, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.12. Third Amendment to Amended and Restated Loan and Security Agreement, dated August 14, 1998, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 10-Q for the quarter ended June 30, 1998.

4.13. Third Amendment to Amended and Restated Loan and Security Agreement, dated August 14, 1998, between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.2 to the Company's Form 10-Q for the quarter ended June 30, 1998. Substantially identical Third Amendments to Amended and Restated Loan and Security Agreements, dated August 14, 1998, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.14. Fourth Amendment to Amended and Restated Loan and Security Agreement, dated November 19, 1998, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 10-Q for the quarter ended September 30, 1998.

4.15. Fourth Amendment to Amended and Restated Loan and Security Agreement, dated November 19, 1998, between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.2 to the Company's Form 10-Q for the quarter ended September 30, 1998. Substantially identical Fourth Amendments to Amended and Restated Loan and Security Agreements, dated November 19, 1998, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.16. Fifth Amendment to Amended and Restated Loan and Security Agreement, dated April 8, 1999, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation.

4.17. Fifth Amendment to Amended and Restated Loan and Security Agreement, dated April 8, 1999, between BankAmerica Business Credit, Inc., and the Company. Substantially identical Fifth Amendments to Amended and Restated Loan and Security Agreements, dated April 8, 1999, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.18. Waiver Letter, dated March 16, 1998, from BankAmerica Business Credit, Inc. which the Company hereby incorporates by reference from Exhibit 10.55 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

4.19. First Supplemental Indenture, dated February 8, 1999, by and between ClimaChem, Inc., the Guarantors, and Bank One, N.A.

10.1. Form of Death Benefit Plan Agreement between the Company and the employees covered under the plan, which the Company hereby incorporates by reference from Exhibit 10(c)(1) to the Company's Form 10-K for the year ended December 31, 1980.

10.2. The Company's 1981 Incentive Stock Option Plan, as amended, and 1986 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibits 10.1 and 10.2 to the Company's Registration Statement No. 33-8302.

10.3. Form of Incentive Stock Option Agreement between the Company and employees as to the Company's 1981 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibit 10.10 to the Company's Form 10-K for the fiscal year ended December 31, 1984.

10.4. Form of Incentive Stock Option Agreement between the Company and employees as to the Company's 1986 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibit 10.6 to the Company's Registration Statement No. 33-9848.

10.5. The 1987 Amendments to the Company's 1981 Incentive Stock Option Plan and 1986 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-K for the fiscal year ended December 31, 1986.

10.6. The Company's 1993 Stock Option and Incentive Plan which the Company hereby incorporates by reference from Exhibit 10.6 to the Company's Form 10-K for the fiscal year ended December 31, 1993.

10.7. The Company's 1993 Non-employee Director Stock Option Plan which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-K for the fiscal year ended December 31, 1993.

10.8. Union Contracts, dated August 5, 1995, between EDC and the Oil, Chemical and Atomic Workers, and the United Steel Workers of America, dated November 1, 1995 which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-K for the fiscal year ended December 31, 1995.

10.9. Lease Agreement, dated March 26, 1982, between Mac Venture, Ltd. and Hercules Energy Mfg. Corporation, which the Company hereby incorporates by reference from Exhibit 10.32 to the Company's Form 10-K for the fiscal year ended December 31, 1981.

10.10. Limited Partnership Agreement dated as of May 4, 1995, between the general partner, and LSB Holdings, Inc., an Oklahoma Corporation, as limited partner which the Company hereby incorporates by reference from Exhibit 10.11 to the Company's Form 10-K for the fiscal year ended December 31, 1995.

10.11. Lease Agreement dated November 12, 1987, between Climate Master, Inc. and West Point Company and amendments thereto, which the Company hereby incorporates by reference from Exhibits 10.32, 10.36, and 10.37, to the Company's Form 10-K for fiscal year ended December 31, 1988.

10.12. Severance Agreement, dated January 17, 1989, between the Company and Jack E. Golsen, which the Company hereby incorporates by reference from Exhibit 10.48 to the Company's Form 10-K for fiscal year ended December 31, 1988. The Company also entered into identical agreements with Tony M. Shelby, David R. Goss, Barry H. Golsen, David M. Shear, and Jim D. Jones and the Company will provide copies thereof to the Commission upon request.

10.13. Third Amendment to Lease Agreement, dated as of December 31, 1987, between Mac Venture, Ltd. and Hercules Energy Mfg. Corporation, which the Company hereby incorporates by reference from Exhibit 10.49 to the Company's Form 10-K for fiscal year ended December 31, 1988.

10.14. Employment Agreement and Amendment to Severance Agreement dated January 12, 1989 between the Company and Jack E. Golsen, dated March 21, 1996 which the Company hereby incorporates by reference from Exhibit 10.15 to the Company's Form 10-K for fiscal year ended December 31, 1995.

10.15. Non-Qualified Stock Option Agreement, dated June 1, 1992, between the Company and Robert C. Brown, M.D. which the Company hereby incorporates by reference from Exhibit 10.38 to the Company's Form 10-K for fiscal year ended December 31, 1992. The Company entered into substantially identical agreements with Bernard G. Ille, Jerome D. Shaffer and C.L.Thurman, and the Company will provide copies thereof to the Commission upon request.

10.16. Loan and Security Agreement (DSN Plant) dated October 31, 1994 between DSN Corporation and The CIT Group which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended September 30, 1994.

10.17. Loan and Security Agreement (Mixed Acid Plant) dated April 5, 1995 between DSN Corporation and The CIT Group, which the Company hereby incorporates by reference from Exhibit 10.25 to the Company's Form 10-K for the fiscal year ended December 31, 1994.

10.18. First Amendment to Loan and Security Agreement (DSN Plant), dated June 1, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.13 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.19. First Amendment to Loan and Security Agreement (Mixed Acid Plant), dated November 15, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.15 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.20 Loan and Security Agreement (Rail Tank Cars), dated November 15, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.16 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.21. First Amendment to Loan and Security Agreement (Rail Tank Cars), dated November 15, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.17 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.22. Letter Amendment, dated May 14, 1997, to Loan and Security Agreement between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended March 31, 1997.

10.23. Amendment to Loan and Security Agreement, dated November 21, 1997, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.19 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.24. First Amendment to Non-Qualified Stock Option Agreement, dated March 2, 1994, and Second Amendment to Stock Option Agreement, dated April 3, 1995, each between the Company and Jack E. Golsen, which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended March 31, 1995.

10.25. Facility Letter, dated August 20, 1997, between Bank of New Zealand, Australia, and Total Energy Systems Limited which the Company hereby incorporates by reference from Exhibit 10.38 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.26. Variation Letter, dated February 10, 1998, between Bank of New Zealand, Australia, and Total Energy Systems Limited which the Company hereby incorporates by reference from Exhibit 10.39 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.27. Debenture Charge, dated March 7, 1995, between Total Energy Systems Limited and Bank of New Zealand which the Company hereby incorporates by reference from Exhibit 10.40 to the ClimaChem Form S-4 Registration Statement, No. 333-44905. T.E.S. Mining Services Pty. Ltd. and Total Energy Systems (NZ) Limited are each parties to substantially identical Debentures, copies of which will be provided to the Commission upon request.

10.28. Anhydrous Ammonia Sales Agreement, dated May 28, 1997, to be effective January 1, 1997, between Koch Nitrogen Company and El Dorado Chemical Company which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.29. Baytown Nitric Acid Project and Supply Agreement dated June 27, 1997, by and among El Dorado Nitrogen Company, El Dorado Chemical Company and Bayer Corporation which the Company hereby incorporates by reference from Exhibit 10.2 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.30. First Amendment to Baytown Nitric Acid Project and Supply Agreement, dated February 1, 1999, between El Dorado Nitrogen Company, El Dorado Chemical Company, and Bayer Corporation. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION UNDER THE FREEDOM OF INFORMATION ACT. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

10.31. Service Agreement, dated June 27, 1997, between Bayer Corporation and El Dorado Nitrogen Company which the Company hereby incorporates by reference from Exhibit 10.3 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.32. Ground Lease dated June 27, 1997, between Bayer Corporation and El Dorado Nitrogen Company which the Company hereby incorporates by reference from Exhibit 10.4 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.33. Participation Agreement, dated as of June 27, 1997, among El Dorado Nitrogen Company, Boatmen's Trust Company of Texas as Owner Trustee, Security Pacific Leasing corporation, as Owner Participant and a Construction Lender, Wilmington Trust Company, Bayerische Landesbank, New York Branch, as a Construction Lender and the Note Purchaser, and Bank of America National Trust and Savings Association, as Construction Loan Agent which the Company hereby incorporates by reference from Exhibit 10.5 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.34. Lease Agreement, dated as of June 27, 1997, between Boatmen's Trust Company of Texas as Owner Trustee and El Dorado Nitrogen

Company which the Company hereby incorporates by reference from Exhibit 10.6 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997.

10.35. Security Agreement and Collateral Assignment of Construction Documents, dated as of June 27, 1997, made by El Dorado Nitrogen Company which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997.

10.36. Security Agreement and Collateral Assignment of Facility Documents, dated as of June 27, 1997, made by El Dorado Nitrogen Company and consented to by Bayer Corporation which the Company hereby incorporates by reference from Exhibit 10.8 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997.

10.37. Amendment to Loan and Security Agreement, dated March 16, 1998, between The CIT Group/Equipment Financing, Inc., and DSN Corporation which the Company hereby incorporates by reference from Exhibit 10.54 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.38. Fifth Amendment to Lease Agreement, dated as of December 31, 1998, between Mac Venture, Ltd. and Hercules Energy Mfg. Corporation.

10.39. Sales Contract, dated December 7, 1998, between Solutia, Inc. and El Dorado Chemical Company. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION UNDER THE FREEDOM OF INFORMATION ACT. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

10.40. Agreement for Purchase and Sale of Anhydrous Ammonia, dated January 1, 1999, between El Dorado Chemical Company and Farmland Industries, Inc. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION UNDER THE FREEDOM OF INFORMATION ACT. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

10.41. Agreement, dated March 23, 1999, among El Dorado Chemical Company, El Dorado Nitrogen Company, Bayer Corporation, ICF Kaiser Engineers, Inc., ICF Kaiser International, Inc., and Acstar Insurance Company.

10.42. Union Contract, dated August 1, 1998, between El Dorado Chemical Company and the International Association of Machinists and Aerospace Workers.

10.43. Non-Qualified Stock Option Agreement, dated April 22, 1998, between the Company and Robert C. Brown, M.D. The Company entered into substantially identical agreements with Bernard G. Ille, Jerome D. Shaffer, Raymond B. Ackerman, Horace G. Rhodes, Gerald J. Gagner, and Donald W. Munson. The Company will provide copies of these agreements to the Commission upon request.

10.44. The Company's 1998 Stock Option and Incentive Plan.

10.45. Letter Agreement, dated March 12, 1999, between Kestrel Aircraft Company and LSB Industries, Inc., Prime Financial Corporation, Herman Meinders, Carlan K. Yates, Larry H. Lemon, Co-Trustee Larry H. Lemon Living Trust.

10.46. Covenant Waiver Letter, dated April 13, 1999, between The CIT Group and DSN Corporation.

21.1. Subsidiaries of the Company

23.1. Consent of Independent Auditors

27.1. Financial Data Schedule

(b) Reports on Form 8-K. The Company did not file any reports on Form 8-K during the fourth quarter of 1998.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, as amended, the Company has caused the undersigned, duly-authorized, to sign this report on its behalf of this 15th day of April, 1999.

LSB INDUSTRIES, INC.

By: /s/ Jack E. Golsen
____
Jack E. Golsen
Chairman of the Board and
President
(Principal Executive Officer)

By: /s/ Tony M. Shelby
____
Tony M. Shelby
Senior Vice President of Finance
(Principal Financial Officer)

By: /s/ Jim D. Jones
____
Jim D. Jones
Vice President, Controller and
Treasurer (Principal Accounting
Officer)

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the undersigned have signed this report on behalf of the Company, in the capacities and on the dates indicated.

Dated: April 15, 1999 By: /s/ Jack E. Golsen
____
Jack E. Golsen, Director

Dated: April 15, 1999 By: /s/ Tony M. Shelby
____
Tony M. Shelby, Director

Dated: April 15, 1999 By: /s/ David R. Goss
____
David R. Goss, Director

Dated: April 15, 1999 By: /s/ Barry H. Golsen
____
Barry H. Golsen, Director

Dated: April 15, 1999 By: /s/ Robert C. Brown

Robert C. Brown, Director

Dated: April 15, 1999 By: /s/ Bernard G. Ille

Bernard G. Ille, Director

Dated: April 15, 1999 By: /s/ Jerome D. Shaffer

Jerome D. Shaffer, Director

Dated: April 15, 1999 By: /s/ Raymond B. Ackerman

Raymond B. Ackerman, Director

Dated: April 15, 1999 By: /s/ Horace Rhodes

Horace Rhodes, Director.

Dated: April 15, 1999 By: /s/ Gerald J. Gagner

Gerald J. Gagner, Director

Dated: April 15, 1999 By: /s/ Donald W. Munson

Donald W. Munson, Director

LSB INDUSTRIES, INC.

Consolidated Financial Statements

Years ended December 31, 1998, 1997, and 1996

Contents

Report of Independent Auditors

The Board of Directors and Stockholders
LSB Industries, Inc.

We have audited the accompanying consolidated balance sheets of LSB Industries, Inc. as of December 31, 1998 and 1997, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 1998. Our audits also included the financial statement schedule listed in the Index at Item 14(a)(2). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and schedule based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of LSB Industries, Inc. at December 31, 1998 and 1997, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 1998, in conformity with generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ Ernst & Young LLP

ERNST & YOUNG LLP

Oklahoma City, Oklahoma
February 19, 1999,
except for paragraphs (A) and (C) of Note 5 and Note 14, as to which the date is
April 14, 1999

LSB INDUSTRIES, INC.

Consolidated Balance Sheets

	December 31 1998	1997
	(In Thousands)	
Assets		
Current assets (Note 5):		
Cash and cash equivalents	$ 1,555	$ 4,934
Trade accounts receivable, net	52,730	52,191
Inventories (Note 3)	63,845	66,374
Supplies and prepaid items	7,809	7,595
Total current assets	125,939	131,094
Property, plant and equipment, net (Notes 4 and 5)	99,228	119,331
Other assets, net	23,480	21,228
	$248,647	$270,653

(Continued on following page)

LSB INDUSTRIES, INC.

Consolidated Balance Sheets (continued)

	December 31 1998	1997
	(In Thousands)	
Liabilities and stockholders' equity		
Current liabilities:		
Drafts payable	$ 758	$ 737
Accounts payable	24,043	28,137
Accrued liabilities	19,006	16,196
Current portion of long-term debt (Note 5)	13,954	15,874
Total current liabilities	57,761	60,944
Long-term debt (Note 5)	155,688	165,067
Commitments and contingencies (Note 10)		
Redeemable, noncumulative, convertible preferred stock, $100 par value; 1,463 shares issued and outstanding (1,539 in 1997) (Note 8)	139	146
Stockholders' equity (Notes 5, 7 and 9):		
Series B 12% cumulative, convertible, preferred stock, $100 par value; 20,000 shares issued and outstanding	2,000	2,000
Series 2 $3.25 convertible, exchangeable Class C preferred stock, $50 stated value; 920,000 shares issued	46,000	46,000
Common stock, $.10 par value; 75,000,000 shares authorized, 15,108,676 shares issued (15,042,356 in 1997)	1,511	1,504
Capital in excess of par value	38,329	38,257
Accumulated other comprehensive loss	(1,559)	(1,003)
Accumulated deficit	(35,166)	(29,773)
	51,115	56,985
Less treasury stock, at cost:		
Series 2 preferred, 5,000 shares	200	200
Common stock, 3,202,690 shares (2,293,390 in 1997)	15,856	12,289
Total stockholders' equity	35,059	44,496
	$248,647	$270,653

See accompanying notes.

LSB Industries, Inc.

Consolidated Statements of Operations

	Year ended December 31, 1998	1997	1996
	(In Thousands, Except Per Share Amounts)		
Revenues:			
Net sales	$310,037	$313,929	$307,160
Other income	1,290	5,167	6,265
Gain on sale of The Tower (Note 2)	12,993	-	-
	324,320	319,096	313,425
Costs and expenses:			
Cost of sales	247,084	257,982	250,388
Selling, general and administrative	61,729	64,770	56,715
Interest	17,327	14,740	10,017
	326,140	337,492	317,120
Loss before provision for income taxes and extra-ordinary charge	(1,820)	(18,396)	(3,695)
Provision for income taxes (Note 6)	100	50	150
Loss before extraordinary charge	(1,920)	(18,446)	(3,845)
Extraordinary charge	-	4,619	-
Net loss	(1,920)	(23,065)	(3,845)
Preferred stock dividends	3,229	3,229	3,229
Net loss applicable to common stock	$ (5,149)	$(26,294)	$ (7,074)
Loss per common share--basic and diluted:			
Loss before extraordinary charge	$(.42)	$(1.68)	$(.55)
Extraordinary charge	-	(.36)	-
Net loss	$(.42)	$(2.04)	$(.55)

See accompanying notes.

LSB Industries, Inc.

Consolidated Statements of Stockholders' Equity

	Common Stock		Non-redeemable Preferred Stock	Capital in Excess of Par Value
	Shares	Par Value		
Balance at December 31, 1995	14,757	$1,476	$48,000	$37,567
Net loss	-	-	-	-
Foreign currency translation adjustment	-	-	-	-
Total comprehensive loss				
Conversion of 27 shares of redeemable preferred stock to common stock	1	-	-	2
Exercise of stock options:				
Cash received	85	8	-	185
Stock tendered and added to treasury at market value	45	5	-	89
Dividends declared:				
Series B 12% preferred stock ($12.00 per share)	-	-	-	-
Redeemable preferred stock ($10.00 per share)	-	-	-	-
Common stock ($.06 per share)	-	-	-	-
Series 2 preferred stock ($3.25 per share)	-	-	-	-
Purchase of treasury stock	-	-	-	-
Balance at December 31, 1996	14,888	1,489	48,000	37,843

(Continued on following page)

Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Accumulated) Deficit)	Treasury Stock-- Common	Treasury Stock-- Preferred	Total
(In Thousands)				
$ 278	$ 5,148	$(10,415)	$ (200)	$ 81,854
-	(3,845)	-	-	(3,845)
(2)	-	-	-	(2)
				(3,847)
-	-	-	-	2
-	-	-	-	193
-	-	(94)	-	-
-	(240)	-	-	(240)
-	(16)	-	-	(16)
-	(780)	-	-	(780)
-	(2,973)	-	-	(2,973)
-	-	(175)	-	(175)
276	(2,706)	(10,684)	(200)	74,018

LSB Industries, Inc.

Consolidated Statements of Stockholders' Equity (continued)

	Common Stock Shares	Common Stock Par Value	Non-redeemable Preferred Stock	Capital in Excess of Par Value
Net loss	-	$ -	$ -	$ -
Foreign currency translation adjustment	-	-	-	-
Total comprehensive loss				
Exercise of stock options:				
Cash received	67	6	-	190
Stock tendered and added to treasury at market value	87	9	-	224
Dividends declared:				
Series B 12% preferred stock ($12.00 per share)	-	-	-	-
Redeemable preferred stock ($10.00 per share)	-	-	-	-
Common stock ($.06 per share)	-	-	-	-
Series 2 preferred stock ($3.25 per share)	-	-	-	-
Purchase of treasury stock	-	-	-	-
Balance at December 31, 1997	15,042	1,504	48,000	38,257
Net loss	-	-	-	-
Foreign currency translation adjustment	-	-	-	-
Total comprehensive loss				
Conversion of 76.5 shares of redeemable preferred stock to common stock	3	-	-	7
Exercise of stock options:				
Cash received	64	7	-	65
Dividends declared:				
Series B 12% preferred stock ($12.00 per share)	-	-	-	-
Redeemable preferred stock ($10.00 per share)	-	-	-	-
Common stock ($.02 per share)	-	-	-	-
Series 2 preferred stock ($3.25 per share)	-	-	-	-
Purchase of treasury stock	-	-	-	-
Balance at December 31, 1998	15,109	1,511	48,000	38,329

(See accompanying notes)

Accumulated Other Comprehensive Income (Loss)	Retained Earnings (Accumulated) Deficit)	Treasury Stock--Common	Treasury Stock--Preferred	Total
(In Thousands)				
$ -	$(23,065)	$ -	$ -	$(23,065)
(1,279)	-	-	-	(1,279)
				(24,344)
-	-	-	-	196
-	-	(233)	-	-
-	(240)	-	-	(240)
-	(16)	-	-	(16)
-	(773)	-	-	(773)
-	(2,973)	-	-	(2,973)
-	-	(1,372)	-	(1,372)
(1,003)	(29,773)	(12,289)	(200)	44,496
-	(1,920)	-	-	(1,920)
(556)	-	-	-	(556)
				(2,476)
-	-	-	-	7
-	-	-	-	72
-	(240)	-	-	(240)
-	(16)	-	-	(16)
-	(244)	-	-	(244)
-	(2,973)	-	-	(2,973)
-	-	(3,567)	-	(3,567)
$(1,559)	$(35,166)	$(15,856)	$(200)	$35,059

LSB Industries, Inc.

Consolidated Statements of Cash Flows

	Year ended December 31, 1998	1997	1996
	(In Thousands)		
Cash flows from operating activities			
Net loss	$(1,920)	$(23,065)	$ (3,845)
Adjustments to reconcile net loss to net cash provided (used) by operations:			
Extraordinary charge related to financing activities	-	4,619	-
Depreciation of property, plant and equipment	11,651	11,142	8,655
Amortization	1,549	1,308	1,124
Provision for possible losses:			
Accounts receivable	1,544	1,544	1,450
Inventory	173	68	578
Notes receivable	1,480	1,093	1,565
Environmental matters	-	300	100
Loan guarantee	1,662	1,093	626
Recapture of prior period provisions for loss on loans receivable secured by real estate and other	(1,081)	(1,383)	-
Loss (gain) on sale of assets	(13,872)	57	(1,574)
Cash provided (used) by changes in assets and liabilities:			
Trade accounts receivable	(2,301)	(3,805)	(8,267)
Inventories	1,341	(1,960)	(2,295)
Supplies and prepaid items	(1,010)	(476)	(1,533)
Accounts payable	(4,016)	(13,549)	13,288
Accrued liabilities	559	2,530	3,441
Net cash provided (used) by operating activities	(4,241)	(20,484)	13,313
Cash flows from investing activities			
Capital expenditures	(9,620)	(12,633)	(19,950)
Principal payments on loans receivable	427	283	742
Proceeds from sale of The Tower, sales of equipment and real estate properties	31,057	1,957	417
Proceeds from the sale of investment securities	-	-	1,524
Other assets	(2,082)	(5,293)	(3,745)
Net cash provided (used) by investing activities	19,782	(15,686)	(21,012)

(Continued on following page)

LSB INDUSTRIES, INC.

Consolidated Statements of Cash Flows (continued)

	Year ended December 31, 1998	1997	1996
	(In Thousands)		
Cash flows from financing activities			
Payments on long-term and other debt	$(20,338)	$(75,846)	$(11,985)
Long-term and other borrowings, net of origination fees	617	162,451	25,029
Debt prepayment charge	-	(4,619)	-
Net change in revolving debt facilities	7,748	(37,525)	(1,266)
Net change in drafts payable	21	201	112
Dividends paid:			
Preferred stocks	(3,229)	(3,229)	(3,229)
Common stock	(244)	(773)	(780)
Purchase of treasury stock	(3,567)	(1,372)	(175)
Net proceeds from issuance of common stock	72	196	193
Net cash provided (used) by financing activities	(18,920)	39,484	7,899
Net increase (decrease) in cash and cash equivalents from all activities	(3,379)	3,314	200
Cash and cash equivalents at beginning of year	4,934	1,620	1,420
Cash and cash equivalents at end of year	$ 1,555	$ 4,934	$ 1,620

See accompanying notes.

1. Basis of Presentation

The accompanying consolidated financial statements include the accounts of LSB Industries, Inc. (the "Company") and its subsidiaries. The Company is a diversified holding company which is engaged, through its subsidiaries, in the manufacture and sale of chemical products (the "Chemical Business"), the manufacture and sale of a broad range of air handling and heat pump products (the "Climate Control Business"), the manufacture or purchase and sale of certain automotive products (the "Automotive Business") and the purchase and sale of machine tools (the "Industrial Products Business"). See Note 13 Segment Information.

All material intercompany accounts and transactions have been eliminated. Certain reclassifications have been made to the financial statements for the years ended December 31, 1997 and 1996 to conform to the consolidated financial statement presentation for the year ended December 31, 1998.

2. Accounting Policies

Use of Estimates

The preparation of consolidated financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Inventories

Purchased machinery and equipment are carried at specific cost plus duty, freight and other charges, not in excess of net realizable value. All other inventory is priced at the lower of cost or market, with cost being determined using the first-in, first-out (FIFO) basis, except for certain heat pump products with a value of $7,095,000 at December 31, 1998 ($8,151,000 at December 31, 1997), which are priced at the lower of cost or market, with cost being determined using the last-in, first-out (LIFO) basis. The difference between the LIFO basis and current cost was $1,062,000 and $1,223,000 at December 31, 1998 and 1997, respectively.

Depreciation

For financial reporting purposes, depreciation is primarily computed using the straight-line method over the estimated useful lives of the assets.

2. Accounting Policies (continued)

Capitalization of Interest

Interest costs of $1,113,000 and $2,405,000 related to the construction of a nitric acid plant were capitalized in 1997 and 1996, respectively (none in 1998), and are amortized over the plant's estimated useful life.

Loans Receivable

In February 1997, a subsidiary of the Company foreclosed on a loan receivable with a carrying amount of $14.0 million and exercised its option to acquire the related office building located in Oklahoma City, known as "The Tower."

In March 1998, the subsidiary closed the sale of The Tower and realized proceeds of approximately $29.3 million from the sale, net of transaction costs. Proceeds from the sale were used to retire the outstanding indebtedness of approximately $13 million in March 1998, for which this property served as collateral. Approximately $15 million of the remaining proceeds were used to reduce indebtedness outstanding under the Company's Revolving Credit Facility. The Company recognized a gain on the sale of the property of approximately $13 million in the first quarter of 1998.

Excess of Purchase Price Over Net Assets Acquired

The excess of purchase price over net assets acquired, which is included in other assets in the accompanying balance sheets, were $2,895,000 and $3,287,000, net of accumulated amortization, of $4,033,000 and $3,641,000 at December 31, 1998 and 1997, respectively, and is amortized by the straight-line method over periods of 10 to 22 years. The carrying value of the excess of purchase price over net assets acquired is reviewed (using estimated future net cash flows, including proceeds from disposal) if the facts and circumstances indicate that it may be impaired. No significant impairment provisions were required in 1998, 1997 or 1996.

Debt Issuance Costs

Debt issuance costs are amortized over the term of the associated debt instrument using the straight-line method. Such costs, which are included in other assets in the accompanying balance sheets, were $4,084,000 and $4,272,000 net of accumulated amortization of $1,141,000 and $683,000 as of December 31, 1998 and 1997, respectively.

2. Accounting Policies (continued)

Research and Development Costs

Costs incurred in connection with product research and development are expensed as incurred. Such costs amounted to $409,000 in 1998, $394,000 in 1997 and $532,000 in 1996.

Advertising Costs

Costs incurred in connection with advertising and promotion of the Company's products are expensed as incurred. Such costs amounted to $2,123,000 in 1998, $2,430,000 in 1997 and $1,814,000 in 1996.

Translation of Foreign Currency

Assets and liabilities of foreign operations, where the functional currency is the local currency, are translated into U.S. dollars at the fiscal year end exchange rate. The related translation adjustments are recorded as cumulative translation adjustments, a separate component of stockholders' equity. Revenues and expenses are translated using average exchange rates prevailing during the year.

Hedging

In 1997, the Company entered into interest rate forward contracts to effectively fix the interest rate on a long-term lease commitment to become effective in 1999 (not for trading purposes). The Company accounts for these contracts under the deferral method, whereby the net gain or loss upon settlement will adjust the item being hedged, the minimum lease rentals, in periods commencing with the lease execution. If the necessary correlation (generally a correlation coefficient of between 80% and 125%) ceases, the differential between the market value and the carrying value will be recognized in operations as a gain or loss. Under the interest rate forward agreement, the Company is the fixed rate payor on notional amounts aggregating $50 million with a weighted average interest rate of 7.12%. The agreement requires a net settlement on maturity in 1999, of which an unrelated third party is contractually obligated for 50%. The Company is required to post margin in the form of bank letters of credit or treasury bills under this interest rate hedge agreement equal to the loss in market value of the contracts since inception. See Note 10 -- Commitments and Contingencies and Note 12 -- Fair Value of Financial Instruments.

2. Accounting Policies (continued)

In August 1998, the Company entered into a three month natural gas swap agreement at a price of $2.56 per MMBtu for the months of December 1998 through February 1999 to hedge the price volatility of ammonia (not for trading purposes). Under these swap agreements, the Company is the fixed-price payor. Monthly payments are made or received based on the differential between the fixed price and the specified index price of natural gas on the settlement date. Gains or losses resulting from the settlement of the swap transactions are recognized in cost of sales when the inventory is sold. At December 31, 1998, the Company had outstanding commodity contracts involving notional amounts of 590,000 MMBtu that are not reflected in the accompanying balance sheet. These notional amounts do not represent amounts exchanged by the parties; rather, they are used as the basis to calculate the amounts due under the agreements.

Loss Per Share

Net loss applicable to common stock is computed by adjusting net loss by the amount of preferred stock dividends. Basic loss per common share is based upon the weighted average number of common shares outstanding during each period after giving appropriate effect to preferred stock dividends. Diluted loss per share is based on the weighted average number of common shares and dilutive common equivalent shares outstanding, if any, and the assumed conversion of dilutive convertible securities outstanding, if any, after appropriate adjustment for interest, net of related income tax effects on convertible notes payable, as applicable. All potentially dilutive securities were antidilutive for all periods presented and have thus, been excluded from diluted loss per share. See Note 7 -- Stockholders' Equity, Note 8 -- Redeemable Preferred Stock, and Note 9 -- Non-redeemable Preferred Stock for a full description of securities which may have a dilutive effect in future periods.

Average common shares outstanding used in computing loss per share are as follows:

	1998	1997	1996
Basic and diluted	12,372,770	12,876,064	12,925,649

Changes in Accounting

Effective January 1, 1998, the Company adopted Statement of Financial Accounting Standards No. 130, "Reporting Comprehensive Income" ("SFAS 130"). The provisions of SFAS 130 require the Company to classify items of other comprehensive income in the financial statements

2. Accounting Policies (continued)

and display the accumulated balance of other comprehensive income separately from retained earnings and additional paid-in capital in the equity section of the balance sheet. The Company has also made similar reclassifications for all prior periods for comparative purposes.

Effective January 1, 1998, the Company changed its method of accounting for the costs of computer software developed for internal use to capitalize costs incurred after the preliminary project stage as outlined in Statement of Position 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use" ("SOP 98-1"). These capitalized costs will be amortized over their estimated useful life. Prior to 1998, these costs were expensed as incurred. The effect of this change on net income for the year ended December 31, 1998 was not material.

Effective January 1, 1998, the Company adopted the Financial Accounting Standards Board's Statement of Financial Accounting Standards No. 131, "Disclosures about Segments of an Enterprise and Related Information" (Statement 131). Statement 131 superseded FASB Statement No. 14, "Financial Reporting for Segments of a Business Enterprise." Statement 131 establishes standards for the way that public business enterprises report information about operating segments in annual financial statements and requires that those enterprises report selected information about operating segments in interim financial reports. Statement 131 also establishes standards for related disclosures about products and services, geographic areas, and major customers. The adoption of Statement 131 did not affect results of operations or financial position, but did affect the disclosure of segment information (Note 13).

Recently Issued Pronouncements

In the second quarter of 1998, the Accounting Standards Executive Committee of the Securities and Exchange Commission released Statement of Position 98-5, "Reporting on the Costs of Start-up Activities" ("SOP 98-5"). SOP 98-5 requires that the costs of start-up activities, including organization costs, be expensed as incurred. As of December 31, 1998, the start-up costs capitalized on the balance sheet are immaterial. SOP 98-5 is effective for fiscal years ending after December 15, 1998 and, accordingly, will be adopted January 1, 1999.

In June 1998, the Financial Accounting Standards Board issued Statement No. 133 ("SFAS 133"), "Accounting for Derivative Instruments and Hedging Activities," which is required to be adopted in years beginning after June 15, 1999. The Statement permits early adoption as of the beginning of any fiscal quarter after its issuance. The Company expects to adopt this new Statement January 1, 2000. The Statement will require the Company to recognize all derivatives on the balance sheet at fair value. Derivatives that are not hedges must be adjusted to fair value

2. Accounting Policies (continued)

through income. If the derivative is a hedge, depending on the nature of the hedge, changes in the fair value of derivatives will either be offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative's change in fair value will be immediately recognized in earnings. The Company has not yet determined what all of the effects of SFAS 133 will be on the earnings and financial position of the Company; however, the Company expects that the interest rate forward contracts, discussed under Accounting Policies   Hedging, will be accounted for as a cash flow hedge upon adoption of SFAS 133, with the effective portion of the hedge being classified in equity in accumulated other comprehensive income or loss. The amount included in accumulated other comprehensive income or loss will be amortized to operations over the initial term of the leveraged lease.

Statements of Cash Flows

For purposes of reporting cash flows, cash and cash equivalents include cash, overnight funds and interest bearing deposits with maturities when purchased by the Company of 90 days or less.

Supplemental cash flow information includes:

	1998	1997	1996
	(In Thousands)		
Cash payments for:			
Interest on long-term debt and other	$17,333	$14,804	$12,038
Income taxes, net of refunds	65	86	345
Noncash financing and investing activities-			
Long-term debt issued for property, plant and equipment	523	1,108	2,226

3. Inventories

Inventories at December 31, 1998 and 1997 consist of:

	Finished (or Purchased) Goods	Work-In-Process	Raw Materials	Total
	(In Thousands)			
1998:				
Chemical products	$10,934	$3,848	$10,281	$25,063
Climate Control products	3,233	2,442	6,673	12,348
Automotive products	13,992	888	5,477	20,357
Machinery and industrial supplies	6,077	-	-	6,077
Total	$34,236	$7,178	$22,431	$63,845
1997 total	$36,429	$8,582	$21,363	$66,374

4. Property, Plant and Equipment

Property, plant and equipment, at cost, consist of:

	December 31 1998	1997
	(In Thousands)	
Land and improvements	$ 2,910	$ 5,425
Buildings and improvements(A)	20,130	34,648
Machinery, equipment and automotive	161,337	154,727
Furniture, fixtures and store equipment	8,098	7,159
Other	3,132	3,246
	195,607	205,205
Less accumulated depreciation, depletion, and amortization	96,379	86,874
	$ 99,228	$118,331

(A) Includes The Tower in 1997 acquired through foreclosure in February 1997 and sold in March 1998 as discussed in Note 2 -- Accounting Policies, Loans Receivable.

5. Long-Term Debt

Long-term debt consists of the following:

	December 31, 1998	December 31, 1997
	(In Thousands)	
Secured revolving credit facility with interest at a base rate plus a specified percentage (8.1% aggregate rate at December 31, 1998)(A)	$ 26,333	$ 19,275
10-3/4% Senior Notes due 2007(B)	105,000	105,000
Secured loan with interest payable monthly(C)	9,570	11,806
Secured revolving credit facility (weighted average interest rate of 7.1% at December 31, 1998)(D)	5,009	4,592
Note payable to bank, due in monthly installments of principal and interest through May 2001	-	12,622
Other, with interest at rates of 7.5% to 10.9%, most of which is secured by machinery and equipment(E)	23,730	27,646
	169,642	180,941
Less current portion of long-term debt	13,954	15,874
Long-term debt due after one year	$155,688	$165,067

(A) In December 1994, the Company, certain subsidiaries of the Company (the "Borrowing Group") and a bank entered into a series of six asset-based revolving credit facilities which provided for an initial term of three years. In November 1997, the Company amended the agreement. The amended agreement provides for a $65 million revolving credit facility (the "Revolving Credit Facility") with four separate loan agreements (the "Credit Facility Agreements"), for the Company and its subsidiaries. Under the Revolving Credit Facility, certain conditions exist which restrict intercompany transfers of amounts borrowed between subsidiaries. Borrowings under the Revolving Credit Facility bear an annual rate of interest at a floating rate based on the lender's prime rate plus .5% per annum or, at the Company's option, on the lender's LIBOR rate plus 2.875% per annum (which rates are subject to increase or reduction based upon specified availability and adjusted tangible net worth levels). The Revolving Credit Facility will terminate on December 31, 2000, subject to automatic renewal for terms of 13 months each, unless terminated by either party. The Credit Facility Agreements also require the payment of an annual facility fee equal to 0.5% of the unused Revolving Credit Facility. The Company may terminate the Revolving Credit Facility prior to

5. Long-Term Debt (continued)

maturity; however, should the Company do so, it would be required to pay a termination fee of $500,000.

Each of the Credit Facility Agreements specify a number of events of default and require the Company to maintain certain financial ratios (including adjusted tangible net worth and debt ratios), limits the amount of capital expenditures, and contains other covenants which restrict, among other things, (i) the incurrence of additional debt; (ii) the payment of dividends and other distributions; (iii) the making of certain investments; (iv) certain mergers, acquisitions and dispositions; (v) the issuance of secured guarantees; and (vi) the granting of certain liens.

Events of default under the Revolving Credit Facility include, among other things, (i) the failure to make payments of principal, interest, and fees, when due; (ii) the failure to perform covenants contained therein; (iii) the occurrence of a change in control if any party is or becomes the beneficial owner of more than 50% of the total voting securities of the Company, except for Jack E. Golsen or members of his immediate family; (iv) default under any material agreement or instrument (other than an agreement or instrument evidencing the lending of money) which would have a material adverse effect on the Company and its subsidiaries which are borrowers under the Revolving Credit Facility, taken as a whole, and which is not cured within the grace period; (v) a default under any other agreement relating to borrowed money exceeding certain limits; and (vi) customary bankruptcy or insolvency defaults. In November 1998, the Company and its subsidiaries amended the financial covenants of the Revolving Credit Facility (the "Amended Covenants"). The Amended Covenants provide for elimination of financial covenants upon the sale, disposal or spin-off of LSB's Automotive subsidiaries so long as the remaining borrowing group maintains a minimum aggregate availability under the Revolving Credit Facility of $15 million.

At December 31, 1998, the Company and its subsidiaries were not in compliance with certain of the financial covenants of the Revolving Credit Facility. In April 1999, the Company obtained waivers of noncompliance and amendments to reset the financial covenants through maturity.

The Revolving Credit Facility is secured by the accounts receivable, inventory, proprietary rights, general intangibles, books and records, and proceeds thereof of the Company.

5. Long-Term Debt (continued)

(B) In 1997, a subsidiary of the Company (ClimaChem, Inc., "CCI") completed the sale of $105 million principal amount of 10 3/4% Senior Notes due 2007 (the "Notes"). The Notes bear interest at an annual rate of 10 3/4% payable semiannually in arrears on June 1 and December 1 of each year. The Notes are senior unsecured obligations of CCI and rank pari passu in right of payment to all existing senior unsecured indebtedness of CCI and its subsidiaries. The Notes are effectively subordinated to all existing and future senior secured indebtedness of CCI.

The Notes were issued pursuant to an Indenture, which contains certain covenants that, among other things, limit the ability of CCI and its subsidiaries to: (i) incur additional indebtedness; (ii) incur certain liens; (iii) engage in certain transactions with affiliates; (iv) make certain restricted payments; (v) agree to payment restrictions affecting subsidiaries; (vi) engage in unrelated lines of business; or (vii) engage in mergers, consolidations or the transfer of all or substantially all of the assets of CCI to another person. In addition, in the event of certain asset sales, CCI will be required to use the proceeds to reinvest in the Company's business, to repay certain debt or to offer to purchase Notes at 100% of the principal amount thereof, plus accrued and unpaid interest, if any, thereon, plus liquidated damages, if any, to the date of purchase.

Under the terms of the Indenture, CCI cannot transfer funds to the Company in the form of cash dividends or other distributions or advances, except for (i) the amount of taxes that CCI would be required to pay if they were not consolidated with the Company and (ii) an amount not to exceed fifty percent (50%) of CCI's cumulative net income from January 1, 1998 through the end of the period for which the calculation is made for the purpose of proposing a payment and (iii) the amount of direct and indirect costs and expenses incurred by the Company on behalf of CCI pursuant to a certain services agreement and a certain management agreement to which CCI and the Company are parties.

Except as described below, the Notes are not redeemable at CCI's option prior to December 1, 2002. After December 1, 2002, the Notes will be subject to redemption at the option of CCI, in whole or in part, at the redemption prices set forth in the Indenture, plus accrued and unpaid interest thereon, plus liquidated damages, if any, to the applicable redemption date. In addition, until December 1, 2000, up to $35 million in aggregate principal amount of Notes are redeemable, at the option of CCI, at a price of 110.75% of the principal amount of the Notes, together with accrued and unpaid interest, if any, thereon, plus liquidated damages, if any, to the date of the redemption, with the net cash proceeds of a public equity offering; provided, however, that at least $65 million in aggregate principal amount of the Notes remain outstanding following such redemption.

5. Long-Term Debt (continued)

In the event of a change of control of the Company or CCI, holders of the Notes will have the right to require CCI to repurchase the Notes, in whole or in part, at a redemption price of 101% of the principal amount thereof, plus accrued and unpaid interest, if any, thereon, plus liquidated damages, if any, to the date of repurchase.

CCI is a holding company with no assets (other than that related to the notes receivable from LSB and affiliates, specified below, and the Notes origination fees which have a net book value of $3.7 million as of December 31, 1998) or operations other than its investments in its subsidiaries, and each of its subsidiaries is wholly owned, directly or indirectly. CCI's payment obligations under the Notes are fully, unconditionally and joint and severally guaranteed by all of the existing subsidiaries of CCI, except for El Dorado Nitrogen Company ("EDNC"). The assets, equity, and earnings of EDNC are inconsequential for all periods presented. Separate financial statements and other disclosures concerning the guarantors are not presented herein because management has determined they are not material to investors. Summarized financial information of CCI and its subsidiaries as of December 31, 1998 and 1997 and the results of operations for each of the three years ended December 31, 1998 is as follows:

	December 31	
	1998	1997
	(In Thousands)	
Balance sheet data:		
Current assets(1)(2)	$ 88,695	$ 88,442
Property, plant and equipment	82,389	84,329
Notes receivable from LSB and affiliates(1)	13,140	13,443
Other assets	10,480	14,661
Total assets	$194,704	$200,875
Current liabilities	$ 33,895	$ 38,004
Long-term debt	127,471	126,346
Other	9,580	9,236
Stockholders' equity	23,758	27,289
Total liabilities and stockholders' equity	$194,704	$200,875

(1) Notes receivable from LSB and affiliates is eliminated when consolidated with the Company.

(2) Current assets include income tax and other receivables due from LSB which aggregate $3.4 million and $4.3 million at December 31, 1998 and 1997, respectively.

5. Long-Term Debt (continued)

	December 31, 1998	1997	1996
	(In Thousands)		
Operations data:			
Total revenues	$257,198	$263,740	$255,618
Costs and expenses:			
Costs of sales	205,148	213,772	207,828
Selling, general and administrative	40,283	37,854	33,122
Interest	13,944	9,788	6,247
	259,375	261,414	247,197
Income (loss) before provision for income taxes and extraordinary charge	(2,177)	2,326	8,421
Provision for income taxes	392	1,429	2,668
Income (loss) before extraordinary charge	(2,569)	897	5,753
Extraordinary charge, net of income tax benefit of $1,750,000	-	2,869	-
Net income (loss)	$ (2,569)	$ (1,972)	$ 5,753

In February 1997, certain subsidiaries of the Chemical Business of the Company entered into a $50 million financing arrangement with John Hancock. The financing arrangement consisted of $25 million of fixed rate notes and $25 million of floating rate notes. In November 1997, in connection with the issuance of the Notes described above, the subsidiaries retired the outstanding principal associated with the John Hancock financing arrangement and incurred a prepayment fee. The prepayment fee paid and loan origination costs expensed in 1997 related to the John Hancock financing arrangement aggregated approximately $4.6 million.

(C) This agreement, as amended, between a subsidiary of the Company and an institutional lender provides for a loan, the proceeds of which were used in the construction of a nitric acid plant, in the aggregate amount of $16.5 million requiring 84 equal monthly payments of principal plus interest, with interest at a fixed rate of 8.86% through maturity in 2002. This agreement is secured by the plant, equipment and machinery, and proprietary rights associated with the plant which has an approximate carrying value of $28.7 million at December 31, 1998.

5. Long-Term Debt (continued)

This agreement, as amended, contains covenants (i) requiring maintenance of an escalating tangible net worth, (ii) restricting distributions and dividends, (iii) restricting a change of control of the subsidiary and the Company and (iv) requiring maintenance of a reducing debt to tangible net worth ratio. In November 1998, the subsidiary of the Company received a waiver for noncompliance of the tangible net worth and debt to tangible net worth ratio through the period ended September 30, 1999. In April 1999, the subsidiary of the Company obtained a waiver of the covenants through June 2000.

(D) At December 31, 1998, the Company's wholly-owned Australian subsidiary, TES, had an AUS $10.5 million (U.S. $6.5 million) revolving credit facility with a bank (the "Amended TES Revolver") which is renewed by the bank on an annual basis. The Amended TES Revolver provides for borrowings based on specified percentages of qualified eligible assets. The interest rate on the Amended TES Revolver is dependent upon the borrowing option elected by TES. Borrowings under an overdraft option, as defined, generally bear interest at the bank's base lending rate (which approximates the U.S. prime rate) plus .5% per annum. Borrowings under the commercial bill option generally bear interest at the bank's yield rate, as defined, plus 1.5% per annum.

The Amended TES Revolver contains certain financial covenants with which the subsidiary must comply. At December 31, 1998, the Company was in technical noncompliance with certain financial covenants contained in the Amended TES Revolver; however, the bank has confirmed that it will not act on any default so long as, in its opinion, such default will not impact the ability of TES or the Company to continue operations or service and repay its borrowings outstanding under the Amended TES Revolver. At December 31, 1998 and 1997, all borrowings outstanding under the Amended TES Revolver have been classified as due within one year in the consolidated balance sheets.

The Amended TES Revolver is secured by substantially all of the assets of TES, plus an unlimited guarantee and indemnity from the Company and certain subsidiaries.

(E) Includes a $2.6 million note payable in 1998 ($3.0 million at December 31, 1997), to an unconsolidated related party. The note is unsecured, bears interest at 10.75% per annum payable monthly, and requires principal payments of $300,000 in 1999 and $2.3 million in 2000.

Maturities of long-term debt for each of the five years after December 31, 1998 are: 1999 $13,954; 2000 $36,821; 2001 $7,913; 2002 $2,929; 2003 $676 and thereafter $107,349.

6. Income Taxes

The provision for income taxes before extraordinary charge consists of the following for the year ended December 31:

	1998	1997	1996
	(In Thousands)		
Current:			
Federal	$ 77	$ -	$ 54
State	23	50	96
	$100	$50	$150

The approximate tax effects of each type of temporary difference and carryforward that are used in computing deferred tax assets and liabilities and the valuation allowance related to deferred tax assets at December 31, 1998 and 1997 are as follows:

	1998	1997
	(In Thousands)	
Deferred tax assets		
Allowance for doubtful accounts and other asset impairments not deductible for tax purposes	$ 6,864	$ 5,361
Capitalization of certain costs as inventory for tax purposes	2,546	2,836
Net operating loss carryforward	25,235	25,390
Investment tax and alternative minimum tax credit carryforwards	1,424	1,397
Other	1,150	956
Total deferred tax assets	37,219	35,940
Less valuation allowance on deferred tax assets	25,534	25,511
Net deferred tax assets	$11,685	$10,429
Deferred tax liabilities		
Accelerated depreciation used for tax purposes	$ 9,546	$ 8,288
Inventory basis difference resulting from a business combination	2,139	2,139
Other	-	2
Total deferred tax liabilities	$11,685	$10,429

The Company is able to realize deferred tax assets up to an amount equal to the future reversals of existing taxable temporary differences. The taxable temporary differences will turn around in

6. Income Taxes (continued)

the loss carryforward period as the differences are depreciated or amortized. Other differences will turn around as the assets are disposed in the normal course of business.

The differences between the amount of the provision for income taxes and the amount which would result from the application of the federal statutory rate to "Loss before provision for income taxes and extraordinary charge" for each of the three years in the period ended December 31, 1998 are detailed below:

	1998	1997	1996
	(In Thousands)		
Benefit for income taxes at federal statutory rate	$(637)	$(8,055)	$(1,293)
Changes in the valuation allowance related to deferred tax assets, net of rate differential	23	7,313	1,591
State income taxes, net of federal benefit	15	33	62
Permanent differences	30	534	364
Foreign subsidiary loss (income)	617	191	(635)
Alternative minimum tax	77	-	54
Other	(25)	34	7
Provision for income taxes	$ 100	$ 50	$ 150

At December 31, 1998, the Company has regular-tax net operating loss ("NOL") carryforwards of approximately $63.8 million (approximately $31.4 million alternative minimum tax NOLs). Certain amounts of regular-tax NOL expire beginning in 1999.

7. Stockholders' Equity

Stock Options

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25") and related interpretations in accounting for its employee stock options because, as discussed below, the alternative fair value accounting provided for under FASB Statement No. 123, "Accounting for Stock-Based Compensation," requires use of option valuation models that were not developed for use in valuing employee stock options. Under APB 25, because the exercise price of the Company's employee stock options equals the market price of the underlying stock on the date of grant, no compensation expense is generally recognized.

7. Stockholders' Equity (continued)

Pro forma information regarding net income and earnings per share is required by Statement 123, which also requires that the information be determined as if the Company has accounted for its employee stock options granted subsequent to December 31, 1994 under the fair value method of that Statement. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions for 1998, 1997 and 1996, respectively: risk-free interest rates of 5.75%, 6.2% and 6.0%; a dividend yield of .5%, 1.43% and 1.38%; volatility factors of the expected market price of the Company's common stock of .57, .42 and .41; and a weighted average expected life of the option of 8.0, 8.0 and 6.8 years.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

For purposes of pro forma disclosures, the estimated fair value of the qualified and non-qualified stock options is amortized to expense over the options' vesting period. The Company's pro forma information follows:

	Year ended December 31,		
	1998	1997	1996
	(In Thousands, Except Per Share Data)		
Net loss applicable to common stock	$(5,943)	$(26,715)	$(7,184)
Loss per common share	(.48)	(2.07)	(.56)

Because Statement 123 is applicable only to options granted subsequent to December 31, 1994, its pro forma effect was not fully reflected until 1998.

7. Stockholders' Equity (continued)

Qualified Stock Option Plans

In November 1981, the Company adopted the 1981 Incentive Stock Option Plan (1,350,000 shares), in March 1986, the Company adopted the 1986 Incentive Stock Option Plan (1,500,000 shares) and, in September 1993, the Company adopted the 1993 Stock Option and Incentive Plan (850,000 shares). Under these plans, the Company is authorized to grant options to purchase up to 3,700,000 shares of the Company's common stock to key employees of the Company and its subsidiaries. The 1981 and 1986 Incentive Stock Option Plans have expired and, accordingly, no additional options may be granted from these plans. Options granted prior to the expiration of these plans continue to remain valid thereafter in accordance with their terms. At December 31, 1998, there are 149,000 of options outstanding related to these two plans. At December 31, 1998, there are 838,500 options outstanding related to the 1993 Stock Option and Incentive Plan which continues to be effective. These options become exercisable 20% after one year from date of grant, 40% after two years, 70% after three years, 100% after four years and lapse at the end of ten years. The exercise price of options to be granted under this plan is equal to the fair market value of the Company's common stock at the date of grant. For participants who own 10% or more of the Company's common stock at the date of grant, the option price is 110% of the fair market value at the date of grant and the options lapse after five years from the date of grant.

In August 1998, the Company adopted the 1998 Incentive Stock Option Plan (1,000,000 shares) subjective to shareholder approval. If approved, the 1998 Plan would have the same terms as described above under the 1993 Stock Option and Incentive Plan.

On April 22, 1998, the Company terminated 116,000 qualified stock options (the "terminated options"), previously granted under the 1993 Plan and replaced the terminated options with newly granted options under and pursuant to the terms of the 1993 Plan (the "replacement options"). The replacement options were granted at the fair market value of the Company's stock on April 22, 1998, have a life and vesting schedule based on the terminated options.

7. Stockholders' Equity (continued)

Activity in the Company's qualified stock option plans during each of the three years in the period ended December 31, 1998 is as follows:

	1998		1997	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	1,048,760	$4.25	1,176,640	$4.08
Granted	119,500	4.19	-	-
Exercised	(63,260)	1.13	(118,880)	2.81
Canceled, forfeited or expired	(117,500)	6.07	(9,000)	6.05
Outstanding at end of year	987,500	4.23	1,048,760	4.25
Exercisable at end of year	532,400	4.09	414,960	3.81
Weighted average fair value of options granted during year		2.16		-

	1996	
	Shares	Weighted Average Exercise Price
	611,140	$3.40
	720,500	4.33
	(120,000)	2.13
	(35,000)	4.21
	1,176,640	4.08
	354,540	3.76
		2.00

Outstanding options to acquire 954,500 shares of stock at December 31, 1998 had exercise prices ranging from $1.13 to $4.88 per share (507,500 of which are exercisable at a weighted average price of $3.93 per share), had a weighted average exercise price of $4.13 and a remaining contractual life of 5.9 years. The balance of options outstanding at December 31, 1998 had exercise prices ranging from $5.36 to $9.00 per share (24,900 of which are exercisable at a weighted average price of $7.54 per share), had a weighted average exercise price of $7.01 and a remaining contractual life of 4.7 years.

Non-qualified Stock Option Plans

The Company's Board of Directors approved the grant of non-qualified stock options to the Company's outside directors, President and certain key employees, as detailed below. The option price was based on the market value of the Company's common stock at the date of grant. These options have vesting terms and lives specific to each grant but generally vest over 48 months and expire five or ten years from the grant date (except for the 1994 extension and 1998 grants discussed below). In June 1994, the Board of Directors extended the expiration date on the grant of options for 165,000 shares to the Company's Chairman for an additional five years. The option price and terms of the option were unchanged except that, in consideration of the extension of time to exercise, the Chairman agreed to a revised vesting schedule for exercise of 20% of the option shares in each of the years 1995, 1996 and 1997 and 40% of the option shares in 1998.

7. Stockholders' Equity (continued)

In 1998, the Board of Directors granted 175,000 stock options, at the price equivalent to the Company's stock price at the date of grant. Options to two key employees for 100,000 shares have a nine-year vesting schedule while the remaining 75,000 vest over 48 months. These options expire ten years from the date of grant. In 1997, the Board of Directors granted 50,000 options to two key employees that vest over 60 months and expire ten years from the date of grant.

In September 1993, the Company adopted the 1993 Nonemployee Director Stock Option Plan (the "Outside Director Plan"). The Outside Director Plan authorizes the grant of non-qualified stock options to each member of the Company's Board of Directors who is not an officer or employee of the Company or its subsidiaries. The maximum number of shares of common stock of the Company that may be issued under the Outside Director Plan is 150,000 shares (subject to adjustment as provided in the Outside Director Plan).

The Company shall automatically grant to each outside director an option to acquire 5,000 shares of the Company's common stock on April 30 following the end of each of the Company's fiscal years in which the Company realizes net income of $9.2 million or more for such fiscal year. The exercise price for an option granted under this plan shall be the fair market value of the shares of common stock at the time the option is granted. Each option granted under this plan to the extent not exercised shall terminate upon the earlier of the termination as a member of the Company's Board of Directors or the fifth anniversary of the date such option was granted. During 1998, the Company granted 105,000 options (none in 1997 or 1996), respectively, under the Outside Director Plan.

Activity in the Company's non-qualified stock option plans during each of the three years in the period ended December 31, 1998 is as follows:

	1998		1997	
	Shares	Weighted Average Exercise Price	Shares	Weighted Average Exercise Price
Outstanding at beginning of year	280,000	$3.44	265,000	$3.31
Granted	280,000	4.19	50,000	4.19
Exercised	-	-	(35,000)	3.13
Surrendered, forfeited or expired	-	-	-	-
Outstanding at end of year	560,000	3.82	280,000	3.44
Exercisable at end of year	335,000	3.37	164,000	3.55
Weighted average fair value of options granted during year		2.62		2.00

1996	
Shares	Weighted Average Exercise Price
285,000	$3.44
-	-
(10,000)	3.13
(10,000)	7.19
265,000	3.31
166,000	3.64

-

7. Stockholders' Equity (continued)

Outstanding options to acquire 520,000 shares of stock at December 31, 1998 had exercise prices ranging from $1.38 to $4.25 per share (295,000 of which are exercisable at a weighted average price of $3.08 per share), had a weighted average exercise price of $3.56 and a remaining contractual life of 7.7 years. The balance of options outstanding at December 31, 1998 had exercise prices ranging from $5.38 to $9.00 per share (40,000 of which are exercisable at a weighted average price of $7.19 per share), had a weighted average exercise price of $7.19 and a remaining contractual life of 5.8 years.

Preferred Share Purchase Rights

In January 1999, the Company's Board of Directors approved the renewal (the "Renewed Rights Plan") of the Company's existing Preferred Share Purchase Rights Plan ("Existing Rights Plan") and declared a dividend distribution of one Renewed Preferred Share Purchase Right (the "Renewed Preferred Right") for each outstanding share of the Company's common stock outstanding upon the Existing Rights Plan's expiration date. The Renewed Preferred Rights are designed to ensure that all of the Company's stockholders receive fair and equal treatment in the event of a proposed takeover or abusive tender offer.

The Renewed Preferred Rights are generally exercisable when a person or group, other than the Company's Chairman and his affiliates, acquire beneficial ownership of 20% or more of the Company's common stock (such a person or group will be referred to as the "Acquirer"). Each Renewed Preferred Right (excluding Renewed Preferred Rights owned by the Acquirer) entitles stockholders to buy one one-hundredth (1/100) of a share of a new series of participating preferred stock at an exercise price of $20. Following the acquisition by the Acquirer of beneficial ownership of 20% or more of the Company's common stock, and prior to the acquisition of 50% or more of the Company's common stock by the Acquirer, the Company's Board of Directors may exchange all or a portion of the Renewed Preferred Rights (other than Renewed Preferred Rights owned by the Acquirer) for the Company's common stock at the rate of one share of common stock per Renewed Preferred Right. Following acquisition by the Acquirer of 20% or more of the Company's common stock, each Renewed Preferred Right (other than the Renewed Preferred Rights owned by the Acquirer) will entitle its holder to purchase a number of the Company's common shares having a market value of two times the Renewed Preferred Right's exercise price in lieu of the new preferred stock.

If the Company is acquired, each Renewed Preferred Right (other than the Renewed Preferred Rights owned by the Acquirer) will entitle its holder to purchase a number of the Acquirer's common shares having a market value at the time of two times the Renewed Preferred Right's exercise price.

7. Stockholders' Equity (continued)

Prior to the acquisition by the Acquirer of beneficial ownership of 20% or more of the Company's stock, the Company's Board of Directors may redeem the Renewed Preferred Rights for $.01 per Renewed Preferred Right.

8. Redeemable Preferred Stock

Each share of the noncumulative redeemable preferred stock, $100 par value, is convertible into 40 shares of the Company's common stock at any time at the option of the holder; entitles the holder to one vote and is redeemable at par. The redeemable preferred stock provides for a noncumulative annual dividend of 10%, payable when and as declared. Dividend payments were current at December 31, 1998 and 1997.

9. Non-redeemable Preferred Stock

The 20,000 shares of Series B cumulative, convertible preferred stock, $100 par value, are convertible, in whole or in part, into 666,666 shares of the Company's common stock (33.3333 shares of common stock for each share of preferred stock) at any time at the option of the holder and entitles the holder to one vote per share. The Series B preferred stock provides for annual cumulative dividends of 12% from date of issue, payable when and as declared. Dividend payments were current at December 31, 1998 and 1997. The terms of the Company's Series B Preferred Stock provides, in part, that in the event of any voluntary or involuntary liquidation, dissolution or winding up of the Company, or any reduction in its capital resulting in any distribution of assets to its stockholders, the holders of the Series B Preferred Stock shall be entitled to receive in cash out of assets of the Company, whether from capital or from earnings available for distribution to the stockholders, before any amount shall be paid to the holder of Common Stock of the Company the sum of One Hundred & No/100 Dollars ($100) per share, plus an amount equal to all accumulated and unpaid cash dividends thereon to the date fixed for payment of such distributive amount.

The Class C preferred stock, designated as a $3.25 convertible exchangeable Class C preferred stock, Series 2, has no par value ("Series 2 Preferred"). The Series 2 Preferred has a liquidation preference of $50.00 per share plus accrued and unpaid dividends and is convertible at the option of the holder at any time, unless previously redeemed, into common stock of the Company at an initial conversion price of $11.55 per share (equivalent to a conversion rate of approximately 4.3 shares of common stock for each share of Series 2 Preferred), subject to adjustment under certain conditions. Upon the mailing of notice of certain corporate actions, holders will have special conversion rights for a 45-day period.

9. Non-redeemable Preferred Stock (continued)

The Series 2 Preferred is redeemable at the option of the Company, in whole or in part, at prices decreasing annually to $50.00 per share on or after June 15, 2003, plus accrued and unpaid dividends to the redemption date. The redemption price at December 31, 1998 was $51.63 per share. Dividends on the Series 2 Preferred are cumulative and are payable quarterly in arrears. Dividend payments were current at December 31, 1998 and 1997.

The Series 2 Preferred also is exchangeable in whole, but not in part, at the option of the Company on any dividend payment date beginning June 15, 1996, for the Company's 6.50% Convertible Subordinated Debentures due 2018 (the "Debentures") at the rate of $50.00 principal amount of Debentures for each share of Series 2 Preferred. Interest on the Debentures, if issued, will be payable semiannually in arrears. The Debentures will, if issued, contain conversion and optional redemption provisions similar to those of the Series 2 Preferred and will be subject to a mandatory annual sinking fund redemption of five percent of the amount of Debentures initially issued, commencing June 15, 2003 (or the June 15 following their issuance, if later).

At December 31, 1998, the Company is authorized to issue an additional 248,538 shares of $100 par value preferred stock and an additional 5,000,000 shares of no par value preferred stock. Upon issuance, the Board of Directors of the Company will determine the specific terms and conditions of such preferred stock.

10. Commitments and Contingencies

Operating Leases

The Company leases certain property, plant and equipment under noncancelable operating leases. Future minimum payments on operating leases with initial or remaining terms of one year or more at December 31, 1998 are as follows:

	(In Thousands)
1999	$ 2,718
2000	2,394
2001	2,139
2002	1,887
2003	1,236
After 2003	4,774
	$15,148

Rent expense under all operating lease agreements, including month-to-month leases, was $3,866,000 in 1998, $4,085,000 in 1997 and $4,337,000 in 1996. Renewal options are available

10. Commitments and Contingencies (continued)

under certain of the lease agreements for various periods at approximately the existing annual rental amounts. Rent expense paid to related parties was $90,000 in each of 1998, 1997 and 1996.

In June 1997, two wholly owned subsidiaries of the Company, El Dorado Chemical Company ("EDC"), and El Dorado Nitrogen Company ("EDNC"), entered into a series of agreements with Bayer Corporation ("Bayer") (collectively, the "Bayer Agreement"). Under the Bayer Agreement, EDNC will act as an agent to construct, and upon completion of construction, will operate a nitric acid plant (the "EDNC Baytown Plant") at Bayer's Baytown, Texas chemical facility. EDC has guaranteed the performance of EDNC's obligations under the Bayer Agreement. Under the terms of the Bayer Agreement, EDNC is to lease the EDNC Baytown Plant pursuant to a leveraged lease from an unrelated third party with an initial lease term of ten years from the date on which the EDNC Baytown Plant becomes fully operational. Upon expiration of the initial ten-year term from the date the EDNC Baytown Plant becomes operational, the Bayer Agreement may be renewed for up to six renewal terms of five years each; however, prior to each renewal period, either party to the Bayer Agreement may opt against renewal. It is anticipated that construction cost of the EDNC Baytown Plant will approximate $69 million and will be completed in the second quarter of 1999. Construction financing of the EDNC Baytown Plant is to be provided by an unaffiliated lender. Neither the Company nor EDC has guaranteed any of the lending obligations for the EDNC Baytown Plant.

In January 1999, the contractor constructing the EDNC Baytown Plant under a turnkey agreement, informed the Company that it could not complete construction alleging a lack of financial resources. The parties to this agreement have demanded the contractor's bonding company to provide funds necessary for subcontractors to complete construction. The Company believes that a substantial portion of the costs to complete the EDNC Baytown Plant, which were to be funded by the construction contractor, will ultimately be funded by proceeds from the bonding company; however, the cost to the Company through its leveraged lease is expected to be impacted by these events. As a result of the delay in completion of the EDNC Baytown Plant, the Company, through EDNC and EDC, has entered into an interim supply agreement with Bayer to provide product from its manufacturing facility in El Dorado, Arkansas. Performance by the Company under this supply agreement will cause the Company to realign its production mix at its El Dorado manufacturing facility. While there are no assurances, the realignment of production mix is not presently anticipated to adversely impact the Company's existing chemical business or the results of operations related thereto.

In connection with the EDNC Baytown Plant, EDNC had entered into a long-term production and supply agreement with Bayer. This agreement provided for a commencement date of February 1, 1999. As mentioned above, EDNC is to provide product under an interim supply

10. Commitments and Contingencies (continued)

agreement until the EDNC Baytown Plant becomes operational; however, EDNC will be responsible to Bayer for certain lost operating profits during this time period as reasonably agreed-upon by the parties. The possible loss, if any, associated with these agreements and contract provisions is not presently determinable; however, they may be material.

Purchase Commitments

A subsidiary of the Company purchases substantial quantities of anhydrous ammonia for use in manufacturing its products. The subsidiary has contracts with three suppliers of ammonia. One contract requires a subsidiary of the Company to purchase not less than 24,000 tons nor more than 72,000 tons of anhydrous ammonia during the contract term which expires on June 30, 2000. A second contract requires a subsidiary of the Company to purchase not less than 5,000 tons of anhydrous ammonia each contract month and is for a term expiring in December 2000. The third contract requires a subsidiary of the Company to take or pay for an average of 10,000 tons of anhydrous ammonia per month and expires April 2000. These contracts are at floating prices. Purchases of anhydrous ammonia under two contracts with similar terms aggregated $31.9 million in 1998 ($40.1 million and $30.4 million in 1997 and 1996, respectively, under similar arrangements). At December 31, 1998, the subsidiary was required to make a deficiency payment of $1.3 million for quantities not taken as deliveries in 1998. The Company is allowed two years to take delivery of product. The subsidiary believes that their demand for ammonia will exceed current purchase requirements and thus the subsidiary will take delivery of the 1998 deficiency prior to expiration of the recovery period. The pricing volatility of such raw material directly affects the operating profitability of a subsidiary of the Company. A subsidiary of the Company also enters into agreements with suppliers of raw materials which require a subsidiary of the Company to provide finished goods in exchange therefore. The subsidiary did not have a significant commitment to provide finished goods with its suppliers under these exchange agreements at December 31, 1998. At December 31, 1998, the Company has a standby letter of credit outstanding related to its Chemical Business of $3.5 million.

A subsidiary of the Company leases certain precious metals for use in the subsidiary's manufacturing process. The agreement at December 31, 1998 requires rentals generally based on 7.5% of the leased metals' market values from January 1999 through July 1999, contract expiration.

In July 1995, a subsidiary of the Company entered into a product supply agreement with a third party whereby the subsidiary is required to make monthly facility fee and other payments which aggregate $71,965. In return for this payment, the subsidiary is entitled to certain quantities of compressed oxygen produced by the third party. Except in circumstances as defined by the agreement, the monthly payment is payable regardless of the quantity of compressed

10. Commitments and Contingencies (continued)

oxygen used by the subsidiary. The term of this agreement, which has been included in the above minimum operating lease commitments, is for a term of 15 years; however, after the agreement has been in effect for 60 months, the subsidiary can terminate the agreement without cause at a cost of approximately $4.5 million. Based on the subsidiary's estimate of compressed oxygen demands of the plant, the cost of the oxygen under this agreement is expected to be favorable compared to floating market prices.

Debt Guarantee

The Company has guaranteed approximately $2.6 million of indebtedness of a start-up aviation company, Kestrel Aircraft Company ("Kestrel"), in exchange for a 44.9% ownership interest. The Company's advances and investment in the aviation company amount to $1,371,000 at December 31, 1998 ($341,000 at December 31, 1997). At December 31, 1998, the Company has accrued the full amount of its commitment under the debt guarantees and fully impaired its investment and advances to Kestrel. The Company recorded losses of $1,662,000 in 1998, $1,093,000 in 1997 and $626,000 in 1996 related to its investment and the debt guarantee. The debt guarantee relates to a $2 million term note and a $2 million revolving credit facility. The $2 million revolving credit facility, on which a subsidiary of the Company has guaranteed $600,000 of indebtedness is expected to be funded by the Company in the first quarter of 1999. Upon demand of the Company's guarantee, the $2 million note guarantee agreement requires monthly principal payments of $11,111 plus interest through maturity in August 2004. At December 31, 1998, Kestrel was in default of the covenants of this term note.

Should demand be made on the Company to perform under its guarantee, the Company expects to foreclose on the assets of Kestrel, along with the other guarantors to enable the Company and the other guarantors to negotiate with potential buyers of Kestrel's stock and/or technology. Proceeds received by the Company, if any, from the sale of its ownership interest in Kestrel will be recognized in the results of operations when realized.

Legal Matters

Following is a summary of certain legal actions involving the Company:

A. In 1987, the U.S. Environmental Protection Agency ("EPA") notified one of the Company's subsidiaries, along with numerous other companies, of potential responsibility for clean-up of a waste disposal site in Oklahoma. In 1990, the EPA added the site to the National Priorities List. Following the remedial investigation and feasibility study, in 1992 the Regional Administrator of the EPA signed the Record of Decision ("ROD") for the site. The ROD detailed EPA's selected remedial action for the site and estimated the cost of the remedy at $3.6 million. In 1992, the Company made settlement proposals which would have entailed a collective payment by the subsidiaries of $47,000. The site

10. Commitments and Contingencies (continued)

owner rejected this offer and proposed a counteroffer of $245,000 plus a reopener for costs over $12.5 million. The EPA rejected the Company's offer, allocating 60% of the cleanup costs to the potentially responsible parties and 40% to the site operator. The EPA estimated the total cleanup costs at $10.1 million as of February 1993. The site owner rejected all settlements with the EPA, after which the EPA issued an order to the site owner to conduct the remedial design/remedial action approved for the site. In August 1997, the site owner issued an "invitation to settle" to various parties, alleging the total cleanup costs at the site may exceed $22 million.

No legal action has yet been filed. The amount of the Company's cost associated with the clean-up of the site is unknown due to continuing changes in the estimated total cost of clean-up of the site and the percentage of the total waste which was alleged to have been contributed to the site by the Company. As of December 31, 1998, the Company has accrued an amount based on a recent preliminary settlement proposal by the alleged potential responsible parties; however, there is no assurance such proposal will be accepted. Such amount is not material to the Company's financial position or results of operations. This estimate is subject to material change in the near term as additional information is obtained. The subsidiary's insurance carriers have been notified of this matter; however, the amount of possible coverage, if any, is not yet determinable.

B. On February 12, 1996, the Chemical Business entered into a Consent Administrative Agreement ("Administrative Agreement") with the state of Arkansas to resolve certain compliance issues associated with nitric acid concentrators. Pursuant to the Administrative Agreement, the Chemical Business installed additional pollution control equipment to address the compliance issues. The Chemical Business was assessed $50,000 in civil penalties associated with the Administrative Agreement. In the summer of 1996 and then on January 28, 1997, the subsidiary executed amendments to the Administrative Agreement ("Amended Agreements"). The Amended Agreements imposed a $150,000 civil penalty, which penalty has been paid. Since the 1997 amendment, the Chemical Business has been assessed stipulated penalties of approximately $67,000 by the Arkansas Department of Pollution Control and Ecology ("ADPC&E") for violations of certain provisions of the 1997 Amendment. The Chemical Business believes that the El Dorado Plant has made progress in controlling certain off-site emissions; however, such off-site emissions have occurred and may continue from time to time, which could result in the assessment of additional penalties against the Chemical Business by the ADPC&E for violation of the 1997 Amendment.

During May 1997, approximately 2,300 gallons of caustic material spilled when a valve in a storage vessel failed, which was released to a stormwater drain, and according to ADPC&E

10. Commitments and Contingencies (continued)

records, resulted in a minor fish kill in a drainage ditch near the El Dorado Plant. In 1998, the ADPC&E issued a Consent Administrative Order ("1998 CAO") to resolve the event. The 1998 CAO includes a civil penalty in the amount of $183,700 which includes $125,000 to be paid over five years in the form of environmental improvements at the El Dorado Plant. The remaining $58,700 has been paid prior to December 31, 1998. The 1998 CAO also requires the Chemical Business to undertake a facility-wide wastewater evaluation and pollutant source control program and wastewater minimization program. The program requires that the subsidiary complete rainwater drain-off studies including engineering design plans for additional water treatment components to be submitted to the ADCP&E by August 2000. The construction of the additional water treatment components shall be completed by August 2001 and the El Dorado Plant has been mandated to be in compliance with final effluent limits on or before February 2002. The wastewater program is currently expected to require future capital expenditures of approximately $4.6 million.

C. In 1996, three lawsuits were filed against the Company's Chemical Business by certain groups of residents of El Dorado, Arkansas, asserting a citizens' suit and two toxic tort lawsuits against the Chemical Business. The citizens' suit alleged violations of the Clean Air Act, the Clean Water Act, the Chemical Business' air and water permits and certain other environmental laws, rules and regulations. The toxic tort lawsuits alleged that the plaintiffs suffered certain injuries and damages as a result of alleged releases of toxic substances from the Chemical Business' El Dorado, Arkansas, manufacturing facility.

The Company and the Chemical Business maintain an Environmental Impairment Insurance Policy ("EIL Insurance") that provides coverage through June 30, 2001 to the Company and the Chemical Business for certain discharges, dispersals, releases, or escapes of certain contaminants and pollutants into or upon land, the atmosphere or any water course or body of water from the Site, which has caused bodily injury, property damage or contamination to others or to other property not on the Site. The EIL Insurance provides limits of liability for each loss up to $20.0 million, except $5.0 million for all remediation expenses, with the maximum limit of liability for all claims under the EIL Insurance not to exceed $20.0 million for each loss or remediation expense and $40.0 million for all losses and remediation expenses. The EIL Insurance also provides a retention of the first $500,000 per loss or remediation expense that is to be paid by the Company. Previous to 1998, the Company's Chemical Business incurred and expensed $500,000 in legal, expert and other costs in connection with the toxic tort and citizen lawsuits described above.

10. Commitments and Contingencies (continued)

During 1998, the Company's Chemical Business settled all claims asserted in the citizens' and toxic tort lawsuits. The settlements required cash payments to the plaintiffs. Substantially all of such payments were funded directly by the Company's EIL Insurance carrier.

The amount of the settlements of the toxic tort cases as discussed above paid by the EIL Insurance and the amount paid under the EIL Insurance for legal and other expenses relating to the defense of the toxic tort cases and the citizen suit case reduce the coverage amount available under the policy then in effect.

D. A civil cause of action has been filed against the Company's Chemical Business and five (5) other unrelated commercial explosives manufacturers alleging that the defendants allegedly violated certain federal and state antitrust laws in connection with alleged price fixing of certain explosive products. The plaintiffs are suing for an unspecified amount of damages, which, pursuant to statute, plaintiffs are requesting be trebled, together with costs. Based on the information presently available to the Company, the Company does not believe that the Chemical Business conspired with any party, including but not limited to, the five (5) other defendants, to fix prices in connection with the sale of commercial explosives. This litigation has been consolidated, for discovery purposes only, with several other actions in a multi-district litigation proceeding in Utah. Discovery in this litigation is in process. The Chemical Business intends to vigorously defend itself in this matter.

The Company's Chemical Business has been added as a defendant in a separate lawsuit pending in Missouri. This lawsuit alleges a national conspiracy, as well as a regional conspiracy, directed against explosive customers in Missouri and seeks unspecified damages. The Company's Chemical Business has been included in this lawsuit because it sold products to customers in Missouri during a time in which other defendants have admitted to participating in an antitrust conspiracy, and because it has been sued in the preceding described lawsuit. Based on the information presently available to the Company, the Company does not believe that the Chemical Business conspired with any party, to fix prices in connection with the sale of commercial explosives. The Chemical Business intends to vigorously defend itself in this matter.

During the third quarter of 1997, a subsidiary of the Company was served with a lawsuit in which approximately 27 plaintiffs have sued approximately 13 defendants, including a subsidiary of the Company alleging personal injury and property damage for undifferentiated compensatory and punitive damages of approximately $7,000,000. Specifically, the plaintiffs assert property damage to their residence and wells, annoyance

10. Commitments and Contingencies (continued)

and inconvenience, and nuisance as a result of daily blasting and round-the-clock mining activities. The plaintiffs are residents living near the Heartland Coal Company ("Heartland") strip mine in Lincoln County, West Virginia, and an unrelated mining operation operated by Pen Coal Inc. During 1999, the plaintiffs withdrew all personal injury claims previously asserted in this litigation. Heartland employed the subsidiary to provide blasting materials and personnel to load and shoot holes drilled by employees of Heartland. Down hole blasting services were provided by the subsidiary at Heartland's premises from approximately August 1991, until approximately August 1994. Subsequent to August 1994, the subsidiary supplied blasting materials to the reclamation contractor at Heartland's mine. In connection with the subsidiary's activities at Heartland, the subsidiary has entered into a contractual indemnity to Heartland to indemnify Heartland under certain conditions for acts or actions taken by the subsidiary for which the subsidiary failed to take, and Heartland is alleging that the subsidiary is liable thereunder for Heartland's defense costs and any losses to or damages sustained by, the plaintiffs in this lawsuit as a result of the subsidiary's operations. Discovery in this litigation is in process. The Company intends to vigorously defend itself in this matter. Based on limited information available, the subsidiary's counsel believes that the subsidiary's possible loss, if any, related to this litigation is not presently expected to have a material adverse effect on the Company.

The Company, including its subsidiaries, is a party to various other claims, legal actions, and complaints arising in the ordinary course of business. In the opinion of management after consultation with counsel, all claims, legal actions (including those described above) and complaints are adequately covered by insurance, or if not so covered, are without merit or are of such kind, or involve such amounts that unfavorable disposition is not presently expected to have a material effect on the financial position of the Company, but could have a material impact to the net loss of a particular quarter or year, if resolved unfavorably.

Other

In 1989 and 1991, the Company entered into severance agreements with certain of its executive officers that become effective after the occurrence of a change in control, as defined, if the Company terminates the officer's employment or if the officer terminates employment with the Company for good reason, as defined. These agreements require the Company to pay the executive officers an amount equal to 2.9 times their average annual base compensation, as defined, upon such termination.

The Company has retained certain risks associated with its operations, choosing to self-insure up to various specified amounts under its automobile, workers' compensation, health and general

10. Commitments and Contingencies (continued)

liability programs. The Company reviews such programs on at least an annual basis to balance the cost-benefit between its coverage and retained exposure.

11. Employee Benefit Plan

The Company sponsors a retirement plan under Section 401(k) of the Internal Revenue Code under which participation is available to substantially all full-time employees. The Company does not contribute any significant amounts to this plan.

12. Fair Value of Financial Instruments

The following discussion of fair values is not indicative of the overall fair value of the Company's balance sheet since the provisions of the SFAS No. 107, "Disclosures About Fair Value of Financial Instruments," do not apply to all assets, including intangibles.

The following methods and assumptions were used by the Company in estimating its fair value of financial instruments:

Borrowed Funds: Fair values for fixed rate borrowings, other than the Notes, are estimated using a discounted cash flow analysis that applies interest rates currently being offered on borrowings of similar amounts and terms to those currently outstanding. The fair value of the Notes was determined based on a market quotation for such securities. As of December 31, 1998 and 1997, carrying values of variable rate and fixed-rate long-term debt which aggregated $169.6 million and $180.9 million, respectively, approximate their fair value.

Hedging Agreements: The fair value of the interest rate forward agreement is estimated based on quoted market prices of instruments with similar terms. As of December 31, 1998, the financial instruments' fair value (which is not reflected on the accompanying balance sheet), net to the Company's 50% interest, represented a liability of approximately $3.3 million ($1.8 million at December 31, 1997). The fair value of the natural gas swap agreements was estimated based on market prices of natural gas for the periods covered by the agreements. At December 31, 1998 and 1997, the fair values of such agreements represented a liability of approximately $255,000 and $165,000, respectively.

As of December 31, 1998, the carrying values of cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities approximated their estimated fair value.

13. Segment Information

Factors Used By Management to Identify the Enterprise's Reportable Segments and Measurement of Segment Profit or Loss and Segment Assets

LSB Industries, Inc. has four reportable segments: the Chemical Business, Climate Control Business, Automotive Business, and Industrial Products Business. The Company's reportable segments are based on business units that offer similar products and services. The reportable segments are each managed separately because they manufacture and distribute distinct products with different production processes.

The Company evaluates performance and allocates resources based on profit or loss from operations before allocation of corporate overhead, interest expense and income taxes. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies.

Description of Each Reportable Segment

Chemical

This segment manufactures and sells fertilizer grade ammonium nitrate for the agriculture industry, explosive grade ammonium nitrate for the mining industry and concentrated, blended and mixed nitric acid for industrial applications. Production from the Company's primary manufacturing facility in El Dorado, Arkansas, for the year ended December 31, 1998 comprises approximately 86% of the chemical segment's sales. Sales to customers of this segment primarily include farmers in Texas and Arkansas, coal mining companies in Kentucky, Missouri and West Virginia and industrial users of acids in the South and East regions of the United States.

The Chemical Business is subject to various federal, state and local environmental regulations. Although the Company has designed policies and procedures to help reduce or minimize the likelihood of significant chemical accidents and/or environmental contamination, there can be no assurances that the Company will not sustain a significant future operating loss related thereto.

The Chemical Business' Australian subsidiary's results of operations have been adversely affected due to the recent economic developments in certain countries in Asia. These economic developments in Asia have had a negative impact on the mining industry in Australia, which this subsidiary services. In February 1999, the Company received a nonbinding offer to acquire the stock of the Australian subsidiary. At the present

13. Segment Information (continued)

time the parties are in negotiation; however, there are no assurances that the transaction will ultimately be consummated. If the Company does not ultimately consummate this sale and the operating results of the Australian subsidiary do not reflect markedly improved conditions, in the near term, it is reasonably possible that the Company will recognize an impairment charge related to the recovery of such net assets.

Further, the Company purchases substantial quantities of anhydrous ammonia for use in manufacturing its products. The pricing volatility of such raw material directly affects the operating profitability of the chemical segment.

Climate Control

This business segment manufactures and sells, primarily from its various facilities in Oklahoma City, a variety of hydronic fan coil, water source heat pump products and other HVAC products for use in commercial and residential air conditioning and heating systems. The Company's various facilities in Oklahoma City comprise substantially all of the Climate Control segment's operations. Sales to customers of this segment primarily include original equipment manufacturers, contractors and independent sales representatives located throughout the world which are generally secured by a mechanic's lien, except for sales to original equipment manufacturers.

Automotive Products

This segment manufactures and sells anti-friction bearings, clutch sets, universal joints and other products for automotive applications to wholesalers, retailers and original equipment manufacturers located throughout the world. Net sales from the Company's primary facility in Oklahoma City comprises approximately 90% of the automotive products segment sales.

At December 31, 1998, the automotive segment has $22.7 million of inventory, a portion of which is in excess of current requirements based on recent sales levels and has been classified with other assets. Management has developed a program to reduce this inventory to desired levels over the near term and believes no significant loss will be incurred on disposition.

In 1998, one customer accounted for 21.1% of Automotive Products net sales. In 1997, two customers accounted for an aggregate of 24.1% of net sales, 12.8% and 11.3% individually and in 1996 one customer accounted for 12.1% of net sales.

13. Segment Information (continued)

Industrial Products

This segment manufactures and purchases machine tools and purchases industrial supplies for sale to machine tool dealers and end users throughout the world. Sales of industrial supplies are generally unsecured, whereas the Company generally retains a security interest in machine tools sold until payment is received.

The industrial products segment attempts to maintain a full line of certain product lines, which necessitates maintaining certain products in excess of management's successive year expected sales levels. Inasmuch as these products are not susceptible to rapid technological changes, management believes no loss will be incurred on disposition.

Credit, which is generally unsecured, is extended to customers based on an evaluation of the customer's financial condition and other factors. Credit losses are provided for in the financial statements based on historical experience and periodic assessment of outstanding accounts receivable, particularly those accounts which are past due. The Company's periodic assessment of accounts and credit loss provisions are based on the Company's best estimate of amounts which are not recoverable. Concentrations of credit risk with respect to trade receivables are limited due to the large number of customers comprising the Company's customer bases, and their dispersion across many different industries and geographic areas. As of December 31, 1998 and 1997, the Company's accounts and notes receivable are shown net of allowance for doubtful accounts of $10.2 million and $9.2 million, respectively.

Information about the Company's operations in different industry segments for each of the three years in the period ended December 31, 1998 is detailed below.

	1998	1997	1996
	(In Thousands)		
Sales:			
Chemical	$139,942	$156,949	$166,163
Climate Control	115,786	105,909	89,275
Automotive Products	39,994	35,499	37,946
Industrial Products	14,315	15,572	13,776
	$310,037	$313,929	$307,160

13. Segment Information (continued)

:

	1998	1997	1996
	(In Thousands)		
Gross profit:			
Chemical	$ 18,274	$ 19,320	$ 25,885
Climate Control	32,278	29,552	21,961
Automotive Products	8,670	3,299	5,868
Industrial Products	3,731	3,776	3,058
	$ 62,953	$ 55,947	$ 56,772
Operating profit (loss):			
Chemical	$ 3,675	$ 5,479	$ 10,971
Climate Control	10,493	8,895	5,362
Automotive Products	(1,827)	(7,251)	(4,134)
Industrial Products	(403)	(993)	(2,685)
	11,938	6,130	9,514
General corporate expenses and other, net	(9,424)	(9,786)	(3,192)
Interest expense	(17,327)	(14,740)	(10,017)
Gain on sale of Tower	12,993	-	-
Loss before provision for income taxes and extraordinary charge	$ (1,820)	$(18,396)	$ (3,695)
Depreciation of property, plant and equipment:			
Chemical	$ 7,992	$ 6,581	$ 5,504
Climate Control	1,602	1,544	1,552
Automotive Products	1,230	1,637	994
Industrial Products	102	190	126
Corporate assets and other	725	1,190	479
Total depreciation of property, plant and equipment	$ 11,651	$ 11,142	$ 8,655

13. Segment Information (continued)

	1998	1997	1996
	(In Thousands)		
Additions to property, plant and equipment:			
Chemical	$ 5,233	$ 8,390	$ 19,137
Climate Control	3,868	1,127	1,551
Automotive Products	619	936	1,306
Industrial Products	130	109	37
Corporate assets and other	293	17,528	145
Total additions to property, plant and equipment	$ 10,143	$ 28,090	$ 22,176
Total assets:			
Chemical	$124,577	$137,570	$132,718
Climate Control	49,516	49,274	50,623
Automotive Products	41,967	42,718	43,212
Industrial Products	11,662	9,929	13,614
Corporate assets and other	20,925	31,162	21,393
Total assets	$248,647	$270,653	$261,560

Revenues by industry segment include revenues from unaffiliated customers, as reported in the consolidated financial statements. Intersegment revenues, which are accounted for at transfer prices ranging from the cost of producing or acquiring the product or service to normal prices to unaffiliated customers, are not significant.

Gross profit by industry segment represents net sales less cost of sales. Operating profit by industry segment represents revenues less operating expenses. In computing operating profit, none of the following items have been added or deducted: general corporate expenses, income taxes or interest expense and, in 1998, before the gain on the sale of The Tower.

Total assets by industry segment are those assets used in the operations of each industry. Corporate assets are those principally owned by the parent company or by subsidiaries not involved in the four identified industries. All corporate assets leased by the Company's subsidiaries have been included in the identified segments' assets.

13. Segment Information (continued)

Information about the Company's domestic and foreign operations for each of the three years in the period ended December 31, 1998 is detailed below:

Geographic Region	1998	1997	1996
		(In Thousands)	
Sales:			
Domestic	$292,740	$285,805	$270,675
Foreign:			
Australia/New Zealand	14,184	26,482	32,917
Others	3,113	1,642	3,568
	$310,037	$313,929	$307,160
Income (loss) before provision for income taxes and extra-ordinary charge:			
Domestic	$ 408	$(17,270)	$ (5,174)
Foreign:			
Australia/New Zealand	(2,898)	(772)	1,705
Others	670	(354)	(226)
	$ (1,820)	$(18,396)	$ (3,695)
Long-lived assets:			
Domestic	$ 94,560	$111,177	$ 94,752
Foreign:			
Australia/New Zealand	4,665	6,046	6,398
Others	3	1,108	1,993
	$ 99,228	$118,331	$103,143

Revenues by geographic region include revenues from unaffiliated customers, as reported in the consolidated financial statements. Revenues earned from sales or transfers between affiliates in different geographic regions are shown as revenues of the transferring region and are eliminated in consolidation.

13. Segment Information (continued)

Revenues from unaffiliated customers include foreign export sales as follows:

Geographic Area	1998	1997	1996
		(In Thousands)	
Mexico and Central and South America	$ 8,126	$ 8,604	$ 9,084
Canada	8,400	5,609	9,703
Middle East	5,135	6,167	6,019
Other	5,774	7,359	8,498
	$27,435	$27,739	$33,304

14. Liquidity and Management's Plan

As discussed in Note 5(B), the Company and its subsidiaries (other than CCI and subsidiaries of CCI) (the "Non-CCI Entities") are dependent upon their separate cash flows and the restricted funds which can be distributed by CCI to the Company under various agreements CCI and its subsidiaries are parties to. As of December 31, 1998, the Non-CCI Entities had working capital of $13.7 million (including $26.5 million of inventories and $13.9 million of accounts receivable), stockholders' equity of $11.3 million (exclusive of their equity in CCI) and long-term debt of $31.7 million ($3.5 million of which is due within one year). For the year ended December 31, 1998, the Non-CCI Entities had net income of $.6 million, inclusive of a gain on the sale of The Tower of $13.0 million, and used cash in operating activities approximating $8.1 million. As previously announced, the Company is focusing its efforts and resources on its core businesses, Climate Control and Chemical, and is evaluating the possible spin-off of its Automotive Business and the most appropriate means of realizing its investments in certain other non-core assets. These non-core assets include the Company's Automotive and Industrial Products Businesses.

Management is also realigning the Company's overhead to better match its focus on the core businesses. This realignment will include the sale of certain Non-CCI Entity assets to CCI, which assets are materially related to the lines of businesses of the Chemical and Climate Control Businesses and create opportunities for CCI and its subsidiaries to expand upon their strengths. The Company is currently negotiating with an asset-based lender, for a $20 million credit facility for the Automotive Business. This facility, if completed as currently structured, would provide for a $2 million term loan and an $18 million revolving credit facility (an increase of availability calculated as of March 31, 1999 of $1.6 million compared to the Automotive Business' current facility). Further, as discussed in Note 5(A), the Company's Revolving Credit Facility provides for the elimination of its financial covenants upon the sale, disposal or spin-off of the

14. Liquidity and Management's Plan (continued)

Automotive Business so long as the remaining borrowing group maintains a minimum aggregate availability under such facility of at least $15 million.

Based on these plans, management believes the Non-CCI Entities will have sufficient operating capital to meet their obligations as they come due. If management is not successful in executing this plan including realignment of overhead to reduce its operating costs or realizing certain excess and non-core assets, it is reasonably possible that this evaluation could change in the near term.

LSB Industries, Inc.

Supplementary Financial Data

Quarterly Financial Data (Unaudited)

(In Thousands, Except Per Share Amounts)

	Three months ended March 31	June 30	September 30	December 31
Total revenues	$92,139	$87,646	$78,919	$ 65,616
Gross profit on net sales	$15,917	$20,379	$15,628	$ 11,029
Net income (loss)	$ 9,278	$ 1,421	$(3,196)	$ (9,423)
Net income (loss) applicable to common stock	$ 8,462	$ 618	$(3,999)	$(10,230)
Earnings (loss) per common share:				
Basic	$.66	$.05	$(.33)	$(.85)
Diluted	$.53	$.05	$(.33)	$(.85)
1997				
Total revenues	$74,864	$91,437	$77,927	$ 75,961
Gross profit on net sales	$10,922	$19,380	$14,541	$ 11,104
Income (loss) before extraordinary charge	$(5,438)	$ 1,467	$(4,779)	$ (9,696)
Net income (loss)	$(5,438)	$ 1,467	$(4,779)	$(14,315)
Net income (loss) applicable to common stock	$(6,241)	$ 648	$(5,582)	$(15,119)
Basic and diluted earnings (loss) per common share:				
Earnings (loss) before extra-ordinary charge	$(0.48)	$0.05	$(0.43)	$(0.82)
Extraordinary charge	-	-	-	(0.36)
Net income (loss)	$(0.48)	$0.05	$(0.43)	$(1.18)

In the first quarter of 1998, a subsidiary of the Company closed the sale of an office building located in Oklahoma City, known as "The Tower." The subsidiary realized proceeds from the sale of approximately $29 million, net of transaction costs.

In the fourth quarter of 1998, the Company's Climate Control group recorded an adjustment to inventory which reduced gross profit by $1.5 million and the Company's Chemical group recorded a provision for loss of approximately $.8 million for a note receivable which increased the Company's net loss.

In the fourth quarter of 1997, in connection with the issuance of $105 million, 10 3/4% Senior Notes due in 2007, a subsidiary of the Company retired the outstanding principal associated with a $50 million financing arrangement and incurred a prepayment fee. The prepayment fee paid and loan origination costs expensed in 1997 relating to the financing arrangement aggregated approximately $4.6 million.

LSB Industries, Inc.

Schedule II -- Valuation and Qualifying Accounts

Years ended December 31, 1998, 1997 and 1996

(Dollars in Thousands)

Description	Balance at Beginning of Year	Additions: Charged to Costs and Expenses	Deductions: Write-offs/ Costs Incurred	Balance at End of Year
Accounts receivable -- allowance for doubtful accounts:(1)				
1998	$4,007	$1,544	$1,998	$3,553
1997	$3,291	$1,544	$ 828	$4,007
1996	$2,584	$1,451	$ 744	$3,291
Inventory -- reserve for slow-moving items:				
1998	$1,531	$ 173	$ -	$1,704
1997	$1,709	$ 68	$ 246	$1,531
1996	$1,318	$ 578	$ 187	$1,709
Notes receivable -- allowance for doubtful accounts:				
1998	$5,158	$1,480	$ -	$6,638
1997	$4,065	$1,093	$ -	$5,158
1996	$2,500	$1,565	$ -	$4,065

(1) Deducted in the balance sheet from the related assets to which the reserve applies.

Other valuation and qualifying accounts are detailed in the Company's notes to consolidated financial statements.

EXHIBIT INDEX

Exhibit No.	Description	Sequential Page No.
2.1	Stock Option Agreement dated as of May 4, 1995, between optionee, LSB Holdings, Inc., an Oklahoma Corporation and the shareholders of a specialty sales organization, an option which the Company hereby incorporates hereby by reference from Exhibit 2.1 to the Company's Form 10-K for fiscal year ended December 31, 1995.	
2.2	Stock Purchase Agreement and Stock Pledge Agreement between Dr. Hauri AG, a Swiss Corporation, and LSB Chemical Corp., which the Company hereby incorporates by reference from Exhibit 2.2 to the Company's Form 10-K for fiscal year ended December 31, 1994.	
3.1	Restated Certificate of Incorporation, the Certificate of Designation dated February 17, 1989, and certificate of Elimination dated April 30, 1993, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Registration Statement, No. 33-61640; Certificate of Designation for the Company's $3.25 Convertible Exchangeable Class C Preferred Stock, Series 2, which the Company hereby incorporates by reference from Exhibit 4.6 to the Company's Registration Statement, No. 33-61640.	
3.2	Bylaws, as amended, which the Company hereby incorporates by reference from Exhibit 3(ii) to the Company's Form 10-Q for the quarter ended June 30, 1998.	
4.1	Specimen Certificate for the Company's Non-cumulative Preferred Stock, having a par value of $100 per share, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 10-Q for the quarter ended June 30, 1983.	
4.2	Specimen Certificate for the Company's Series B Preferred Stock, having a par value of $100 per share, which the Company hereby incorporates by reference from Exhibit 4.27 to the Company's Registration Statement No. 33-9848.	
4.3	Specimen Certificate for the Company's Series 2 Preferred, which the Company hereby incorporates by reference from Exhibit 4.5 to the Company's Registration Statement No. 33-61640.	
4.4	Specimen Certificate for the Company's Common Stock, which the Company incorporates by reference from Exhibit 4.4 to the Company's Registration Statement No. 33-61640.	
4.5	Renewed Rights Agreement, dated January 6, 1999, between the Company and Bank One, N.A., which the Company hereby incorporates by reference from Exhibit No. 1 to the Company's Form 8-A Registration Statement, dated January 27, 1999.	
4.6	Indenture, dated as of November 26, 1997, by and among ClimaChem, Inc., the Subsidiary Guarantors and Bank One, NA, as trustee, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 8-K, dated November 26, 1997.	

4.7 Form 10 3/4% Series B Senior Notes due 2007 which the Company hereby incorporates by reference from Exhibit 4.3 to the ClimaChem Registration Statement, No. 333-44905.

4.8 Amended and Restated Loan and Security Agreement, dated November 21, 1997, by and between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation which the Company hereby incorporates by reference from Exhibit 10.2 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

4.9 Amended and Restated Loan and Security Agreement, dated November 21, 1997, by and between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.11 to the Company's Form 10-K for the fiscal year ended December 31, 1997. Substantially identical Amended and Restated Loan and Security Agreements dated November 21, 1997, were entered into by each of L&S Bearing Co., and Summit Machine Tool Manufacturing Corp., with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.10 First Amendment to Amended and Restated Loan and Security Agreement, dated March 12, 1998, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation which the Company hereby incorporates by reference from Exhibit 10.53 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

4.11 First Amendment to Amended and Restated Loan and Security Agreement, dated March 12, 1998, between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.13 to the Company's Form 10-K for the fiscal year ended December 31, 1997. Substantially identical First Amendments to Amended and Restated Loan and Security Agreements, dated March 12, 1998, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.12 Third Amendment to Amended and Restated Loan and Security Agreement, dated August 14, 1998, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 10-Q for the quarter ended June 30, 1998.

4.13 Third Amendment to Amended and Restated Loan and Security Agreement, dated August 14, 1998, between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.2 to the Company's Form 10-Q for the quarter ended June 30, 1998. Substantially identical Third Amendments to Amended and Restated Loan and Security Agreements, dated August 14, 1998, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.14 Fourth Amendment to Amended and Restated Loan and Security Agreement, dated November 19, 1998, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation, which the Company hereby incorporates by reference from Exhibit 4.1 to the Company's Form 10-Q for the quarter ended September 30, 1998.

4.15 Fourth Amendment to Amended and Restated Loan and Security Agreement, dated November 19, 1998, between BankAmerica Business Credit, Inc., and the Company, which the Company hereby incorporates by reference from Exhibit 4.2 to the Company's Form 10-Q for the quarter ended September 30, 1998. Substantially identical Fourth Amendments to Amended and Restated Loan and Security Agreements, dated November 19, 1998, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.16 Fifth Amendment to Amended and Restated Loan and Security Agreement, dated April 8, 1999, between BankAmerica Business Credit, Inc., and Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Company and Slurry Explosive Corporation.

4.17 Fifth Amendment to Amended and Restated Loan and Security Agreement, dated April 8, 1999, between BankAmerica Business Credit, Inc., and the Company. Substantially identical Fifth Amendments to Amended and Restated Loan and Security Agreements, dated April 8, 1999, were entered into by each of L&S Bearing Co. and Summit Machine Tool Manufacturing Corp. with BankAmerica Business Credit, Inc., and are hereby omitted and such will be provided upon the Commission's request.

4.18 Waiver Letter, dated March 16, 1998, from BankAmerica Business Credit, Inc. which the Company hereby incorporates by reference from Exhibit 10.55 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

4.19 First Supplemental Indenture, dated February 8, 1999, by and among ClimaChem, Inc., the Guarantors, and Bank One, N.A.

10.1 Form of Death Benefit Plan Agreement between the Company and the employees covered under the plan, which the Company hereby incorporates by reference from Exhibit 10(c)(1) to the Company's Form 10-K for the year ended December 31, 1980.

10.2 The Company's 1981 Incentive Stock Option Plan, as amended, and 1986 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibits 10.1 and 10.2 to the Company's Registration Statement No. 33-8302.

10.3 Form of Incentive Stock Option Agreement between the Company and employees as to the Company's 1981 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibit 10.10 to the Company's Form 10-K for the fiscal year ended December 31, 1984.

10.4 Form of Incentive Stock Option Agreement between the Company and employees as to the Company's 1986 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibit 10.6 to the Company's Registration Statement No. 33-9848.

10.5 The 1987 Amendments to the Company's 1981 Incentive Stock Option Plan and 1986 Incentive Stock Option Plan, which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-K for the fiscal year ended December 31, 1986.

10.6 The Company's 1993 Stock Option and Incentive Plan which the Company hereby incorporates by reference from Exhibit 10.6 to the Company's Form 10-K for the fiscal year ended December 31, 1993.

10.7 The Company's 1993 Non-employee Director Stock Option Plan which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-K for the fiscal year ended December 31, 1993.

10.8 Union Contracts, dated August 5, 1995, between EDC and the Oil, Chemical and Atomic Workers, and the United Steel Workers of America, dated November 1, 1995 which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-K for the fiscal year ended December 31, 1995.

10.9 Lease Agreement, dated March 26, 1982, between Mac Venture, Ltd. and Hercules Energy Mfg. Corporation, which the Company hereby incorporates by reference from Exhibit 10.32 to the Company's Form 10-K for the fiscal year ended December 31, 1981.

10.10 Limited Partnership Agreement dated as of May 4, 1995, between the general partner, and LSB Holdings, Inc., an Oklahoma Corporation, as limited partner which the Company hereby incorporates by reference from Exhibit 10.11 to the Company's Form 10-K for the fiscal year ended December 31, 1995.

10.11 Lease Agreement dated November 12, 1987, between Climate Master, Inc. and West Point Company and amendments thereto, which the Company hereby incorporates by reference from Exhibits 10.32, 10.36, and 10.37, to the Company's Form 10-K for fiscal year ended December 31, 1988.

10.12 Severance Agreement, dated January 17, 1989, between the Company and Jack E. Golsen, which the Company hereby incorporates by reference from Exhibit 10.48 to the Company's Form 10-K for fiscal year ended December 31, 1988. The Company also entered into identical agreements with Tony M. Shelby, David R. Goss, Barry H. Golsen, David M. Shear, and Jim D. Jones and the Company will provide copies thereof to the Commission upon request.

10.13 Third Amendment to Lease Agreement, dated as of December 31, 1987, between Mac Venture, Ltd. and Hercules Energy Mfg. Corporation, which the Company hereby incorporates by reference from Exhibit 10.49 to the Company's Form 10-K for fiscal year ended December 31, 1988.

10.14 Employment Agreement and Amendment to Severance Agreement dated January 12, 1989 between the Company and Jack E. Golsen, dated March 21, 1996 which the Company hereby incorporates by reference from Exhibit 10.15 to the Company's Form 10-K for fiscal year ended December 31, 1995.

10.15 Non-Qualified Stock Option Agreement, dated June 1, 1992, between the Company and Robert C. Brown, M.D. which the Company hereby incorporates by reference from Exhibit 10.38 to the Company's Form 10-K for fiscal year ended December 31, 1992. The Company entered into substantially identical agreements with Bernard G. Ille, Jerome D. Shaffer and C.L.Thurman, and the Company will provide copies thereof to the Commission upon request.

10.16 Loan and Security Agreement (DSN Plant) dated October 31, 1994 between DSN Corporation and The CIT Group which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended September 30, 1994.

10.17 Loan and Security Agreement (Mixed Acid Plant) dated April 5, 1995 between DSN Corporation and The CIT Group, which the Company hereby incorporates by reference from Exhibit 10.25 to the Company's Form 10-K for the fiscal year ended December 31, 1994.

10.18 First Amendment to Loan and Security Agreement (DSN Plant), dated June 1, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.13 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.19 First Amendment to Loan and Security Agreement (Mixed Acid Plant), dated November 15, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.15 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.20 Loan and Security Agreement (Rail Tank Cars), dated November 15, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.16 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.21 First Amendment to Loan and Security Agreement (Rail Tank Cars), dated November 15, 1995, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.17 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.22 Letter Amendment, dated May 14, 1997, to Loan and Security Agreement between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended March 31, 1997.

10.23 Amendment to Loan and Security Agreement, dated November 21, 1997, between DSN Corporation and The CIT Group/Equipment Financing, Inc. which the Company hereby incorporates by reference from Exhibit 10.19 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.24 First Amendment to Non-Qualified Stock Option Agreement, dated March 2, 1994, and Second Amendment to Stock Option Agreement, dated April 3, 1995, each between the Company and Jack E. Golsen, which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended March 31, 1995.

10.25 Facility Letter, dated August 20, 1997, between Bank of New Zealand, Australia, and Total Energy Systems Limited which the Company hereby incorporates by reference from Exhibit 10.38 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.26 Variation Letter, dated February 10, 1998, between Bank of New Zealand, Australia, and Total Energy Systems Limited which the Company hereby incorporates by reference from Exhibit 10.39 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.27 Debenture Charge, dated March 7, 1995, between Total Energy Systems Limited and Bank of New Zealand which the Company hereby incorporates by reference from Exhibit 10.40 to the ClimaChem Form S-4 Registration Statement, No. 333-44905. T.E.S. Mining Services Pty. Ltd. and Total Energy Systems (NZ) Limited are each parties to substantially identical Debentures, copies of which will be provided to the Commission upon request.

10.28 Anhydrous Ammonia Sales Agreement, dated May 28, 1997, to be effective January 1, 1997, between Koch Nitrogen Company and El Dorado Chemical Company which the Company hereby incorporates by reference from Exhibit 10.1 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.29 Baytown Nitric Acid Project and Supply Agreement dated June 27, 1997, by and among El Dorado Nitrogen Company, El Dorado Chemical Company and Bayer Corporation which the Company hereby incorporates by reference from Exhibit 10.2 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.30 First Amendment to Baytown Nitric Acid Project and Supply Agreement, dated February 1, 1999, between El Dorado Nitrogen Company, El Dorado Chemical Company, and Bayer Corporation. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION UNDER THE FREEDOM OF INFORMATION ACT. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

10.31 Service Agreement, dated June 27, 1997, between Bayer Corporation and El Dorado Nitrogen Company which the Company hereby incorporates by reference from Exhibit 10.3 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.32 Ground Lease dated June 27, 1997, between Bayer Corporation and El Dorado Nitrogen Company which the Company hereby incorporates by reference from Exhibit 10.4 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.33 Participation Agreement, dated as of June 27, 1997, among El Dorado Nitrogen Company, Boatmen's Trust Company of Texas as Owner Trustee, Security Pacific Leasing corporation, as Owner Participant and a Construction Lender, Wilmington Trust Company, Bayerische Landesbank, New York Branch, as a Construction Lender and the Note Purchaser, and Bank of America National Trust and Savings Association, as Construction Loan Agent which the Company hereby incorporates by reference from Exhibit 10.5 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF COMMISSION ORDER CF #5551, DATED SEPTEMBER 25, 1997, GRANTING A REQUEST FOR CONFIDENTIAL TREATMENT UNDER THE FREEDOM OF INFORMATION ACT AND THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED.

10.34 Lease Agreement, dated as of June 27, 1997, between Boatmen's Trust Company of Texas as Owner Trustee and El Dorado Nitrogen Company which the Company hereby incorporates by reference from Exhibit 10.6 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997.

10.35 Security Agreement and Collateral Assignment of Construction Documents, dated as of June 27, 1997, made by El Dorado Nitrogen Company which the Company hereby incorporates by reference from Exhibit 10.7 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997.

10.36 Security Agreement and Collateral Assignment of Facility Documents, dated as of June 27, 1997, made by El Dorado Nitrogen Company and consented to by Bayer Corporation which the Company hereby incorporates by reference from Exhibit 10.8 to the Company's Form 10-Q for the fiscal quarter ended June 30, 1997.

10.37 Amendment to Loan and Security Agreement, dated March 16, 1998, between The CIT Group/Equipment Financing, Inc., and DSN Corporation which the Company hereby incorporates by reference from Exhibit 10.54 to the ClimaChem Form S-4 Registration Statement, No. 333-44905.

10.38 Fifth Amendment to Lease Agreement, dated as of December 31, 1998, between Mac Venture, Ltd. and Hercules Energy Mfg. Corporation.

10.39 Sales Contract, dated December 7, 1998, between Solutia, Inc. and El Dorado Chemical Company. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION UNDER THE FREEDOM OF INFORMATION ACT. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

10.40 Agreement for Purchase and Sale of Anhydrous Ammonia, dated January 1, 1999, between El Dorado Chemical Company and Farmland Industries, Inc. CERTAIN INFORMATION WITHIN THIS EXHIBIT HAS BEEN OMITTED AS IT IS THE SUBJECT OF A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION UNDER THE FREEDOM OF INFORMATION ACT. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

10.41 Agreement, dated March 23, 1999, among El Dorado Chemical Company, El Dorado Nitrogen Company, Bayer Corporation, ICF Kaiser Engineers, Inc., ICF Kaiser International, Inc., and Acstar Insurance Company.

10.42 Union Contract, dated August 1, 1998, between El Dorado Chemical Company and the International Association of Machinists and Aerospace Workers.

10.43 Non-Qualified Stock Option Agreement, dated April 22, 1998, between the Company and Robert C. Brown, M.D. The Company entered into substantially identical agreements with Bernard G. Ille, Jerome D. Shaffer, Raymond B. Ackerman, Horace G. Rhodes, Gerald J. Gagner, and Donald W. Munson. The Company will provide copies of these agreements to the Commission upon request.

10.44 The Company's 1998 Stock Option and Incentive Plan.

10.45 Letter Agreement, dated March 12, 1999, between Kestrel Aircraft Company and LSB Industries, Inc., Prime Financial Corporation, Herman Meinders, Carlan K. Yates, Larry H. Lemon, Co-Trustee Larry H. Lemon Living Trust.

10.46 Covenant Waiver Letter, dated April 13, 1999, between The CIT Group and DSN Corporation.

21.1. Subsidiaries of the Company

23.1. Consent of Independent Auditors

27.1. Financial Data Schedule

FIFTH AMENDMENT
TO AMENDED AND RESTATED
LOAN AND SECURITY AGREEMENT

THIS FIFTH AMENDMENT TO AMENDED AND RESTATED LOAN AND SECURITY AGREEMENT (the "Amendment") is dated as of April 8, 1999, and entered into by and between BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION (successor-in-interest to BANKAMERICA BUSINESS CREDIT, INC.) ("Lender") and CLIMATE MASTER, INC. ("Climate Master"), INTERNATIONAL ENVIRONMENTAL CORPORATION ("IEC"), EL DORADO CHEMICAL COMPANY ("EDC") and SLURRY EXPLOSIVE CORPORATION ("Slurry") (Climate, IEC, EDC, and Slurry being collectively referred to herein as "Borrower").

WHEREAS, Lender and Borrower have entered into that certain Amended and Restated Loan and Security Agreement dated as of November 21, 1997 as amended by that certain First Amendment to Amended and Restated Loan and Security Agreement dated as of March 12, 1998, that certain Second Amendment to Amended and Restated Loan and Security Agreement dated as of June 30, 1998, that certain Third Amendment to Amended and Restated Loan and Security Agreement dated as of August 14, 1998, and that certain Fourth Amendment to Amended and Restated Loan and Security Agreement dated as of November 19, 1998 (as so amended, the "Agreement");

WHEREAS, two Events of Default have occurred under the Agreement;

WHEREAS, the Borrower desires that the Lender waive the Events of Default and amend the Agreement in certain respects; and

WHEREAS, the Lender is willing to waive the Events of Default and amend the Agreement subject to the terms and conditions contained herein;

NOW, THEREFORE, in consideration of the mutual conditions and agreements set forth in the Agreement and this Amendment, and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties, intending to be legally bound, hereby agree as follows:

ARTICLE I

Definitions

Section 1.01. Definitions. Capitalized terms used in this Amendment, to the extent not otherwise defined herein, shall have the same meanings as in the Agreement, as amended hereby.

Section 1.02. Amendment to Name of Lender. Effective as of April 1, 1999 Bank of America National Trust and Savings Association became the successor-in-interest to Bank America Business Credit, Inc. All references in the Agreement and in each Loan Document to "BankAmerica Business Credit, Inc." or "BABC" are now amended to refer to "Bank of America National Trust and Savings Association" which is the "Lender" under the Agreement and the other Loan Documents.

Section 1.03. New Definition. The following definition is hereby added to the Agreement:

> "Early Termination Fee" means a single fee of $500,000 which shall be jointly and severally due and owing from the LSB Consolidated Borrowing Group if, prior to December 31, 2000, any of the LSB-Related Loan Agreements are terminated other than in accordance with their terms.

ARTICLE II

Amendments

Section 2.01 Amendment to Section 9.16. Section 9.16 of the Agreement is hereby amended to read in its entirety as follows:

> "9.16 At all times (i) prior to the Automotive Termination Date and (ii) after the Automotive Termination Date but only if a Springing Covenant Event has occurred whereafter such financial covenant shall remain in effect until the termination of this Agreement, the following

financial covenant shall be in effect:

CCI Adjusted Tangible Net Worth. The CCI Adjusted Tangible Net Worth will not be less than the following amounts at the end of each of the Fiscal Quarters during the following Fiscal Years:

Fiscal Quarters in the Following Fiscal Years	Amount
First Fiscal Quarter during Fiscal Year Ending December 31, 1999	$14,500,000*
Second Fiscal Quarter during Fiscal Year Ending December 31, 1999	$19,500,000*
Third Fiscal Quarter during Fiscal Year Ending December 31, 1999	$21,500,000*
Fourth Fiscal Quarter during Fiscal Year Ending December 31, 1999	$23,500,000*

Fiscal Quarters in the Following Fiscal Years	Amount
First Fiscal Quarter during Fiscal Year Ending December 31, 2000 and each Fiscal Quarter during each Fiscal Year ending thereafter:	The CCI Adjusted Tangible Net Worth as of December 31, 1999 plus fifty percent (50%) of CCI's profits for the fiscal quarter then ending without taking into account any losses, plus all cash dividends to LSB from December 31, 1999."

* Includes all Distributions to LSB made after January 1, 1999

Section 2.02. Amendment to Section 9.17. Section 9.17 of the Agreement is hereby amended to read in its entirety as follows:

"9.17 At all times (i) prior to the Automotive Termination Date and (ii) after the Automotive Termination Date but only if a Springing Covenant Event has occurred whereafter such financial covenant shall remain in effect until the termination of this Agreement, the following financial covenant shall be in effect:

Debt Ratio. The ratio of Debt of the CCI Consolidated Group to the CCI Adjusted Tangible Net Worth will not be greater than the following ratios at the end of each of the Fiscal Quarters during the following Fiscal Years:

Fiscal Quarters in the Following Fiscal Years	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Fiscal Year Ending December 31, 1999	10:1	7.6:1	6.9:1	6.3:1
Fiscal Year Ending December 31, 1999 and	6.3:1	6.3:1	6.3:1	6.3:1

Each Fiscal Quarter during each Fiscal Year ending thereafter: 6.3:1

Section 2.03. Amendment to Article 12. Article 12 of the Agreement is hereby amended to read in its entirety as follows:

"12. TERM AND TERMINATION. The term of this Agreement shall extend until December 31, 2000 (the "Termination Date"). This Agreement shall automatically be renewed thereafter for successive terms of thirteen (13) months each, unless this Agreement is terminated as provided below. The Lender and the Borrower shall each have the right to terminate this Agreement, without premium or penalty, at the end of the initial term or at the end of any renewal term by giving the other written notice not less than sixty (60) days prior to the end of such term by registered or certified mail. The Borrower may also terminate this Agreement at any time during its initial term or any renewal periods if: (a) it gives the Lender sixty (60) days prior written notice of termination by registered or certified mail; (b) it pays and performs all Obligations on or prior to the effective date of termination; and (c) except as otherwise provided herein, it pays the Lender, on or prior to the effective date of termination, the Early Termination Fee if such termination is made prior to the Termination Date. The Lender may also terminate this Agreement without notice upon an Event of Default that has not been cured or otherwise waived to Lender's satisfaction. Upon the effective date of termination of this Agreement for any reason whatsoever, all Obligations shall become immediately due and payable. Notwithstanding the termination of this Agreement, until all Obligations are paid and performed in full, the Lender shall retain all its rights and remedies hereunder (including, without limitation, in all then existing and after-arising Collateral)."

ARTICLE III

Waivers

Section 3.01. Waiver of Events of Default.

(a) The Lender hereby waives the following Events of Default: (i) the CCI Adjusted Tangible Net Worth for the Fiscal Quarter ending December 31, 1998 was less than $18,500,000, in breach of Section 9.16 of the Loan Agreement; and (ii) the CCI Consolidated Group's Debt Ratio for the Fiscal Quarter ending December 31, 1998 was greater than 7.75 to 1.0, in breach of Section 9.17 of the Loan Agreement.

(b) The foregoing waiver is only applicable to and shall only be effective to the extent described above. The waiver is limited to the facts and circumstances referred to herein and shall not operate as (i) a waiver of or consent to non-compliance with any other section or provision of the Loan Agreement, (ii) a waiver of any right, power, or remedy of the Lender under the Loan Agreement (except as provided herein), or (iii) a waiver of any other Event of Default or Event which may exist under the Loan Agreement.

ARTICLE IV

Ratifications, Representations and Warranties

Section 4.01. Ratifications. The terms and provisions set forth in this Amendment shall modify and supersede all inconsistent terms and provisions set forth in the Agreement and, except as expressly modified and superseded by this Amendment, the terms and provisions of the Agreement, including, without limitation, all financial covenants contained therein, are ratified and confirmed and shall continue in full force and effect. Lender and Borrower agree that the Agreement as amended hereby shall continue to be legal, valid, binding and enforceable in accordance with its terms.

Section 4.02. Representations and Warranties. Borrower hereby represents and warrants to Lender that the execution, delivery and performance of this Amendment and all other loan, amendment or security documents to which Borrower is or is to be a party hereunder (hereinafter referred to collectively as the "Loan Documents") executed and/or delivered in connection herewith, have been authorized by all requisite corporate action on the part of Borrower and will not violate the Articles of Incorporation or Bylaws of Borrower.

ARTICLE V

Conditions Precedent

Section 5.01. Conditions. The effectiveness of this Amendment is subject to the satisfaction of the following conditions precedent (unless specifically waived in writing by the Lender):

(a) Lender shall have received all of the following, each dated (unless otherwise indicated) as of the date of this Amendment, in form and substance satisfactory to Lender in its sole discretion:

(i) Company Certificate. A certificate executed by the Secretary or Assistant Secretary of Borrower certifying (A) that Borrower's Board of Directors has met and adopted, approved, consented to and ratified the resolutions attached thereto which authorize the execution, delivery and performance by Borrower of the Amendment and the Loan Documents, (B) the names of the officers of Borrower authorized to sign this Amendment and each of the Loan Documents to which Borrower is to be a party hereunder, (C) the specimen signatures of such officers, and (D) that neither the Articles of Incorporation nor Bylaws of Borrower have been amended since the date of the Agreement;

(ii) No Material Adverse Change. There shall have occurred no material adverse change in the business, operations, financial condition, profits or prospects of Borrower, or in the Collateral since January 31, 1999, and the Lender shall have received a certificate of Borrower's chief executive officer to such effect;

(iii) Other Documents. Borrower shall agree to execute and deliver such other documents and instruments including, but not limited to, UCC assignments reflecting "Bank of America National Trust and Savings Association" as assignee, as well as such record searches as Lender may require.

(b) All corporate proceedings taken in connection with the transactions contemplated by this Amendment and all documents, instruments and other legal matters incident thereto shall be satisfactory to Lender and its legal counsel, Jenkes & Gilchrist, a Professional Corporation.

(c) Amendment Fee. Borrower shall have paid to Lender a fee of $100,000.

ARTICLE VI

Miscellaneous

Section 6.01. Survival of Representations and Warranties. All representations and warranties made in the Agreement or any other document or documents relating thereto, including, without limitation, any Loan Document furnished in connection with this

Amendment, shall survive the execution and delivery of this Amendment and the other Loan Documents, and no investigation by Lender or any closing shall affect the representations and warranties or the right of Lender to rely thereon.

Section 6.02. Reference to Agreement. The Agreement, each of the Loan Documents, and any and all other agreements, documents or instruments now or hereafter executed and delivered pursuant to the terms hereof or pursuant to the terms of the Agreement as amended hereby, are hereby amended so that any reference therein to the Agreement shall mean a reference to the Agreement as amended hereby.

Section 6.03. Severability. Any provision of this Amendment held by a court of competent jurisdiction to be invalid or unenforceable shall not impair or invalidate the remainder of this Amendment and the effect thereof shall be confined to the provision so held to be invalid or unenforceable.

Section 6.04. APPLICABLE LAW. THIS AMENDMENT AND ALL OTHER LOAN DOCUMENTS EXECUTED PURSUANT HERETO SHALL BE DEEMED TO HAVE BEEN MADE AND TO BE PERFORMABLE IN THE STATE OF OKLAHOMA AND SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF OKLAHOMA.

Section 6.05. Successors and Assigns. This Amendment is binding upon and shall inure to the benefit of Lender and Borrower and their respective successors and assigns; provided, however, that Borrower may not assign or transfer any of its rights or obligations hereunder without the prior written consent of Lender. Lender may assign any or all of its rights or obligations hereunder without the prior consent of Borrower.

Section 6.06. Counterparts. This Amendment may be executed in one or more counterparts, each of which when so executed shall be deemed to be an original, but all of which when taken together shall constitute one and the same instrument.

Section 6.07. Effect of Waiver. No consent or waiver, express or implied, by Lender to or of any breach of or deviation from any covenant or condition of the Agreement or duty shall be deemed a consent or waiver to or of any other breach of or deviation from the same or any other covenant, condition or duty. No failure on the part of Lender to exercise and no delay in exercising, and no course of dealing with respect to, any right, power, or privilege under this Amendment, the Agreement or any other Loan Document shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power, or privilege under this Amendment, the Agreement or any other Loan Document preclude any other or further exercise thereof or the exercise of any other right, power, or privilege. The rights and remedies provided for in the Agreement and the other Loan Documents are cumulative and not exclusive of any rights and remedies provided by law.

Section 6.08. Headings. The headings, captions and arrangements used in this Amendment are for convenience only and shall not affect the interpretation of this Amendment.

Section 6.09. Releases. As a material inducement to Lender to enter into this Amendment, Borrower hereby represents and warrants that there are no claims or offsets against, or defenses or counterclaims to, the terms and provisions of and the other obligations created or evidenced by the Agreement or the other Loan Documents. Borrower hereby releases, acquits, and forever discharges Lender, and its successors, assigns, and predecessors in interest, their parents, subsidiaries and affiliated organizations, and the officers, employees, attorneys, and agents of each of the foregoing (all of whom are herein jointly and severally referred to as the "Released Parties") from any and all liability, damages, losses, obligations, costs, expenses, suits, claims, demands, causes of action for damages or any other relief, whether or not now known or suspected, of any kind, nature, or character, at law or in equity, which Borrower now has or may have ever had against any of the Released Parties, including, but not limited to, those relating to (a) usury or penalties or damages therefor, (b) allegations that a partnership existed between Borrower and the Released Parties, (c) allegations of unconscionable acts, deceptive trade practices, lack of good faith or fair dealing, lack of commercial reasonableness or special relationships, such as fiduciary, trust or confidential relationships, (d) allegations of dominion, control, alter ego, instrumentality, fraud, misrepresentation, duress, coercion, undue influence, interference or negligence, (e) allegations of tortious interference with present or prospective business relationships or of antitrust, or (f) slander, libel or damage to reputation, (hereinafter being collectively referred to as the "Claims"), all of which Claims are hereby waived.

Section 6.10. Expenses of Lender. Borrower agrees to pay on demand (i) all costs and expenses reasonably incurred by Lender in connection with the preparation, negotiation and execution of this Amendment and the other Loan Documents executed pursuant hereto and any and all subsequent amendments, modifications, and supplements hereto or thereto, including, without limitation, the costs and fees of Lender's legal counsel and the allocated cost of staff counsel and (ii) all costs and expenses reasonably incurred by Lender in connection with the enforcement or preservation of any rights under the Agreement, this Amendment and/or other Loan Documents, including, without limitation, the costs and fees of Lender's legal counsel and the allocated cost of staff counsel.

Section 6.11. NO ORAL AGREEMENTS. THIS AMENDMENT, TOGETHER WITH THE OTHER LOAN DOCUMENTS AS WRITTEN, REPRESENT THE FINAL AGREEMENTS BETWEEN LENDER AND BORROWER AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES. THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN LENDER AND BORROWER.

IN WITNESS WHEREOF, the parties have executed this Amendment on the date first above written.

"BORROWER":

CLIMATE MASTER, INC.

By: /s/ Tony M. Shelby
Tony M. Shelby
Vice President

INTERNATIONAL ENVIRONMENTAL
CORPORATION

By: /s/ Tony M. Shelby
Tony M. Shelby
Vice President

EL DORADO CHEMICAL COMPANY

By: /s/ Tony M. Shelby
Tony M. Shelby
Vice President

SLURRY EXPLOSIVE CORPORATION

By: /s/ Tony M. Shelby
Tony M. Shelby
Vice President

"LENDER"

BANK OF AMERICA NATIONAL TRUST AND
SAVINGS ASSOCIATION

By: /s/ Michael J. Jasaitis

Michael J. Jasaitis, Vice President

CONSENTS AND REAFFIRMATIONS

The undersigned hereby acknowledges the execution of, and consents to, the terms and conditions of that certain Fifth Amendment to Amended and Restated Loan and Security Agreement dated as of April 8, 1999, between Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Corporation, Slurry Explosive Corporation and Bank of America National Trust and Savings Association ("Creditor") and reaffirms its obligations under that certain Continuing Guaranty (the "Guaranty") dated as of November 21, 1997, made by the undersigned in favor of the Creditor, and acknowledges and agrees that the Guaranty remains in full force and effect and the Guaranty is hereby ratified and confirmed.

Dated as of April 8, 1999.

CLIMACHEM, INC.

By: /s/ Tony M. Shelby
____
Tony M. Shelby, Vice President

CONSENTS AND REAFFIRMATIONS

Each of the undersigned hereby acknowledges the execution of, and consents to, the terms and conditions of that certain Fifth Amendment to Amended and Restated Loan and Security Agreement dated as of April 8, 1999, between Climate Master, Inc., International Environmental Corporation, El Dorado Chemical Corporation, Slurry Explosive Corporation and Bank of America National Trust and Savings Association ("Creditor") and each reaffirms its obligations under that certain Continuing Guaranty with Security Agreement (the "Guaranty") dated as of November 21, 1997, and acknowledges and agrees that such Guaranty remains in full force and effect and each Guaranty is hereby ratified and confirmed.

Dated as of April 8, 1999.

LSB INDUSTRIES, INC.
LSB CHEMICAL CORP.
SUMMIT MACHINE TOOL MANUFACTURING CORP.
MOREY MACHINERY MANUFACTURING CORPORATION
CHP CORPORATION
KOAX CORP.
APR CORPORATION
CLIMATE MATE, INC.
THE ENVIRONMENTAL GROUP, INC.
UNIVERSAL TECH CORPORATION

By: /s/ Tony M. Shelby
____
Tony M. Shelby, Vice President
acting on behalf of each of
the above

L&S AUTOMOTIVE PRODUCTS CO.
L&S BEARING CO.
INTERNATIONAL BEARINGS, INC.
LSB EXTRUSION CO.
ROTEX CORPORATION
TRIBONETICS CORPORATION

By: /s/ David R. Goss
____
David R. Goss, Vice Chairman
acting on behalf of each of
the above

FIFTH AMENDMENT
TO AMENDED AND RESTATED
LOAN AND SECURITY AGREEMENT

THIS FIFTH AMENDMENT TO AMENDED AND RESTATED LOAN AND SECURITY AGREEMENT (the "Amendment") is dated as of April 8, 1999, and entered into by and between BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION (successor-in-interest to BANKAMERICA BUSINESS CREDIT, INC.) ("Lender") and LSB INDUSTRIES, INC. ("Borrower").

WHEREAS, Lender and Borrower have entered into that certain Amended and Restated Loan and Security Agreement dated as of November 21, 1997 as amended by that certain First Amendment to Amended and Restated Loan and Security Agreement dated as of March 12, 1998, that certain Second Amendment to Amended and Restated Loan and Security Agreement dated as of June 30, 1998, that certain Third Amendment to Amended and Restated Loan and Security Agreement dated as of August 14, 1998, and that certain Fourth Amendment to Amended and Restated Loan and Security Agreement dated as of November 19, 1998 (as so amended, the "Agreement");

WHEREAS, two Events of Default have occurred under the Agreement;

WHEREAS, the Borrower desires that the Lender waive the Events of Default and amend the Agreement in certain respects; and

WHEREAS, the Lender is willing to waive the Events of Default and amend the Agreement subject to the terms and conditions contained herein;

NOW, THEREFORE, in consideration of the mutual conditions and agreements set forth in the Agreement and this Amendment, and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties, intending to be legally bound, hereby agree as follows:

ARTICLE I

Definitions

Section 1.01. Definitions. Capitalized terms used in this Amendment, to the extent not otherwise defined herein, shall have the same meanings as in the Agreement, as amended hereby.

Section 1.02. Amendment to Name of Lender. Effective as of April 1, 1999 Bank of America National Trust and Savings Association became the successor-in-interest to Bank America Business Credit, Inc. All references in the Agreement and in each Loan Document to "BankAmerica Business Credit, Inc." or "BABC" are now amended to refer to "Bank of America National Trust and Savings Association" which is the "Lender" under the Agreement and the other Loan Documents.

Section 1.03. New Definition. The following definition is hereby added to the Agreement:

> "Early Termination Fee" means a single fee of $500,000 which shall be jointly and severally due and owing from the LSB Consolidated Borrowing Group if, prior to December 31, 2000, any of the LSB-Related Loan Agreements are terminated other than in accordance with their terms.

ARTICLE II

Amendments

Section 2.01. Amendment to Section 9.16. Section 9.16 of the Agreement is hereby amended to read in its entirety as follows:

> "9.16 At all times (i) prior to the Automotive Termination Date and (ii) after the Automotive Termination Date but only if a Springing Covenant Event has occurred whereafter such financial covenant shall remain in effect until the termination of this Agreement, the following financial covenant shall be in effect:

LSB Adjusted Tangible Net Worth. The LSB Adjusted Tangible Net Worth increased by an amount equal to the purchase price paid by Borrower for its treasury stock for purchases from January 1, 1998 through termination of this Agreement, which amount shall not exceed $6,000,000, will not be less than the following amounts at the end of each of the Fiscal Quarters during the following Fiscal Years:

Fiscal Quarters in Following Fiscal Years	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Fiscal Quarter during Fiscal Year Ending December 31, 1999:	$21,300,000	$23,600,000	$24,000,000	$23,500,000
First Fiscal Quarter during Fiscal Year Ending December 31, 2000:	The LSB Adjusted Tangible Net Worth as of December 31, 1999 less $4,500,000 and less all dividends paid by LSB in cash from January 1, 2000 until the date of calculation.			
Second Fiscal Quarter during Fiscal Year Ending December 31, 2000:	The LSB Adjusted Tangible Net Worth as of March 31, 2000 plus fifty percent (50%) of the profits for the fiscal quarter then ending, if any, with no deductions for losses, less all dividends paid by LSB in cash from January 1, 2000 until the date of calculation.			
Third Fiscal Quarter during Fiscal Year Ending December 31, 2000 and each Fiscal Quarter during each Fiscal Year ending thereafter	The LSB Adjusted Tangible Net Worth as of June 30, 2000 plus fifty percent (50%) of the profits for the fiscal quarter then ending, if any, with no deductions for losses, less all dividends paid by LSB in cash from January 1, 2000 until the date of calculation.			

Section 2.02. Amendment to Section 9.17. Section 9.17 of the Agreement is hereby amended to read in its entirety as follows:

"9.17 At all times (i) prior to the Automotive Termination Date and (ii) after the Automotive Termination Date but only if a Springing Covenant Event has occurred whereafter such financial covenant shall remain in effect until the termination of this Agreement, the following financial covenant shall be in effect:

LSB Debt Ratio. The ratio of Debt of the LSB Consolidated Borrowing Group to the LSB Adjusted Tangible Net Worth increased by an amount equal to the purchase price paid by Borrower for its treasury stock for purchases from January 1, 1998 through termination of this Agreement, which amount shall not exceed $6,000,000, will not be greater than the following ratios at the end of each of the Fiscal Quarters during the following Fiscal Years:

Fiscal Quarters in the Following Fiscal Years	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
Fiscal Year Ending December 31, 1999	9.3:1	8.4:1	8.1:1	8.1:1
Fiscal Year Ending December 31, 2000	8.1:1	8.1:1	8.1:1	8.1:1

Each Fiscal Quarter during each Fiscal Year ending thereafter: 8.1:1

Section 2.03. Amendment to Article 12 of the Agreement. Article 12 of the Agreement is hereby amended to read in its entirety as follows:

"12. TERM AND TERMINATION. The term of this Agreement shall extend until December 31, 2000 (the "Termination Date"). This Agreement shall automatically be renewed thereafter for successive terms of thirteen (13) months each, unless this Agreement is terminated as provided below. The Lender and the Borrower shall each have the right to terminate this Agreement, without premium or penalty, (i) at the end of the initial term or at the end of any renewal term by giving the other written notice not less than sixty (60) days prior to the end of such term by registered or certified mail, or (ii) as provided in Section 6.16. The Borrower may also terminate this Agreement at any time during its initial term or any renewal periods if: (a) it gives the Lender sixty (60) days prior written notice of termination by registered or certified mail; (b) it pays all Revolving Loans and reimburses Lender for all Letter of Credit obligations under this Agreement on or prior to the effective date of termination; and (c) except as otherwise provided herein, it pays the Lender, on or prior to the effective date of termination, the Early Termination Fee if such termination is made prior to the Termination Date. The Lender may also terminate this Agreement without notice upon an Event of Default that has not been cured or otherwise waived to Lender's satisfaction. Upon the effective date of termination of this Agreement for any reason whatsoever, all Obligations shall become immediately due and payable. Notwithstanding the termination of this Agreement, until all Obligations are paid and performed in full, the Lender shall retain all its rights and remedies hereunder (including, without limitation, in all then existing and after-arising Collateral) except as otherwise provided in Section 6.16 of this Agreement."

ARTICLE III

Waivers

Section 3.01. Waiver of Events of Default.

(a) The Lender hereby waives the following Events of Default: (i) the LSB Consolidated Borrowing Group's Adjusted Tangible Net Worth for the Fiscal Quarter ending December 31, 1998 was less than $34,500,000, in breach of Section 9.16 of the Loan Agreement; and (ii) the LSB Consolidated Borrowing Group's Debt Ratio for the Fiscal Quarter ending December 31, 1998 was greater than 5.00 to 1.0, in breach of Section 9.17 of the Loan Agreement.

(b) The foregoing waiver is only applicable to and shall only be effective to the extent described above. The waiver is limited to the facts and circumstances referred to herein and shall not operate as (i) a waiver of or consent to non-compliance with any other section or provision of the Loan Agreement, (ii) a waiver of any right, power, or remedy of the Lender under the Loan Agreement (except as provided herein), or (iii) a waiver of any other Event of Default or Event which may exist under the Loan Agreement.

ARTICLE IV

Ratifications, Representations and Warranties

Section 4.01. Ratifications. The terms and provisions set forth in this Amendment shall modify and supersede all inconsistent terms and provisions set forth in the Agreement and, except as expressly modified and superseded by this Amendment, the terms and provisions of the Agreement, including, without limitation, all financial covenants contained therein, are ratified and confirmed and shall continue in full force and effect. Lender and Borrower agree that the Agreement as amended hereby shall continue to be legal, valid, binding and enforceable in accordance with its terms.

Section 4.02. Representations and Warranties. Borrower hereby represents and warrants to Lender that the execution, delivery and performance of this Amendment and all other loan, amendment or security documents to which Borrower is or is to be a party hereunder (hereinafter referred to collectively as the "Loan Documents") executed and/or delivered in connection herewith, have been authorized by all requisite corporate action on the part of Borrower and will not violate the Articles of Incorporation or Bylaws of Borrower.

ARTICLE V

Conditions Precedent

Section 5.01. Conditions. The effectiveness of this Amendment is subject to the satisfaction of the following conditions precedent (unless specifically waived in writing by the Lender):

(a) Lender shall have received all of the following, each dated (unless otherwise indicated) as of the date of this Amendment, in form and substance satisfactory to Lender in its sole discretion:

(i) Company Certificate. A certificate executed by the Secretary or Assistant Secretary of Borrower certifying (A) that Borrower's Board of Directors has met and adopted, approved, consented to and ratified the resolutions attached thereto which authorize the execution, delivery and performance by Borrower of the Amendment and the Loan Documents, (B) the names of the officers of Borrower authorized to sign this Amendment and each of the Loan Documents to which Borrower is to be a party hereunder, (C) the specimen signatures of such officers, and (D) that neither the Articles of Incorporation nor Bylaws of Borrower have been amended since the date of the Agreement;

(ii) No Material Adverse Change. There shall have occurred no material adverse change in the business, operations, financial condition, profits or prospects of Borrower, or in the Collateral since January 31, 1999, and the Lender shall have received a certificate of Borrower's chief executive officer to such effect;

(iii) Other Documents. Borrower shall agree to execute and deliver such other documents and instruments including, but not limited to, UCC assignments reflecting "Bank of America National Trust and Savings Association" as assignee, as well as such record searches as Lender may require.

(b) All corporate proceedings taken in connection with the transactions contemplated by this Amendment and all documents, instruments and other legal matters incident thereto shall be satisfactory to Lender and its legal counsel, Jenkens & Gilchrist, a Professional Corporation.

ARTICLE VI

Miscellaneous

Section 6.01. Survival of Representations and Warranties. All representations and warranties made in the Agreement or any other document or documents relating thereto, including, without limitation, any Loan Document furnished in connection with this Amendment, shall survive the execution and delivery of this Amendment and the other Loan Documents, and no investigation by Lender or any closing shall affect the representations and warranties or the right of Lender to rely thereon.

Section 6.02. Reference to Agreement. The Agreement, each of the Loan Documents, and any and all other agreements, documents or instruments now or hereafter executed and delivered pursuant to the terms hereof or pursuant to the terms of the Agreement as amended hereby, are hereby amended so that any reference therein to the Agreement shall mean a reference to the Agreement as amended hereby.

Section 6.03. Severability. Any provision of this Amendment held by a court of competent jurisdiction to be invalid or unenforceable shall not impair or invalidate the remainder of this Amendment and the effect thereof shall be confined to the provision so held to be invalid or unenforceable.

Section 6.04. APPLICABLE LAW. THIS AMENDMENT AND ALL OTHER LOAN DOCUMENTS EXECUTED PURSUANT HERETO SHALL BE DEEMED TO HAVE BEEN MADE AND TO BE PERFORMABLE IN THE STATE OF OKLAHOMA AND SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF OKLAHOMA.

Section 6.05. Successors and Assigns. This Amendment is binding upon and shall inure to the benefit of Lender and Borrower and their respective successors and assigns; provided, however, that Borrower may not assign or transfer any of its rights or obligations hereunder without the prior written consent of Lender. Lender may assign any or all of its rights or obligations hereunder without the prior consent of Borrower.

Section 6.06. Counterparts. This Amendment may be executed in one or more counterparts, each of which when so executed shall be deemed to be an original, but all of which when taken together shall constitute one and the same instrument.

Section 6.07. Effect of Waiver. No consent or waiver, express or implied, by Lender to or of any breach of or deviation from any covenant or condition of the Agreement or duty shall be deemed a consent or waiver to or of any other breach of or deviation from the same or any other covenant, condition or duty. No failure on the part of Lender to exercise and no delay in exercising, and no course of dealing with respect to, any right, power, or privilege under this Amendment, the Agreement or any other Loan Document shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power, or privilege under this Amendment, the Agreement or any other Loan Document preclude any other or further exercise thereof or the exercise of any other right, power, or privilege. The rights and remedies provided for in the Agreement and the other Loan Documents are cumulative and not exclusive of any rights and remedies provided by law.

Section 6.08. Headings. The headings, captions and arrangements used in this Amendment are for convenience only and shall not affect the interpretation of this Amendment.

Section 6.09. Releases. As a material inducement to Lender to enter into this Amendment, Borrower hereby represents and warrants that there are no claims or offsets against, or defenses or counterclaims to, the terms and provisions of and the other obligations created or evidenced by the Agreement or the other Loan Documents. Borrower hereby releases, acquits, and forever discharges Lender, and its successors, assigns, and predecessors in interest, their parents, subsidiaries and affiliated organizations, and the officers, employees, attorneys, and agents of each of the foregoing (all of whom are herein jointly and severally referred to as the "Released Parties") from any and all liability, damages, losses, obligations, costs, expenses, suits, claims, demands, causes of action for damages or any other relief, whether or not now known or suspected, of any kind, nature, or character, at law or in equity, which Borrower now has or may have ever had against any of the Released Parties, including, but not limited to, those relating to (a) usury or penalties or damages therefor, (b) allegations that a partnership existed between Borrower and the Released Parties, (c) allegations of unconscionable acts, deceptive trade practices, lack of good faith or fair dealing, lack of commercial reasonableness or special relationships, such as fiduciary, trust or confidential relationships, (d) allegations of dominion, control, alter ego, instrumentality, fraud, misrepresentation, duress, coercion, undue influence, interference or negligence, (e) allegations of tortious interference with present or prospective business relationships or of antitrust, or (f) slander, libel or damage to reputation, (hereinafter being collectively referred to as the "Claims"), all of which Claims are hereby waived.

Section 6.10. Expenses of Lender. Borrower agrees to pay on demand (i) all costs and expenses reasonably incurred by Lender in connection with the preparation, negotiation and execution of this Amendment and the other Loan Documents executed pursuant hereto and any and all subsequent amendments, modifications, and supplements hereto or thereto, including, without limitation, the costs and fees of Lender's legal counsel and the allocated cost of staff counsel and (ii) all costs and expenses reasonably incurred by Lender in connection with the enforcement or preservation of any rights under the Agreement, this Amendment and/or other Loan Documents, including, without limitation, the costs and fees of Lender's legal counsel and the allocated cost of staff counsel.

Section 6.11. NO ORAL AGREEMENTS. THIS AMENDMENT, TOGETHER WITH THE OTHER LOAN DOCUMENTS AS WRITTEN, REPRESENT THE FINAL AGREEMENTS BETWEEN LENDER AND BORROWER AND MAY NOT BE CONTRADICTED BY EVIDENCE OF PRIOR, CONTEMPORANEOUS OR SUBSEQUENT ORAL AGREEMENTS OF THE PARTIES. THERE ARE NO UNWRITTEN ORAL AGREEMENTS BETWEEN LENDER AND BORROWER.

IN WITNESS WHEREOF, the parties have executed this Amendment on the date first above written.

"BORROWER"

LSB INDUSTRIES, INC.

By: /s/ Tony M. Shelby
____
Tony M. Shelby, Vice President

"LENDER"

BANK OF AMERICA NATIONAL TRUST AND
SAVINGS ASSOCIATION

By: /s/ Michael J. Jasaitis
____
Michael J. Jasaitis, Vice President

ACKNOWLEDGED AND AGREED TO:

Each of the following "LSB Guarantor Subsidiaries" hereby acknowledges the execution of and consents to the terms and conditions of that certain Fifth Amendment to Amended and Restated Loan and Security Agreement dated as of April 8, 1999 between LSB Industries, Inc., and Lender.

MOREY MACHINE TOOL MANUFACTURING
CORPORATION

By: /s/ Tony M. Shelby
____
Tony M. Shelby,
Vice President acting on behalf of
each of the above.

L&S AUTOMOTIVE PRODUCTS, CO.
LSB EXTRUSION CO.
INTERNATIONAL BEARINGS, INC.
ROTEX CORPORATION
TRIBONETICS CORPORATION

By: /s/ David R. Goss
____
David R. Goss,
Vice Chairman acting on behalf of
each of the above.

CONSENTS AND REAFFIRMATIONS

Each of the undersigned hereby acknowledges the execution of, and consents to, the terms and conditions of that certain Fifth Amendment to Amended and Restated Loan and Security Agreement dated as of April 8, 1999, between LSB Industries, Inc. and Bank of America National Trust and Savings Association ("Creditor") and reaffirms its obligations under (i) that certain Continuing Guaranty with Security Agreement (the "Guaranty") dated as of November 21, 1997, and (ii) that certain Cross-Collateralization and Cross-Guaranty Agreement (the "Cross-Collateralization Agreement") dated as of November 21, 1997, each made by the undersigned in favor of the Creditor, and acknowledges and agrees that the Guaranty and the Cross-Collateralization Agreement remain in full force and effect and the Guaranty and the Cross-Collateralization Agreement are hereby ratified and confirmed.

Dated as of April 8, 1999.

LSB INDUSTRIES, INC.
SUMMIT MACHINE TOOL MANUFACTURING CORP.
MOREY MACHINERY MANUFACTURING CORPORATION

By: /s/ Tony M. Shelby
____
Tony M. Shelby, Vice President acting on behalf of each of the above

L&S BEARING CO.
L&S AUTOMOTIVE PRODUCTS CO.
INTERNATIONAL BEARINGS, INC.
LSB EXTRUSION CO.
ROTEX CORPORATION
TRIBONETICS CORPORATION

By: /s/ David R. Goss
____
David R. Goss, Vice Chairman acting on behalf of each of the above

CLIMACHEM, INC.
as Issuer

THE GUARANTORS
named herein

and

BANK ONE, N.A.
As Trustee

FIRST SUPPLEMENTAL INDENTURE

Dated as of February 8, 1999

Supplementing and Amending the Indenture

Dated as of November 26, 1997

$105,000,000 10 3/4% Senior Notes Due 2007

FIRST SUPPLEMENTAL INDENTURE

This First Supplemental Indenture, dated as of February 8, 1999, is by and among ClimaChem, Inc., an Oklahoma corporation (the "Company"), The Environmental Group, Inc., an Oklahoma corporation, International Environmental Corporation, an Oklahoma corporation, Climate Master, Inc., a Delaware corporation, CHP corporation, an Oklahoma corporation, KOAX Corp., an Oklahoma corporation, APR Corporation, an Oklahoma corporation, Climate Mate, Inc., a corporation organized under the laws of Canada, The Environmental Group International Limited, a corporation organized under the laws of England, LSB Chemical Corp., an Oklahoma corporation, El Dorado Chemical Company, an Oklahoma corporation, Slurry Explosive Corporation, an Oklahoma corporation, Universal Tech Corporation, an Oklahoma corporation, Total Energy Systems Limited, a corporation organized under the laws of Queenstown, Australia, Total Energy Systems (NZ) Ltd., a corporation organized under the laws of New Zealand, T.E.S. Mining Services Pty. Ltd., a corporation organized under the laws of Queensland, Australia, Northwest Financial Corporation, an Oklahoma corporation, DSN Corporation, an Oklahoma corporation (collectively, the "Guarantors"), Total Energy Systems (International) Pty Ltd., a corporation organized under the laws of Queensland, Australia ("TESI"), ClimateCraft, Inc., an Oklahoma corporation ("CLCR"), ACP Manufacturing Corp., an Oklahoma corporation ("ACP"), ThermalClime, Inc., an Oklahoma corporation ("Thermal"), and Bank One, N.A., as trustee (the "Trustee").

RECITALS

WHEREAS, the Company, the Guarantors and the Trustee are parties to that certain Indenture, dated as of November 26, 1997, (the "Indenture"), pursuant to which the 10 3/4% Senior Notes due 2007 (the "Notes") were issued; and

WHEREAS, the Company was issued all of the issued and outstanding shares of stock of CLCR, ACP and Thermal, thereby causing CLCR, ACP and Thermal to be Wholly Owned Subsidiaries of the Company; and

WHEREAS, Total Energy Systems Limited, a Wholly Owned Subsidiary of the Company, was issued all of the issued and outstanding shares of stock of TESI, thereby causing TESI to be an indirect Wholly Owned Subsidiary of the Company; and

WHEREAS, Section 11.5 of the Indenture provides that the Company shall cause any person that becomes a Subsidiary of the Company or any Guarantor to promptly execute and deliver to the Trustee a supplemental indenture pursuant to which such Subsidiary shall become a Guarantor under Article 11 of the Indenture and shall guarantee the

Notes pursuant to the terms thereof; and

WHEREAS, capitalized terms used herein and not otherwise defined are used as defined in the Indenture.

NOW, THEREFORE, in consideration of these premises and for other good and valuable consideration, the receipt and adequacy of which is hereby acknowledged, the Company, the Guarantors, TESI, CLCR, ACP and Thermal agree as follows for the benefit of each other, the Trustee and the equal and ratable benefit of the Holders of the Notes, and hereby amend and supplement the Indenture as follows:

Section 1. Addition of Guarantors. In accordance with Section 11.5 ofthe Indenture, TESI, CLCR, ACP and Thermal each agree to become a Guarantor under Article 11 of the Indenture and hereby guarantees the Notes pursuant to the terms thereof.

Section 2. Modification of Indenture. Upon the execution and delivery of this First Supplemental Indenture, the Indenture shall be modified to reflect the addition of TESI, CLCR, ACP and Thermal as Guarantors under the Indenture, and this First Supplemental Indenture shall form a part of the Indenture for all purposes.

Section 3. Ratification. Except to the extent amended by or inconsistent with this First Supplemental Indenture, the Company, the Guarantors, TESI, CLCR, ACP, Thermal and the Trustee hereby ratify and reconfirm the Indenture in its entirety.

Section 4. Miscellaneous.

A. Counterparts. This First Supplemental Indenture may be executed in any number of counterparts, each of which so executed shall be an original, but all such counterparts shall together constitute but one and the same instrument.

B. Meaning of Terms. Any capitalized terms used in this First Supplemental Indenture and not defined herein shall have the meanings specified in the Indenture, unless the context shall otherwise require.

C. Governing Law. THIS FIRST SUPPLEMENTAL INDENTURE SHALL BE GOVERNED BY, AND CONSTRUED AND ENFORCED IN ACCORDANCE WITH, THE INTERNAL LAW OF THE STATE OF NEW YORK.

IN WITNESS WHEREOF, the parties hereto have caused this First Supplemental Indenture to be executed as of the date first above written.

CLIMACHEM, INc.

By: /s/ James L. Wewers

Title: Vice President

THE ENVIRONMENTAL GROUP, INC.

By: /s/ Barry H. Golsen

Title: Executive Vice President

INTERNATIONAL ENVIRONMENTAL CORPORATION

By: /s/ Barry H. Golsen

Title: Chief Executive Officer

CLIMATE MASTER, INC.

By: /s/ Barry H. Golsen

Title: Executive Vice President

CHP CORPORATION

By: /s/ Barry H. Golsen

Title: President

KOAX CORP.

By: /s/ Barry H. Golsen
____

Title: President
____

APR CORPORATION

By: /s/ Barry H. Golsen
____

Title: President
____

CLIMATE MATE, INC.

By: David R. Goss
____

Title: President
____

THE ENVIRONMENTAL GROUP
INTERNATIONAL LIMITED

By: /s/ Barry H. Golsen
____

Title: Director
____

LSB CHEMICAL CORP.

By: James L. Wewers
____

Title: President
____

EL DORADO CHEMICAL COMPANY

By: /s/ James L. Wewers
____

Title: President
____

SLURRY EXPLOSIVE CORPORATION

By: /s/ James L. Wewers

Title: Vice President

UNIVERSAL TECH CORPORATION

By: /s/ James L. Wewers

Title: Vice President

TOTAL ENERGY SYSTEMS LIMITED

By: /s/ James L. Wewers

Title: Vice President

TOTAL ENERGY SYSTEMS (NZ) LTD.

By: /s/ James L. Wewers

Title: Director

T.E.S. MINING SERVICES PTY. LTD.

By: /s/ James L. Wewers

Title: Director

NORTHWEST FINANCIAL
CORPORATION

By: /s/ David R. Goss

Title: Vice President

DSN CORPORATION

By: /s/ Barry H. Golsen

Title: President

TOTAL ENERGY SYSTEMS
(INTERNATIONAL) PTY LTD

By:

Title: Director

CLIMATECRAFT, INC.

By: /s/ Barry H. Golsen

Title: Vice President

ACP MANUFACTURING CORP.

By: /s/ Barry H. Golsen

Title: Vice President

THERMALCLIME, INC.

By /s/ Barry H. Golsen

Title: President

BANK ONE, N.A., AS TRUSTEE

By: /s/ David B. Knox

Title: Authorized Signer

GUARANTEE

For value received, ThermalClime, Inc., an Oklahoma company, hereby irrevocably, unconditionally guarantees on a senior basis to the Holder of the Security upon which this Guarantee is endorsed the due and punctual payment, as set forth in the Indenture pursuant to which such Security and this Guarantee were issued, of the principal of, premium (if any) and interest on such Security when and as the same shall ecome due and payable for any reason according to the terms of such Security and Article XI of the Indenture. The Guarantee of the Security upon which this Guarantee is endorsed will not become effective until the Trustee signs the Certificate of authentication on such Security.

THERMALCLIME, INC.

By: /s/ Barry H. Golsen

Name: Barry H. Golsen

Title: President

FIRST AMENDMENT TO
BAYTOWN NITRIC ACID PROJECT AND SUPPLY AGREEMENT*

This First Amendment to Baytown Nitric Acid Project and Supply Agreement (this "Agreement") is made and entered into on February 16, 1999 and effective as of February 1, 1999 (the "Effective Date"), by and among EL DORADO NITROGEN COMPANY, an Oklahoma corporation ("EDNC"), EL DORADO CHEMICAL COMPANY, an Oklahoma corporation ("El Dorado") and BAYER CORPORATION, an Indiana corporation ("Bayer").

Preamble

EDNC, El Dorado and Bayer are parties to that certain Baytown Nitric Acid Project and Supply Agreement dated June 27, 1997 (the "Project and Supply Agreement"). The parties have agreed to amend the Project and Supply Agreement upon and subject to the terms and conditions set forth herein. Therefore, in consideration of the premises and the mutual covenants and agreements set forth herein, the parties hereto, intending to be legally bound, agree as follows:

Agreement

1. Defined Terms and Condition Precedent to Effectiveness. Capitalized terms used herein not otherwise defined herein shall have the meanings ascribed to them in the Project and Supply Agreement.

2. Amendment to Section 1.1 Definition of Additional Capital Investment. Section 1.1 of the Project and Supply Agreement is hereby amended to add the following phrase to the parenthetical clause in the second line of such section, following the words "other than Initial Capital Investments:"

". . . and any other capital investments necessary to render the EDNC Baytown Plant Fully Operational) . . ."

3. Amendment to Section 1.42 Definition of Initial Capital Investment.

(a) Section 1.42 of the Project and Supply Agreement is hereby amended to add a semicolon and the following clause to the end of Section 1.42(ii)(b) thereof (following the words "Base Amount"):

". . . provided, however, that no amount incurred in respect of consulting fees or other Capital Costs Subject to Sharing (other than any costs that were contemplated at the inception of the Project and Supply Agreement and that were not caused by the delay in performance of ICF Kaiser Engineers, Inc. (the "Contractor")) in respect of services rendered to EDNC from and after February 1, 1999 shall be included in the calculation of the Initial Capital Investment under this Section 1.42(ii). Fees paid to Benham Engineering Company in

*INFORMATION IN THIS DOCUMENT HAS BEEN OMITTED FROM THIS PUBLIC FILING PURSUANT TO A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

respect of construction supervision services incurred after February 1, 1999 shall not be considered consulting fees under this subsection, and shall be included in calculating the Base Amount in the manner specified in subsection 1.42(ii)(c) hereof."

(b) Section 1.42 of the Project and Supply Agreement is further amended to add the following new paragraph (c) to the end of such Section:

"(c) In addition, the Base Amount (as it may be adjusted pursuant to this Section 1.42) shall also be increased by an amount equal to fifty percent (50%) of any capital costs incurred by EDNC in excess of the amounts contemplated by Subparagraph (A) of Schedule 1.42(A) in connection with the completion and commissioning of the EDNC Baytown Plant, not to exceed Three Million U.S. Dollars (U.S. $3,000,000) in the aggregate. The adjustment to the Base Amount contemplated by the preceding sentence shall be subject to and contingent upon the following conditions: (a) Bayer shall have the continuing right to a full and complete audit of the costs associated with the completion and commissioning of the EDNC Baytown Plant, as contemplated by Section 34 hereof; (b) the foregoing adjustment to the Base Amount shall only apply to items actually incurred by EDNC that may be capitalized and which would not have been incurred but for the failure in performance by the Contractor under the Turnkey Engineering, Procurement and Construction Agreement dated August 26, 1997 between EDNC and the Contractor ("Turnkey Contract"); (c) the adjustment to the Base Amount shall only be made if, from and after the date EDNC shall have rendered the EDNC Baytown Plant Fully Operational; (d) all sources of recourse, including without limitation any rights that EDNC might have against the Contractor (including any right to liquidated or delay damages), any issuer of any payment or performance bond supporting the construction and completion of the EDNC Baytown Plant, and any insurance carrier or the Contractor or subcontractors or materialmen against which EDNC might now or hereafter have a valid claim, shall be pursued diligently by EDNC; (e) any recoveries by EDNC from the Contractor and third parties pursuant to rights under the Turnkey Agreement under the preceding clause (d) other than recoveries under any payment or performance bonds ("Third Party Recoveries"), shall be applied as set forth in Exhibit C to reduce the Base Amount (but not by more than Three Million U.S. Dollars (U.S. $3,000,000)), and the Base Amount shall be retroactively and prospectively adjusted to reflect such recoveries; (f) if Bayer exercises its rights under Articles 16 or 17 hereof, the appropriate termination fee shall not be adjusted to reflect any additional capital contemplated by this paragraph; (g) increased capital under this paragraph shall have no effect upon the calculation of the Profit Component under Section 1.57 hereof; and (h) project change orders requested and approved after February 1, 1999 shall be considered capitalizable items under paragraph (A) of Schedule 1.42(A), unless such project change orders are related to the failure in performance of Contractor under the Turnkey Contract. The parties agree to execute an appropriate amendment to Schedule 1.42(A) to reflect any adjustment contemplated by this paragraph.

4. Amendment to Section 2.1 - Supply. The third sentence of Section 2.1 of the Project and Supply Agreement is hereby amended and restated to read in its entirety as follows: "In the event of any planned or unplanned outage, Bayer, EDNC and El Dorado agree that the Back Up Supply Plan, attached hereto as Exhibit D, shall

become operative." Section 2.1 of the Project and Supply Agreement is further amended to add the following sentence to the end of Section 2.1 thereof:

"EDNC shall substantially complete construction of and commence operations of the EDNC Baytown Plant no later than May 31, 1999, and shall render the EDNC Baytown Plant Fully Operational no later than June 30, 1999. For purposes of this sentence, the "commencement of operations" shall be defined as the production of Nitric Acid meeting the specifications in merchantable quantities."

4A. Amendment to Section 5.3. Section 5.3 of the Project and Supply Agreement is hereby deleted and replaced with the word "[Reserved]."

5. Amendments to Section 17.1 Bayer's Optional Termination Rights and Schedule 1.42(A) Initial Capital Investment.

(a) Section 17.1(A) of the Project and Supply Agreement is hereby amended to read in its entirety as follows:

"(A) Failure by EDNC (i) to complete construction and commence the operations of the EDNC Baytown Plant prior to May 31, 1999; or (ii) to render the EDNC Baytown Plant Fully Operational prior to June 30, 1999 (provided, in each case, that such failure is not substantially related to a material breach by Bayer of its obligations under the Project Agreements); provided, however, that if such failure is by reason of a Force Majeure Event occurring after February 1, 1999, then Bayer shall not have the option to terminate this Agreement if (x) EDNC provides to Bayer, within ten (10) days of the occurrence of such Force Majeure Event, a plan reasonably acceptable to Bayer to remedy such Force Majeure Event as soon as practicable but no later than June 30, 1999, (y) EDNC remedies such Force Majeure Event as soon as practicable but no later than June 30, 1999 pursuant to such plan, and (z) neither the Owner Participant nor the Indenture Trustee serves a Triggering Notice on Bayer during the pendency of such Force Majeure Event pursuant to Section 1 of the Agreement dated June 27, 1997 among Bayer, Security Pacific Leasing Corporation as Owner Participant, Bayerische Landesbank, New York Branch, EDNC, El Dorado, Wilmington Trust Company, as Indenture Trustee, and Boatmen's Trust Company of Texas, as Owner Trustee (the "Three Option Agreement")."

(b) The date "February 1, 1999" set forth in Section 17.1(D) of the Project and Supply Agreement is hereby deleted and replaced with "June 30,1999."

(c) The period at the end of subsection (D) of Section 17.1 of the Project and Supply Agreement is hereby deleted and replaced with "; or".

(d) The following subsection (E) hereby is added to Section 17.1 of the Project and Supply Agreement:

"(E) in the event that (1) material adverse developments or changes occurring after the date hereof (including without limitation any material adverse

development or change in conditions now existing, whether or not foreseeable) in connection with the construction, testing or operation of the EDNC Baytown Plant or the financing of the project give Bayer reasonable grounds to believe that EDNC will not (a) fulfill its covenants contained herein and meet the dates specified in Sections 17.1(A) or 17.1(D) and (b) EDNC fails to provide assurances satisfactory to Bayer (in the exercise of its reasonable discretion) of such performance within ten (10) days of written demand therefor by Bayer, or (2) EDNC acknowledges in writing to any party its inability to meet the dates specified in Section 17.1(A) or 17.1(D) hereof."

6. Amendments to Schedule 1.42. Item (E) of Schedule 1.42(A) is hereby amended to reflect that Construction Interest Charges shall be those charges actually incurred, not to exceed $4,440,000. In addition, the note at the conclusion of this Schedule shall be revised to read as follows:

"Items B, D, F and G are estimates and are subject to adjustment to the actual incurred costs on or prior to the Commencement Date. Item (E) is a not-to-exceed estimate and shall be adjusted to actual incurred costs (not to exceed the specified amount) on or prior to the Commencement Date."

7. Payment to Bayer.

(a) EDNC acknowledges and agrees that Bayer will incur substantial monetary costs as a direct result of the delays addressed by this Agreement, and that such costs are in amounts difficult to ascertain. As a consequence, and in consideration of the foregoing amendments reflected herein, EDNC hereby agrees to indemnify and hold harmless Bayer from and against its actual net losses incurred between February 1, 1999 and the date the EDNC Baytown Plant is able to produce Bayer's requirements of Nitric Acid (the "Requirements Date") under the Cost Categories described on Exhibit A hereto. Such indemnification shall not amend, modify or be in lieu of Bayer's rights specified in the Project and Supply Agreement. The calculation of the hypothetical cost to produce Nitric Acid at the EDNC Baytown Plant during the subject period shall be calculated in conformity with Exhibit B hereto, using actual volumes taken by Bayer during this period to measure the differential between the cost of Nitric Acid, had it been produced at the EDNC Baytown Plant, and the cost of nitric acid purchased from EDNC under the Start Up Supply Plan or the Interim Supply Agreement (as the case may be) between EDNC and Bayer. EDNC shall reimburse Bayer for such actual net costs incurred as calculated in the manner specified in the following subsections 7(b) and 7(c).

(b) Bayer's actual net costs shall be calculated by the parties hereto and reimbursed by EDNC in the manner specified in subsections Section 7(b) and (c). On or prior to the date which is fifteen (15) days following the Requirements Date, Bayer shall deliver to EDNC its written calculation of the actual net cost Impact of Delayed Start Up of the EDNC Baytown Plant, calculating costs in the Cost Categories set forth on Exhibit A hereto (the "Impact Statement"). The Impact Statement (x) shall reflect the actual costs and other expenses incurred by Bayer during the period from February 1, 1999 through and including the Requirements Date (the "Delay Period") as a consequence of the delay in EDNC's substantial completion and commencement of operations of the EDNC Baytown Plant; (y) shall be prepared using the same methodology employed in preparing Exhibit B hereto and shall be delivered without prejudice to the right of Bayer to recoup costs and expenses thereafter ascertained or determined; and (z) shall be prepared using actual volumes, actual prices, incurred freight, handling and unloading expenses, idle equipment fees and other verifiable charges wherever possible. EDNC shall have fifteen (15) days to object in writing to any line item contained in the Impact Statement, and barring any objection such Impact Statement shall become final and binding upon all parties. Any objection by EDNC shall be stated with specificity, shall set forth any differences from EDNC's calculations, and shall be resolved in the manner specified in Section 22 of the Project and Supply Agreement. EDNC agrees to pay (in the manner specified by subsection 7(c) hereof) any amount reflected on the Impact Statement as to which no objection is lodged.

(c) EDNC shall render payment of the amounts determined under this Section 7 as follows: (i) twenty percent (20%) of the amount determined under Section 7(a) hereof (or, in the event of a dispute under the preceding subsection, twenty percent (20%) of any amount not in controversy) shall be paid to Bayer by EDNC without offset or counterclaim of any kind whatsoever in immediately available funds on or before the twenty-fifth (25th) day following the delivery of the Impact Statement; and (ii) the balance of the relevant amount (or, in the event of a dispute under the preceding subsection, the balance of the amount not in controversy) shall be paid by EDNC and El Dorado to Bayer in the form of a credit (the "Credit"), which Credit shall bear interest at the rate of 7.11% per annum on the outstanding principal balance thereof until reduced to zero (0) as hereinafter provided. The principal balance of, and accrued interest on, the Credit shall be reduced exclusively by application in the form of credits to Nitric Acid purchases by Bayer through the period that is (y) twenty-four (24) months following the Requirements Date, if the initial principal balance of the Credit is less than or equal to Three Million U.S. Dollars (U.S. $3,000,000), and (z) thirty-six (36) months following the Requirements Date, if the initial principal balance of the Credit exceeds Three Million U.S. Dollars (U.S. $3,000,000), whereupon any remaining principal and interest not reduced by credit to Nitric Acid purchases shall be due and payable in full in immediately available funds. In the event any line item of the Impact Statement is disputed by EDNC under subsection 7(b), the disputed amount shall, immediately following resolution under Section 22 of the Project and Supply Agreement, be reflected in a supplemental cash payment and supplemental Credit determined as provided above.

(d) The Credit (and any supplemental Credit), as it may be hereafter adjusted under subsection (e) hereof, shall be taken against Nitric Acid purchases on a unit basis, calculated and re-adjusted semi-annually, by dividing the remaining principal balance and accrued interest of the Credit, as it may be hereafter adjusted under subsection (e) hereof, by the actual (for past months commencing on the Requirements Date) and budgeted (for those months for which actual figures are not yet available through the termination date of the subject Credit, as established under the preceding clause (c)(y) or (z), as appropriate) consumption of nitric acid by Bayer during the period from the Requirements Date through the termination date of the subject Credit, as established under the preceding clause (c)(y) or (z), as appropriate.

(e) The Credit allowed Bayer pursuant to this Section 7 shall be reduced, retroactively and prospectively, effective on January 1, 2000, by an amount to be established by agreement of the parties in respect of those cost savings realized by Bayer during the period September 1, 1998 through January 31, 1999 as a consequence of the delayed start-up of the EDNC Baytown Plant, and shall be calculated without prejudice to the right of EDNC to recoup credits which would reduce actual costs and other expenses incurred by Bayer. The amount of this adjustment shall be

calculated utilizing the Cost Categories identified on Exhibit A hereto and the same methodology utilized by the parties in calculating the Credit and preparing the Impact Statement.

(f) In the event Bayer elects to terminate the Project and Supply Agreement and the related documents, the obligation of the parties to pay the amounts or allow any credits otherwise payable or allowable under this Section 7 shall be extinguished; provided, however that any such extinguishment shall not affect the right of Bayer to seek indemnifiable damages or other amounts to which it is otherwise entitled under the Project and Supply Agreement. The method of calculation of costs set forth in this Section 7 and the fact that EDNC has agreed in this Agreement to pay any such amounts hereunder shall not be deemed an admission by either party as to the level of damages, if any, incurred by Bayer in connection with the delayed start-up of the EDNC Baytown Plant.

8. Waiver of Cure Periods. As a consequence of and as additional consideration for the extensions and forbearances hereby granted by Bayer, EDNC hereby waives the cure period applicable to any default by EDNC in its obligations to render Fully Operational the EDNC Baytown Plant.

9. Representations and Warranties. Bayer hereby represents and warrants to EDNC, and EDNC represents to Bayer as follows:

(a) this Agreement (and the Interim Supply Agreement) have been duly and validly authorized, executed and delivered by such party (including, in the case of EDNC, authorized by unanimous approval of all of its directors) and constitute legal, valid and binding obligations of such party enforceable against it in accordance with their respective terms; and

(b) the execution, delivery and performance of this Agreement (and the Interim Supply Agreement) by such party will not:

(i) violate or conflict with its charter or bylaws;

(ii) breach or result in a default (or an event which, with the giving of notice or the passage of time, or both, would constitute a default) under, require any consent under, result in the imposition of any lien under or give to others any rights of termination, acceleration, suspension, revocation, cancellation or amendment of any agreement to which it is a party;

(iii) breach or otherwise violate any order, writ, judgment, injunction or decree issued by any governmental person or entity which names such party or is directed to such party or any of its respective properties or assets;

(iv) violate any Laws; or

(v) require any consent, authorization, approval, exemption or other action by, or any filing, registration or qualification with, any governmental person or entity other than those which have been made or obtained prior to the date hereof.

10. Effect of Breach by EDNC. The extensions and forbearances granted herein represent a conditional waiver by Bayer of its rights under the Project and Supply Agreement; in the event of any breach or failure of compliance EDNC with the terms and conditions of this Agreement, the extension and waiver granted by Bayer in this Agreement shall be null and void and Bayer shall be free to pursue its rights and remedies under the Project and Supply Agreement as if the extension and waiver granted herein had not been granted.

11. Other Provisions. The parties acknowledge that the payment by EDNC of the amounts described in Section 7 is in consideration of the agreement by Bayer to forbear from the exercise of its termination rights under Section 17.1 of the Project and Supply Agreement for the limited period of time described herein. Neither Bayer nor EDNC, by virtue of this Amendment, agrees to waive, relinquish, amend, restate or release any of its remaining rights under the Project and Supply Agreement, and Bayer does not, by this Amendment, agree to further extensions beyond the date specified in Section 5 hereof. Subject to the amendments set forth herein, all other provisions of the Project and Supply Agreement shall remain in full force and effect as they are currently set forth in the Project and Supply Agreement. All references to the Project and Supply Agreement in any document, instrument or agreement described in, referred to, annexed to, contemplated by or incorporated by reference in the Project and Supply Agreement or this Agreement shall be deemed to mean the Project and Supply Agreement as amended hereby. Without limiting the foregoing, upon execution of this Agreement, each reference in the Project and Supply Agreement to "this Agreement," "hereunder," "hereof," "herein," or words of like import, and each reference in any document related thereto or executed in connection therewith, shall mean and be a reference to the Project and Supply Agreement as amended hereby, and the Project and Supply Agreement and this Agreement shall be read together and construed as one single instrument. Any dispute regarding the terms or provisions of this Amendment shall be resolved in the manner specified in Section 22 of the Project and Supply Agreement.

12. Counterparts; Telefacsimile Execution. This Agreement may be executed in any number of counterparts, and by each of the parties on separate counterparts, each of which, when so executed, shall be deemed an original, but all of which shall constitute but one and the same instrument. Delivery of an executed counterpart of this Agreement by telefacsimile shall be equally as effective as delivery of a manually executed counterpart of this Agreement. Any party delivering an executed counterpart of this Agreement by telefacsimile also shall deliver a manually executed counterpart of this Agreement, but the failure to deliver a manually executed counterpart shall not affect the validity, enforceability or binding effect of this Agreement.

13. Effect on Ground Lease. Bayer agrees not to exercise its right of termination under the Ground Lease for so long as the waivers and forbearances reflected herein hereof remain in force and effect.

[signature page follows]

IN WITNESS WHEREOF, the parties hereto have executed this First Amendment to Baytown Nitric Acid Project and Supply Agreement as of the date first above written.

BAYER CORPORATION

By: ________________________________

Name: ________________________________

Title: ________________________________

EL DORADO NITROGEN COMPANY

By: ________________________________

Name: ________________________________

Title: ________________________________

El Dorado Chemical Company hereby consents and agrees to the amendment represented hereby and executes this First Amendment to Baytown Nitric Acid and Supply Agreement solely for purposes of confirming its continuing guaranty as set forth in Section 35 of the Project and Supply Agreement.

EL DORADO CHEMICAL COMPANY

By: ________________________________

Name: ________________________________

Title: ________________________________

EXHIBIT A

Cost Categories

Start Up Expenses

Handling & Unloading Expenses

Idle Ammonia Pipeline Expenses

Purchased Acid Costs under Start-Up Supply Plan

Idle Equipment fees, Etc., Associated with Purchased Acid Costs under Start Up Supply Plan

Purchased Acid Costs if Acid had been produced on site

Loss of Dilution benefit to Bayer on EDNC 3rd Party Sales

Bayer Security Services

Bayer Management SG&A Expense

Bayer Legal Fees

Net Steam Exported (after 2/1/99)

Miscellaneous other costs (subject to review and agreement by the parties)

EXHIBIT B

Calculation of Nitric Acid Costs if Produced on Site

Exhibit B

Estimated Nitric Acid Costs
Assuming acid produced at Baytown

	Sep	Oct	Nov	Dec	Jan
Volume ST					
			***		
Fixed Costs					
Variable Cost					
Ammonia					
Terminal Fee					
Pipeline Fee					
Net Capital Amt.					
Profit Component					
Lost Steam Credit					
Ammonia Inefficiency					
Miscellaneous					
Total Cost/ST					
Total Cost $					
Ammonia Price/ST					

***THE REMAINDER OF THIS EXHIBIT HAS BEEN OMITTED FROM THIS PUBLIC FILING PURSUANT TO A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

Exhibit B
Continued

Estimated Nitric Acid Costs
Assuming acid produced at Baytown

	Feb	Mar	Apr	May	Jun
Volume ST					
			***		
Fixed Costs					
Variable Cost					
Ammonia					
Terminal Fee					
Pipeline Fee					
Net Capital Amt.					
Profit Component					
Lost Steam Credit					
Ammonia Inefficiency					
Miscellaneous					
Total Cost/ST					
Total Cost $					
Ammonia Price/ST					

***THE REMAINDER OF THIS EXHIBIT HAS BEEN OMITTED FROM THIS PUBLIC FILING PURSUANT TO A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

EXHIBIT C

Third Party Recoveries by EDNC under subsection (d) of Section 1.42(c) shall be applied to reduce the Base Amount as follows:

***

***THE REMAINDER OF THIS EXHIBIT HAS BEEN OMITTED FROM THIS PUBLIC FILING PURSUANT TO A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

FIFTH AMENDMENT
TO
LEASE AGREEMENT
3200 W. Reno
Oklahoma City, Oklahoma

This Fifth Amendment to Lease Agreement, dated as of the ____ day of October, 1998, by and between MAC VENTURE, LTD., an Oklahoma limited partnership ("Owner"), and HERCULES ENERGY MFG. CORPORATION, an Oklahoma corporation ("Tenant").

WITNESSETH

WHEREAS, Owner has leased to Tenant certain real property known as 3200 W. Reno, Oklahoma City, Oklahoma, along with certain appurtenances and improvements located thereon (the "Leased Premises"), pursuant to the terms and conditions of a Lease Agreement, dated March 26, 1982, as amended by an Amendment to Lease Agreement dated August 31, 1983, and by a Second Amendment to Lease Agreement dated June 6, 1985, and by a Third Amendment to Lease Agreement dated December 31, 1987, and by a Fourth Amendment to Lease Agreement dated December 14, 1993, between Owner and Tenant (said Agreements are hereinafter collectively referred to as "Lease Agreement"); and

WHEREAS, the parties desire to reduce the size of the Leased Premises to 30,000 square feet of warehouse and shop space which will be leased at a monthly rental amount of $3,750.00; and

WHEREAS, the parties desire to extend the term of the Lease Agreement with said extension commencing January 1, 1999 and expiring December 31, 1999.

NOW, THEREFORE, in consideration of the mutual covenants and agreements contained herein, the receipt and sufficiency of which is hereby acknowledged, the Owner and Tenant do hereby amend the Lease Agreement as follows:

1. Effective as of January 1, 1999, the Leased Premises are reduced in size to 30,000 square feet of warehouse and shop space which will be leased at a monthly rental amount of $3,750.00 per month.

2. Effective as of December 31, 1998, the term of the Lease Agreement is extended for a period commencing January 1, 1999 and expiring December 31, 1999, on the same terms and conditions as set forth in the Lease Agreement, except for those changes set forth in paragraph 1 above.

3. Except as expressly amended herein, the Lease Agreement shall remain in full force and effect and is hereby confirmed and ratified by the Owner and Tenant.

IN WITNESS WHEREOF, this Fifth Amendment to Lease Agreement is dated as of the ____ day of October, 1998.

MAC VENTURE, LTD., an Oklahoma limited partnership, by First Industries Capital Corporation, General Partner

____
President

HERCULES ENERGY MFG. CORPORATION

____
President

Solutia (SELLER)

10300 Olive Boulevard
P.O. Box 66760
St. Louis, Missouri 63166-6760
(314) 674-1000

SALES CONTRACT

SOLD TO El Dorado Chemical (BUYER)
P.O. Box 1373
Oklahoma City, OK 73101

THE FOLLOWING GOODS, SUBJECT TO TERMS AND CONDITIONS AS STATED BELOW AND ON THE REVERSE SIDE HEREOF.

PERIOD	January 1, 1999 through December 31, 2000 and continuing calendar year to calendar year thereafter unless canceled, in writing, by either party prior to the preceding October 1st.
GOODS	Anhydrous Ammonia
QUANTITY	minimum of 5,000 tons per month additional quantities available provided such quantities are mutually agreed to by both parties.
PRICE	*** *** *** *** *** ***
PAYMENT TERMS	Net 15 days from date of invoice, with end of month billing
F.O.B.	Seller's *** plant
ADDITIONAL TERMS AND CONDITIONS	A pipeline freight allowance (PA) of $*** is included to match the current competitive freight position for delivery into El Dorado Chemical's plant. The pipeline freight allowance will reduced by the amount that the freight can be reduced below $***.

This contract shall not be binding on Seller unless executed by Buyer and an authorized representative of Seller and delivered to Seller within thirty days from the date below.

EXECUTED BY Dated ______________________

EL DORADO CHEMICAL COMPANY, BUYER SOLUTIA, INC., SELLER

____

By ______________________________ By ______________________________

Title ______________________________ Title ______________________________

***INDICATES INFORMATION IN THIS DOCUMENT WHICH HAS BEEN OMITTED FROM THIS PUBLIC FILING PURSUANT TO A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

1. EXCUSE OF PERFORMANCE. (a) Deliveries may be suspended by either party in the event of: Act of God, war, riot, fire, explosion, accident, flood, sabotage; lack of adequate fuel, power, raw materials, labor, containers or transportation facilities; compliance with governmental requests, laws, regulations, orders or actions; breakage or failure of machinery or apparatus; national defense requirements or any other event, whether or not of the class or kind enumerated herein, beyond the reasonable control of such party; or in the event of labor trouble, strike, lockout or injunction (provided that neither party shall be required to settle a labor dispute against its own best judgment); which event makes impracticable the manufacture, transportation, acceptance or use of a shipment of the goods or of a material upon which the manufacture of the goods is dependent.

(b) If Seller determines that its ability to supply the total demand for the goods, or obtain any or a sufficient quantity of any material used directly or indirectly in the manufacture of the goods, is hindered, limited or made impracticable, Seller may allocate its available supply of the goods or such material (without obligation to acquire other supplies of any such goods or material) among itself and its purchasers on such basis as Seller determines to be equitable without liability for any failure of performance which may result therefrom.

(c) Deliveries suspended or not made by reason of this section shall be canceled without liability, but this contract shall otherwise remain unaffected.

2. BUYER'S CREDIT. Seller reserves the right, among other remedies, either to terminate this contract or to suspend further deliveries under it in the event Buyer fails to pay for any one shipment when same becomes due. Should Buyer's financial responsibility become unsatisfactory to Seller, cash payments or security satisfactory to Seller may be required by Seller for future deliveries and for the goods theretofore delivered.

3. WEIGHTS AND CONTAINERS. In the case of bulk carload, tank car, tank truck or barge shipments, Seller's weights shall govern unless proved to be in error. Where returnable containers are used in shipment, title to such containers shall remain in Seller, and a deposit in the amount required by Seller must be made at the time payment is tendered for the goods. Such containers must be kept in good condition, must not be used for any material other than the good shipped therein and must be returned within sixty (60) days from date of shipment. On such containers being so returned in good condition, a refund of the deposit will be made.

4. SHIPMENTS. The quantity shipped in any contract month may be limited by Seller to either (a) the average of the monthly quantities purchased by Buyer for the preceding contract months or (b) the maximum quantity covered by this contract divided by the number of months in the period of this contract (provided, however, that if different quantities apply to different time periods within the period of this contract, Seller may limit shipments based upon the current maximum quantity for the applicable time period under this contract divided by the number of months in such time period). Any quantity not shipped as a result of any such limitation shall be deducted from the total quantity of this contract. Seller shall not be bound to tender delivery of any quantities for which Buyer has not given shipping instructions.

5. LIMITED WARRANTY. Subject to Section 6 and unless otherwise expressly provided herein, Seller warrants title and that the goods shall conform to Seller's standard specifications or to the attached specifications, if any. Subject to the preceding sentence and except as otherwise expressly provided herein, SELLER MAKES NO REPRESENTATION OR WARRANTY OF ANY KIND, EXPRESS OR IMPLIED, AS TO MERCHANTABILITY, FITNESS FOR PARTICULAR PURPOSE, OR ANY OTHER MATTER WITH RESPECT TO THE GOODS, whether used alone or in combination with any other material.

6. LIMITATION OF LIABILITY. (a) Within thirty (30) days after receipt of each shipment of the goods, Buyer shall examine such goods for any damage, defect or shortage. All claims for any cause whatsoever (whether such cause be based on contract, negligence, strict liability, other tort or otherwise) shall be deemed waived unless made in writing and received by Seller within sixty (60) days after Buyer's receipt of the goods, in respect to

which such claim is made, or, if such claim is for non-delivery of such goods, within sixty (60) days after the date upon which such goods were to be delivered, provided that as to any such cause not reasonably discoverable within such sixty (60) day period (including that discoverable only in processing, further manufacture, other use or resale) any claim shall be made in writing and received by Seller within one hundred eighty (180) days after Buyer's receipt of the goods, in respect to which such claim is made, or within thirty (30) days after Buyer learns of the facts giving rise to such claim, whichever shall first occur. Failure of Seller to receive written notice of any such claim within the applicable time period shall be deemed an absolute and unconditional waiver by Buyer of such claim irrespective of whether the facts giving rise to such claim shall have then been discovered or of whether processing, further manufacture, other use or resale of the goods shall have then taken place.

(b) BUYER'S EXCLUSIVE REMEDY SHALL BE FOR DAMAGES, AND SELLER'S TOTAL LIABILITY FOR ANY AND ALL LOSSES AND DAMAGES ARISING OUT OF ANY CAUSE WHATSOEVER (WHETHER SUCH CAUSE BE BASED IN CONTRACT, NEGLIGENCE, STRICT LIABILITY, OTHER TORT OR OTHERWISE) SHALL IN NO EVENT EXCEED THE PURCHASE PRICE OF THE GOODS IN RESPECT TO WHICH SUCH CAUSE ARISES OR, AT SELLER'S OPTION, THE REPAIR OR REPLACEMENT OF SUCH GOODS, AND IN NO EVENT SHALL SELLER BE LIABLE FOR INCIDENTAL, CONSEQUENTIAL OR PUNITIVE DAMAGES RESULTING FROM ANY SUCH CAUSE. Seller shall not be liable for, and Buyer assumes liability for, all personal injury and property damage connected with the handling, transportation, possession, processing, further manufacture, other use or resale of the goods, whether the goods are used alone or in combination with any other material. Transportation charges for the return of the goods shall not be paid unless authorized in advance by Seller.

(c) If Seller furnishes technical or other advice to Buyer, whether or not at Buyer's request, with respect to processing, further manufacture, other use or resale of the goods, Seller shall not be liable for, and Buyer assumes all risk of, such advice and the results thereof.

7. PATENTS. Subject to Section 6 and unless otherwise expressly provided herein, Seller warrants that the goods sold pursuant to this contract, except for those made for Buyer according to Buyer's specifications, do not infringe any valid U.S. patent. This warranty is given upon condition that Buyer promptly notify Seller of any claim or suit involving Buyer in which such infringement is alleged and that, if Seller is affected, Buyer permit Seller to control completely the defense or compromise of any such allegation of infringement. Seller does not warrant that the use of the goods or any material made therefrom, whether the goods are used alone or in combination with any other material, will not infringe a patent. Seller reserves the right to terminate Seller's warranty under this Section 7 at any time with respect to any undelivered goods, it being agreed that in the event of such termination Buyer may, without penalty, thereafter refuse acceptance of such undelivered goods.

8. FREIGHT AND TAXES. Any increase in freight rates paid by Seller on shipments covered by this contract and hereafter becoming effective and any tax or governmental charge or increase in same (excluding any franchise or income tax or other tax or charge based on income) (a) increasing the cost to Seller of producing, selling or delivering the goods or of procuring materials used therein or (b) payable by Seller because of the production, sale or delivery of the goods, such as Sales Tax, Use Tax, Retailer's Occupational Tax, Gross Receipts Tax, Value Added Tax, may, at Seller's option, be added to the price herein specified.

9. PRICE REVISION.

10. Price Protection.

11. COMPLIANCE WITH CERTAIN LAWS. Subject to Section 6 and unless otherwise expressly provided herein, the goods shall be produced in compliance with the requirements of the Fair Labor Standards Act of 1938, as amended, and Executive Order 11246.

12. ASSIGNMENT. Buyer shall not (by operation of law or otherwise) assign its rights or delegate its performance hereunder without the prior written consent of Seller, and any attempted assignment or delegation without such consent shall be void.

13. MISCELLANEOUS. THE VALIDITY, INTERPRETATION AND PERFORMANCE OF THIS CONTRACT AND ANY DISPUTE CONNECTED HEREWITH SHALL BE GOVERNED AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF MISSOURI. This contract constitutes the full understanding of the parties, a complete allocation of risks between them and a complete and exclusive statement of the terms and condition of their agreement. Except as provided in Sections 9 and 10 hereof, no conditions, usage of trade, course of dealing or performance, understanding or agreement purporting to modify, vary, explain or supplement the terms or conditions of this contract shall be binding unless hereafter made in writing and signed by the party to be bound, and no modification shall be effected by the acknowledgment or acceptance of purchase order or shipping instruction forms containing terms or conditions at variance with or in addition to those set forth herein. No waiver by either Seller or Buyer with respect to any breach or default or of any right or remedy and no course of dealing, shall be deemed to constitute a continuing waiver of any other breach or default or of any other right or remedy, unless such waiver be expressed in writing signed by the party to be bound.

AGREEMENT FOR PURCHASE AND SALE
OF ANHYDROUS AMMONIA*

THIS AGREEMENT ("Agreement") is made this 1st day of January, 1999, by and between Farmland Industries, Inc. (hereinafter "Seller"), a Kansas Corporation, with its principal place of business in Kansas City, Missouri, and El Dorado Chemical Company (hereinafter "Buyer"), an Oklahoma corporation, with its principal place of business in El Dorado, Arkansas.

WITNESSETH

WHEREAS, Seller represents that it has the right to sell certain quantities of anhydrous ammonia as hereinafter defined ("Product"); and

WHEREAS, Seller desires to sell and Buyer wishes to purchase the quantities of Product herein stipulated upon the conditions, covenants, and agreements contained herein;

NOW, THEREFORE, in consideration of the mutual covenants, promises and agreements contained herein, Seller and Buyer agree as follows:

1. Quantity: Seller shall deliver to Buyer at El Dorado, Arkansas a volume of Product of not less than twenty four thousand (24,000) tons and not more than seventy two thousand (72,000) tons, during the contract term, commencing January 1, 1999.

2. Minimum/Maximum Monthly and Quarterly Quantities: Seller shall not be required to deliver more than six thousand (6,000) tons and not less than two thousand (2,000) ton of Product in any one month. Seller shall not be required to deliver more than eighteen thousand (18,000) tons and not less than six thousand (6,000) tons of Product in any one quarter.

3. Forecast of Buyer's Purchases: During the term of this Agreement, Buyer shall provide a written forecast quarterly by month for purchases for each quarter of the contract year. Buyer shall make this quarterly forecast and deliver it to Seller on or before the 15th day of the month preceding the quarter.

4. Term: This Agreement shall commence at 12:01 a.m., Central Standard Time, January 1, 1999, and shall continue until 11:59 p.m. Central Standard Time, June 30, 2000, unless terminated earlier in accordance with the provisions hereof.

5. Price:

(a) The parties to this Agreement have intentionally left the purchase price to be paid by Buyer open for periodic determination, pursuant to the contract pricing formula contained herein. It is the intention of the parties that there be a binding agreement from the date of the signing of this Agreement, even if the price is not determined at the time since a contract pricing formula is contained herein.

(b) "Base Price" hereunder shall be calculated as follows, for each calendar month during the term of this Agreement:

*INFORMATION IN THIS DOCUMENT HAS BEEN OMITTED FROM THIS PUBLIC FILING PURSUANT TO A REQUEST BY THE COMPANY FOR CONFIDENTIAL TREATMENT BY THE SECURITIES AND EXCHANGE COMMISSION. THE OMITTED INFORMATION HAS BEEN FILED SEPARATELY WITH THE SECRETARY OF THE SECURITIES AND EXCHANGE COMMISSION FOR PURPOSES OF SUCH REQUEST.

(1) On or before the first day of each calendar month during the term of this Agreement, Seller shall calculate on a million British Thermal Unit basis (hereinafter MMBTU), *** cost of natural gas, for such calendar month; plus a nominal fee of *** per MMBTU for procurement and expense incurred in gas negotiation and purchase. Such cost shall exclude gains or losses pursuant to Paragraph 5(h) herein;

(2) The natural gas price per MMBTU, as calculated in 5(b)(1) above, shall be multiplied by ***;

(3) To the results of 5(b)(2) shall be added an amount of ***;

(4) The results in 5(b)(3) shall be multiplied by ***.

The total amount in 5(b)(4) shall be defined as the "Base Price".

(c) The "*** Ammonia Price" shall be defined as the ***.

(d) If at any time during the term of this Agreement the "*** Ammonia Price" exceeds the "Base Price", the sale/purchase price per ton of Product hereunder shall be calculated as follows:

(1) The "Base Price" shall be noted;

(2) The "*** Ammonia Price" shall be noted;

(3) ***;

(4) ***;

(5) The f.o.b. sale/purchase price at any time during the term of this Agreement when the "*** Ammonia Price" exceeds the "Base Price" shall be an amount equal to ***.

(e) If at any time during the term of this Agreement the "*** Ammonia Price" is below the "Base Price", the sale/purchase price per ton of Product hereunder, shall be the "*** Ammonia Price".

(f) Volume discounts may be earned quarterly for Product priced monthly by either 5(d) or 5(e). Credit will be issued on total volume per quarter and calculated as follows:

***

(g) All Product for shipments to Buyer's El Dorado, Arkansas location shall be delivered to Buyer via Koch Pipeline unless such pipeline becomes unavailable due to mechanical failure of the pipeline. In the event the Koch Pipeline is unavailable for that reason, Product shall be shipped by rail cars and each party hereto shall use its best efforts to minimize the cost of shipment by rail car. In the event Product is shipped by rail car, the purchase price for Product shall be adjusted to reflect the actual cost of such transportation.

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(h) Gains or losses resulting from Seller's activities in the natural gas Futures market shall not be incorporated into the gas cost calculations irrespective of whether delivery is taken by Farmland in any Futures transaction.

6. Verification of *** Natural Gas Prices: Buyer shall have the right, at any time during the term of this Agreement, to request Seller to provide documentation to a mutually acceptable audit firm to verify that excess charges for natural gas have not been made.

7. Delivery/Freight:

(a) Pipeline - As shipper of record Seller shall invoice Buyer for all actual Koch Pipeline tariff charges plus a *** per short ton meter fee for tons transported by pipeline to Buyer's El Dorado, Arkansas facility. Seller will credit Buyer for all shrink refunds allowed Seller by the Koch Pipeline on tons transported to El Dorado during the term of the Agreement.

(b) Rail - Freight charges on rail shipments shall be invoiced to Buyer at either (i) the then current railroad tariff rate, or (ii) a negotiated contract freight rate as agreed by the parties. Seller may invoice Buyer and Buyer shall pay Seller tank car demurrage at a daily rate of *** per car per day for each day commencing with the eighth day after constructive placement of the car at Buyer's destination. Such rail shipments shall be priced at the time of the order by Seller.

8. Invoices and Payment: Seller shall deliver invoices to Buyer as soon after the end of each calendar month as is reasonably possible. Buyer shall make payments to Seller for each month's purchases, on or before the fifteenth (15th) day of the following month. Payment shall be made by wire transfer to such bank or banks as Seller shall designate. If at any time during the term of this Agreement, Buyer becomes delinquent in payment or in Seller's reasonable judgment there has occurred a material adverse change in the financial condition of Buyer which could reasonably be expected to impair Buyer's ability to carry out its financial obligations to Seller, Seller shall have the sole and exclusive right to require the Buyer to open an irrevocable letter of credit for the benefit of Farmland Industries, Inc., at a bank or banks, acceptable to Farmland Industries, Inc. for an amount not to exceed the result of multiplying *** by the contract price per ton of Product in the most recently completed calendar month.

9. Default and Nonpayment: Default in payment, or failure to perform any of the terms and conditions of this Agreement, shall constitute a default by either party to this Agreement. In the event that either party (i) defaults in making payment provided for herein when due or (ii) defaults in the performance of any other material obligation provided for herein and, if such default is susceptible of cure, fails to cure any such default of a material obligation within 30 days of receipt of written notice form the non-defaulting party thereof, the non-defaulting party shall have the right, by giving written notice to the defaulting party, to immediately terminate this Agreement.

On the occurrence of a default by either party, the non-defaulting party shall have the option to terminate this Agreement without liability of any kind as to future shipments; to alter credit terms provided to Buyer; to stop any Product in transit; to treat any default as substantially impairing the value of the whole

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Agreement, and hence a breach thereof. If Buyer does not pay any invoice on its due date, then all outstanding invoices of Seller to Buyer under this or any other agreement shall become immediately due and payable, and Seller may assess a finance charge of *** per month, or the maximum legal rate if less, on remittances not received by their due date. On the occurrence of a default by either party, the defaulting party shall be liable to the non-defaulting part for all costs, losses, and expenses incurred by such non-defaulting party by reason thereof, including reasonable attorneys' fees.

10. Product Specifications: "Product", where used in this Agreement, means Product solution of commercial grade, having ammonia (NH_3) content of not less than ***, having water content of not more than ***, and having oil content of not more than ***. Product tendered to any pipeline shall meet or exceed such pipeline's Product quality specifications for Product shipped therein. Seller shall be nominated as shipper of record on those volumes of Product sold pursuant to this Agreement and shipped via Koch Pipeline.

11. Determination of Weights: "Ton", where used in this Agreement, means two thousand pounds (2,000 lbs.) avoirdupois, as measured by Koch Pipeline meter tickets if delivery is made by pipeline, by bills of lading if delivery is made by rail or truck.

12. Manufacture and Delivery: Seller specifically reserves the right to manufacture at, or exchange to, and to deliver from, any origin, all of the Product transferred to the location scheduled and agreed to quarterly pursuant to this Agreement.

13. Disclaimer of Warranties: There are no warranties which extend beyond the description on the face hereof, and SELLER MAKES NO WARRANTY OF ANY KIND, EXPRESS OR IMPLIED, WHETHER OF MERCHANTABILITY OR FITNESS FOR ANY PURPOSE OR AGAINST INFRINGEMENT OR OTHERWISE. Buyer assumes all risk and liability for the use of the Product purchased, whether used singly or in combination with other substances and for loss, damage, or injury to persons, or property of Buyer or others arising out of the use or possession of the Product; Buyer agrees to indemnify Seller from loss (including costs of defense) in connection with claims arising from use or possession of the Product.

14. Claims by Buyer or Seller: Notices by Seller or Buyer of claims as to Product delivered, or for the nondelivery thereof, shall be made within thirty (30) days after delivery, or the date fixed for delivery, as the case may be, and failure to give such notice shall constitute a waiver by Seller or Buyer of all claims in respect thereto. Buyer's sole claim for loss or damage arising from nondelivery of Product hereunder shall be the difference between the price for the Product specified in this Agreement, and the average price of such Product then charged by major suppliers of Product at the point of shipment specified in this Agreement, duly adjusted for freight charges. In no event shall any claims of any kind be greater than, nor shall Seller in any event be liable for, any amount in excess of the purchase price of the Product in respect of which claim is made. SELLER SHALL NOT BE LIABLE FOR ANY SPECIAL, INDIRECT, INCIDENTAL OR CONSEQUENTIAL DAMAGES, ARISING FROM SELLER'S PERFORMANCE OR BREACH OF THIS AGREEMENT AND/OR USE OR POSSESSION OF THE PRODUCT, OR FOR LOSS OF PROFIT FROM RESALE OF PRODUCT. No suit or legal proceeding arising upon this Agreement shall be maintainable against Seller or Buyer unless commenced or made within one (1) year after passing of title to Product, or delivery of or failure to deliver Product hereunder.

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15. Conflicting Terms: Notwithstanding any provision herein to the contrary, no term in Seller's or Buyer's purchase order, acknowledgment form or other document which conflicts with the terms hereof or increases Seller's or Buyer's obligations hereunder, shall be binding on either party unless accepted in writing by both parties hereunder.

16. Waiver: Any waiver by Seller or Buyer of any term, provision, or condition of this Agreement, or of any default hereunder in any one or more instances shall not be deemed to be a further or continuing waiver of such term, provision or condition, or of any subsequent default hereunder.

17. Force Majeure: Neither party will be liable for failure to perform or for delay in performing this Agreement where such failure or delay is occasioned by acts of any government, compliance with law or government regulations, acts of God, war, riots, insurrections, civil commotion or disturbances, fire, flood, or accident or by any other cause or circumstances whether of like or different character, beyond the control of the party affected thereby, herein referred to as "Events of Force Majeure". Failure to obtain a supply of Product by Seller from a third party supplier shall not be an Event of Force Majeure that can be exercised by Seller. The party asserting that an Event of Force Majeure has occurred shall send the other party notice thereof by cable or telex no later than three (3) days after the beginning of such claimed event setting forth a description of the Event of Force Majeure, an estimate of its effect upon the party's ability to perform its obligations under this Agreement and the duration thereof. The notice shall be supplemented by such other information or documentation as the party receiving the notice may reasonably request. As soon as possible after the cessation of any Event of Force Majeure, the party which asserted such event shall give the other party written notice of such cessation. Whenever possible, each party shall give the other party notice of any threatened or impending Event of Force Majeure. If an Event of Force Majeure affecting Seller's or Buyer's performance by the party affected (the "affected party") shall be excused during the continuation of the Event of Force Majeure and the other party shall send written notice to the affected party whether the notifying party elects to (a) reduce the quantity of Product specified in this Agreement by the amount which cannot be delivered or received and/or (b) reschedule deliveries on a commercially reasonable basis for delivery during the remainder of the applicable Contract Year.

"In the Event of Force Majeure affecting Seller, Seller shall allocate its available Product to Buyer in the same proportion as the quantity delivered to Buyer's El Dorado, Arkansas facility hereunder during the twelve (12) months preceding the Event of Force Majeure is to the total quantity of all Product sold or used by Seller during such twelve (12) month period". (Provided, however, the total Product Buyer received shall not exceed the quantities in Article 2.) In the event Seller has not given written notice of cessation of force majeure, and such Event of Force Majeure prevents deliveries of Product for more than thirty (30) consecutive days, Buyer shall have the right to terminate this Agreement.

18. Acquisition of Plant: In the event that El Dorado Chemical Company or affiliated company having a common parent acquires more than fifty percent (50%) interest in and to a plant or company that produces or has the capacity to produce Product, Buyer may upon twelve (12) months' written notice to Seller, terminate this Contract and thereafter have no further responsibility to accept or pay for any quantity of Product hereunder.

19. Commission/Broker Fees: Seller and Buyer represent that they are dealing with each other, that neither is the agent of the other, and that no broker or agent has been involved, either directly or indirectly, in consummating this Agreement and the sale of Product hereunder. SELLER AGREES TO INDEMNIFY, PROTECT AND SAVE BUYER HARMLESS from the claims of any person or entity for

commissions or finder's fees or similar fees in connection with the transaction set forth herein where the claimant alleges that his or its contact with this transaction is traceable to Seller. BUYER AGREES TO INDEMNIFY, PROTECT, AND SAVE SELLER HARMLESS from the claims of any person or entity for commissions or finder's fees or similar fees in connection with the transaction set forth herein where the claimant alleges that his or its contact with this transaction is traceable to Buyer.

20. Taxes: Any and all taxes of any type whatsoever levied, prior to passage of title, against Product transferred pursuant to this Agreement shall be paid by Seller promptly as required by law. Any and all taxes of any type whatsoever levied against the Product at or upon, or subsequent to, passage of title shall be paid by Buyer promptly as required by law. Title to and risk of loss of the Product shall pass to the Buyer as the Product progressively passes into tank cars, and/or pipeline. Notwithstanding any provision to the contrary in this Agreement, with regard to sales/purchases of Product pursuant to this Agreement, Buyer shall pay any and all taxes or charges that are due and owing under the federal Superfund (Comprehensive Environmental Response, Compensation and Liability Act of 1986) statutes, or regulations promulgated thereunder, as amended. Notwithstanding any provision to the contrary in this Agreement with regard to sales/purchases of Product pursuant to this Agreement, Buyer shall pay any and all taxes and charges that may become in the future due and owing because of the future enactment of any state law or regulation establishing a state tax or fee of any kind whatsoever on the manufacturing and/or sale of Product or any constituent part thereof. All taxes hereunder are in addition to those prices described herein.

21. Notices: No notice, actual or constructive, shall be effective against any party unless it is (a) in writing; (b) signed by the party giving the notice; and (c) sent by registered mail, postage prepaid, or personally served on the party intended to receive said notice.

The address to be used on a mailed notice for each party shall be as follows:

To Seller: Farmland Industries, Inc.
3315 N. Oak Trafficway
P. O. Box 7305, Dept. 314
Kansas City, Missouri 64116
Facsimile: 816-459-5913

To Buyer: El Dorado Chemical Company
P. O. Box 231
El Dorado, Arkansas 71731
Facsimile: 501-863-1426
Attn.: Warren Jones

El Dorado Chemical Co.
16 S. Pennsylvania
Oklahoma City, OK 73007
Facsimile: 405-235-5067
Attn.: James Wewers
David Shear

22. Alternate Dispute Resolution: In the event of any controversy arising out of or relating to this Contract, or any breach thereof, the parties agree to submit the dispute for

resolution to a senior executive of both parties. Such executives shall meet within thirty (30) days of written request of either party.

In the event the parties are unable to resolve the controversy through such meeting, the dispute shall be submitted to binding arbitration in accordance with the rules of the Missouri Arbitration Act. V.A.M.S. 435 et. Seq. (or Uniform Arbitration Act). Such arbitration shall be initiated by either party by notifying the other party in writing and requesting a panel of five (5) arbitrators from the American Arbitration Association. Alternate strikes shall be made to the panel commencing with the party requesting the arbitration until one name remains. Such individual shall be the arbitrator for the controversy. The party requesting the arbitration shall notify the arbitrator who shall hold a hearing(s) within sixty (60) days of the notice. The arbitrator shall render a decision within twenty (20) days after the conclusion of the hearing(s). Judgment upon the award rendered by the Arbitrator may be entered in any court having jurisdiction thereof.

23. Confidentiality: The parties agree to maintain as confidential the terms of this Agreement and not to divulge such terms to any third party without the written consent of the other.

24. Miscellaneous: This Agreement expresses the whole agreement of the parties. There are no promises, condition, or obligations, other than those enumerated herein. This Agreement shall supersede all previous or contemporaneous communications, representations, or agreement, verbal or written, between or among the parties. No usage of trade or prior course of dealing or performance between Buyer and Seller shall be deemed to modify the terms of this Agreement. This Agreement shall not be modified except in writing signed by the party to be charged. Headings are for reference only, and do not affect the meaning of any paragraph.

This Agreement shall not be assigned by either party without the prior written consent of the other party except that either party may assign its interest under this Agreement to a successor to all or any substantial portion (more than 50%) of its business or assets, or to any parent, subsidiary, or affiliated company having a common parent. Any purported assignment of this Agreement or any part thereof, except as set forth above, shall be void.

Any provision of this Agreement which is prohibited or unenforceable in any jurisdiction shall, as to such jurisdiction, be ineffective to the extent of such prohibition or unenforceability without invalidating the remaining provisions hereof, and any such prohibition or unenforceability in any jurisdiction shall not invalidate or render unenforceable such provision in any other jurisdiction. To the extent permitted by applicable law, the parties hereby waive any provision of law which renders any provision hereof prohibited or unenforceable in any respect.

[The remainder of this page intentionally left blank.]

This Agreement shall be governed in all respects, including, but not limited to, interpretation and performance by the laws of the State of Kansas. Remedies herein reserved are cumulative and in addition to any other or further remedies Seller or Buyer may have at law or in equity.

No termination of this Agreement shall affect the rights or obligations theretofore accrued.

IN WITNESS WHEREOF, the parties have executed this Agreement the day and year first above written.

FARMLAND INDUSTRIES, INC. (Seller)	EL DORADO CHEMICAL COMPANY (Buyer)
By:______________________________	By:____________________________
Title:___________________________	Title:_________________________
Date:____________________________	Date:__________________________

AGREEMENT

This Agreement ("Agreement"), dated as of March 23, 1999, is made among El Dorado Nitrogen Company, an Oklahoma corporation with an office and principal place of business in Oklahoma City, Oklahoma ("El Dorado Nitrogen"), El Dorado Chemical Company, an Oklahoma corporation with an office and principal place of business in Oklahoma City, Oklahoma ("El Dorado Chemical"), Bayer Corporation, an Indiana corporation with an office and principal place of business in Pittsburgh, Pennsylvania ("Bayer"), ICF Kaiser Engineers, Inc., an Ohio corporation with an office and principal place of business in Fairfax, Virginia ("Kaiser"), ICF Kaiser International, Inc., a Delaware corporation with an office and principal place of business in Fairfax, Virginia ("Kaiser International"), and Acstar Insurance Company, a Connecticut corporation with an office and principal place of business in New Britain, Connecticut ("Acstar").

WITNESSETH:

WHEREAS, on August 26, 1997, El Dorado Nitrogen, Kaiser, and Kaiser International, as guarantor of the performance of Kaiser, entered into a contract, as amended, amended and restated, supplemented or otherwise modified (the "Contract"), for the design and construction of a certain nitric acid plant with a production capacity of 1,265 short tons per day and all necessary ancillary work and connections, located in Baytown, Texas, all as more particularly described in said Contract (the "Project");

WHEREAS, El Dorado Nitrogen, as set out in the Contract, acts as the duly authorized construction agent of the Project's owner, First Security Bank, National Association, as trustee;

WHEREAS, on September 10, 1997, Acstar, as surety, issued for said Project a certain performance and payment bond (No. 7362) with Kaiser as the principal, and El Dorado Nitrogen and Bayer as the dual obligees (the "Bond");

WHEREAS, in connection with the issuance of the Bond Kaiser executed and delivered to Acstar an indemnification agreement (the "Indemnification Agreement");

WHEREAS, Kaiser failed to complete the Project in the time specified in the Contract;

WHEREAS, Kaiser, during the course of performance, failed to make certain payments due certain subcontractors for labor and materials provided to the Project;

WHEREAS, certain subcontractors or suppliers to Kaiser on said Project have made claims, or have threatened to make claims, or may in the future make claims, against the Bond for alleged non-payment of labor and materials provided on the Project, which claims (so far as they relate to the time period prior to February 1, 1999) are set forth and described in Schedules A, B and C attached hereto (the "Subcontractor Claims") and subcontractors or suppliers making such claims are herein referred to as the "Subcontractors";

WHEREAS, on or about January 29, 1999, El Dorado Nitrogen issued a Notice of Default (the "Notice of Default") to Kaiser, demanding that Kaiser cure certain Events of Default alleged therein within ten (10) days or suffer a default termination;

WHEREAS, the Notice of Default was sent by El Dorado Nitrogen to Acstar;

WHEREAS, Kaiser disputed certain allegations made by El Dorado Nitrogen in the Notice of Default; and

WHEREAS, since January 29, 1999, the parties hereto have been engaged in continuous discussions and other efforts to resolve their disputes and disagreements;

NOW, THEREFORE, for good and valuable consideration and in consideration of the mutual covenants contained herein, and intending to be legally bound, the parties agree and covenant as follows:

1. Acstar hereby waives and releases any and all rights it has to conduct an investigation to determine what defenses it has under the Bond and to assert any such defenses.

2. Acstar, Kaiser and Kaiser International hereby waive and release any and all rights or claims they have to any unpaid Contract funds , whether deemed unearned Contract balance or earned retainage (the "Contract Funds"). Said Contract Funds shall be expended by El Dorado Nitrogen for the completion of the Project.

3. Kaiser represents and warrants to El Dorado Nitrogen, El Dorado Chemical and Bayer that Schedules A, B and C comprise a complete listing of Subcontractors and Subcontractor Claims and cumulatively represent a complete listing of all amounts due and owing through January 31, 1999 on the Project. Schedules A, B and C are in all respects true and accurate to the best of Kaiser's knowledge, after due inquiry, and represent invoices (other than a claim of Shaw in the amount of $1,335,997 million (the "Disputed Amount"), which amount is being deposited in an escrow account pursuant to paragraph 5 hereof) that are due and owing through January 31, 1999 to the indicated Subcontractor.

4. On a date no more than ten (10) business days after the date hereof, Acstar agrees to pay to the Subcontractors listed in Schedule B an amount equal to $11,564,003. The actual date of such $11,564,003 payment and the deposit by Acstar of the $1,335,997 into the escrow account pursuant to paragraph 5 hereof is herein referred to as the "Effective Date." Prior to or contemporaneously with the payments set forth on Schedule B, Kaiser, Acstar, Bayer and El Dorado Nitrogen shall receive from each such Subcontractor, as a condition of the payments set forth

on Schedule B, a full release of claims and liens for all work performed prior to February 1, 1999, and a written acknowledgement and waiver that such payment constitutes payment of all amounts due to such Subcontractors for work performed or materials provided prior to February 1, 1999. Acstar shall receive from each Subcontractor listed on Schedule B a complete and full release of any and all claims or rights such Subcontractor may have against Acstar under the Bond, with the exception of Shaw Constructors in the amount of $1.0 million, and with the exception of Insulations Inc., which will provide the same release upon receipt of the payment in paragraph 6.

5. Also on a date no more than 10 business days after the date hereof, Acstar shall pay the Disputed Amount of $1,335,997 to Wilmington Trust Company, as Escrow Agent (the "Escrow Agent") for El Dorado Nitrogen, El Dorado Chemical and Bayer, to be held by it and distributed under and in accordance with the Escrow Agreement, in the form attached hereto as Exhibit A (the "Escrow Agreement"). Such payment to the Escrow Agent shall be final and, except as specifically provided below, neither Kaiser nor Acstar shall have any right or claim to recovery of any portion thereof, whether or not paid to Shaw under the terms of the Escrow Agreement. Kaiser and El Dorado Nitrogen shall cooperate in the performance by Kaiser of the third party audit of the invoices from Shaw Constructors. In the event that any portion of the Disputed Amount is not paid to Shaw Constructors (the "Recovery"), then Kaiser shall first receive reimbursement from the Recovery of the out of pocket audit fees actually incurred by Kaiser. After reimbursement of such audit fees, then the Recovery, up to the amount of $600,000, shall be used by El Dorado Nitrogen first for payment and satisfaction of its obligation under paragraph 7 to make the El Dorado Payment. In the event any funds remain in said Escrow Account after the full disbursement of the amounts set forth in the preceding sentence,

then provided Kaiser has made the payments under paragraph 6, Kaiser may use any such remaining funds to pay for costs it incurred at the Project other than the $500,000 amount pursuant to paragraph 6 hereof.

6. With respect to Subcontractor Claims, Kaiser and Kaiser International jointly and severally shall pay an amount equal to $500,000 (the "$500,000 Amount") in two (2) installments of $250,000 each. The first $250,000 installment shall be paid by Kaiser no later than April 1, 1999. The second $250,000 installment shall be paid by Kaiser no later than May 1, 1999. The payments of the $500,000 Amount shall be disbursed in accordance with Schedule C attached hereto. All parties shall receive, as a condition of the payments set forth on Schedule C, a full release of liens for all work performed prior to February 1, 1999, and a written acknowledgement and waiver that such payment constitutes full and final payment of all amounts due to such Subcontractors for work performed or materials provided prior to February 1, 1999. Acstar shall receive from each Subcontractor listed on Schedule C a complete and full release of any and all claims or rights such Subcontractor may have against Acstar under the Bond.

7. Also, with respect to Subcontractor Claims, El Dorado Nitrogen shall pay to Subcontractors, for Subcontractor Claims only and in connection with this Agreement only, up to a maximum total amount of $600,000 (the "El Dorado Payment"), towards Subcontractor Claims set forth in Schedule A. Kaiser and Kaiser International jointly and severally shall pay all additional or other amounts necessary to make full payment and satisfy all amounts owed to any Subcontractors, material providers, consultants or other costs associated with the Project incurred

prior to February 1, 1999. As a condition of such payments, Acstar, Kaiser, Bayer and El Dorado Nitrogen shall receive a release of claims and liens for all work performed prior to February 1, 1999 and a written acknowledgement and waiver that such payment constitutes full and final payment of all amounts due to such Subcontractors for work performed, or services provided, or materials provided prior to February 1, 1999. The party paying such Subcontractor listed on Schedule A shall use best efforts to obtain from such Subcontractor a complete and full release of any and all claims or rights such Subcontractor may have against Acstar under the Bond.

8. If Kaiser and Kaiser International shall fail to pay the $500,000 Amount described in paragraph 6 above on the due date of each installment, on a date five (5) Business Days following the date on which the conditions set forth below have been satisfied, Acstar shall pay such amount to the Subcontractors in accordance with Schedule C. Acstar's obligations under this paragraph 8 shall be subject to (i) its prior full recovery of an amount equal to $12.9 million under the Indemnification Agreement, (ii) its determination, as evidenced by an opinion of its counsel, that it has a present and enforceable right to recover such $500,000 and its ability to obtain full satisfaction of said right, under the Indemnification Agreement. Amounts paid by Acstar under this paragraph 8 shall be distributed as though paid by Kaiser under paragraph 6.

9. El Dorado Nitrogen and El Dorado Chemical, jointly and severally, hereby agree to indemnify Acstar and hold it harmless from and against any and all Subcontractor Claims and any and all claims for labor or material provided by a Subcontractor or supplier to the Project, including all reasonable attorneys' fees and other costs of litigation incurred by Acstar in defending any such claims, except such fees and costs incurred prior to the Effective Date. The indemnification obligation hereunder is conditioned on Acstar providing written notice of any claim to El Dorado Nitrogen and El Dorado Chemical, within 15 business days for claims and within seven (7) business days for lawsuits, of

Acstar's receipt thereof. Upon receipt thereof, El Dorado Nitrogen and El Dorado Chemical shall provide a defense for Acstar against any such conforming claim.

10. On the Effective Date, the Notice of Default issued by El Dorado Nitrogen against Kaiser shall be withdrawn without prejudice.

11. Kaiser shall continue performance of the Contract as EPC Contractor in accordance with the terms and conditions of the Contract (except as expressly and specifically modified herein) and provide, at no cost to El Dorado Nitrogen or El Dorado Chemical, all the proper and appropriate supervisory personnel, including, without limitation, all technical and engineering personnel, all start-up and commissioning personnel, and such other personnel necessary to manage and direct its Subcontractors and perform all other necessary services to complete the Project, as provided in the Contract, except as modified with respect to Completion Dates by paragraph 13 hereof (the "Completion Effort").

12. During said Completion Effort, El Dorado Nitrogen will be represented by its consultant, Benham Constructors, Inc. ("Benham"), and Kaiser shall cooperate with Benham in its participation in the Completion Effort. El Dorado Nitrogen shall pay and be solely responsible for any and all compensation and fees due Benham.

13. On the Effective Date, (i) a new deadline of April 15, 1999 will apply to the Project for initial production of Nitric Acid, (ii) the Completion Date of the Project, as set forth in Section 3 of the Contract, will be deemed to have been extended to May 1, 1999 (the "Extended Completion Dates"),and Final Completion and Final Acceptance, as set forth in Secion 4.7 of the Contract, shall occur no later than June 1, 1999. Except for initial production run testing and the performance test (as required in the Contract), El Dorado Nitrogen shall determine the operating rates and hours of operation of the Project. Kaiser

shall conduct the performance test (as required in the Contract) at the earliest possible time after April 15, 1999, but no later than May 15, 1999, but subject to El Dorado Nitrogen making the Project reasonably available to Kaiser to perform the performance tests and reasonably cooperating with Kaiser to facilitate the performance tests. Expressly contingent on Kaiser's satisfaction of those obligations set forth in paragraphs 6, 7, and 11 hereof, on the Effective Date, El Dorado Nitrogen hereby releases and waives any right it has to liquidated damages for accrued delays prior to April 15, 1999. If, however, either of the Extended Completion Dates is not achieved by Kaiser, as aforedescribed, then Kaiser and Kaiser International, jointly and severally, shall be liable to El Dorado Nitrogen for liquidated damages in the amount of Forty-Four Thousand Dollars ($44,000) per day for each day of the delay after April 15, 1999 or May 1, 1999, as the case may be, until the requirement for that date is met, but in no event shall the aggregate total of such liquidated damages exceed $44,000 per day.

14. On the Effective Date, El Dorado Nitrogen and El Dorado Chemical, on the one hand, and Kaiser and Kaiser International on the other, hereby release each other from any and all claims, causes of action, debts, damages, and demands whatsoever, each ever had or now has against the other, or the other's parents, subsidiaries or affiliates, arising out of or relating to the liquidated damages under the Contract prior to April 15, 1999 or the failure of Kaiser or Kaiser International to complete the Contract or the Project prior to March 23, 1999, provided, however, that this release in no manner affects any obligation set forth in the Contract including, without limitation, all warranty obligations, design obligations and Project performance guarantees of Kaiser, Kaiser International or Kaiser's Subcontractors under the Contract (unless and solely to the extent such obligation is specifically and expressly modified by this Agreement) or any of the obligations set forth in this Agreement. The effectiveness of this release is subject to the

performance by El Dorado Nitrogen and El Dorado Chemical, on the one hand, and Kaiser and Kaiser International, on the other hand, of their respective obligations in this Agreement and in the Contract.

15. Except as specifically and expressly modified in this Agreement, all obligations and responsibilities of the parties under the Contract remain unchanged and in full force and effect.

16. Upon satisfaction of Acstar's obligations in paragraph 4 and paragraph 8 (if any shall arise), El Dorado Nitrogen and Bayer, as obligees under the Bond, and Kaiser as principal under the Bond, hereby release Acstar as surety under the Bond from any and all claims, causes of action, debts, damages and demands whatsoever any ever had, now has or may have against Acstar, its parents, subsidiaries or affiliates, arising out of or relating to the Bond on the Project in any way whatsoever from the beginning of the world to the date hereof.

17. Kaiser shall provide to El Dorado Nitrogen on behalf of itself and its Subcontractors a complete set of documentation as required by the Contractincluding, but not limited to, all inspection reports, test reports, approvals and certifications of the work, in accordance with Exhibit B.

18. This Agreement represents and contains the entire understanding of the parties and may not be amended except by a writing executed by all parties.

19. Subject to paragraph 3 hereof, the parties acknowledge that Schedules A, B, and C may require adjustment in the event it is determined that the exact amounts due to Subcontractors differs from that set out in those schedules.

20. This Agreement may be executed in one or more counterparts, each of which shall be deemed an original, but all of which shall constitute one and the same Agreement.

IN WITNESS WHEREOF, the parties have made and executed this Agreement on the date as first set forth above.

ATTEST: EL DORADO NITROGEN COMPANY

____________________________ By: ____________________________
Its
____________________________ Duly Authorized

ATTEST: EL DORADO CHEMICAL COMPANY

____________________________ By: ____________________________
Its
____________________________ Duly Authorized

ATTEST: BAYER CORPORATION

____________________________ By: ____________________________

Its
____________________________ Duly Authorized

ATTEST: ICF KAISER ENGINEERS, INC.

____________________________ By: ____________________________

Its
____________________________ Duly Authorized

ATTEST: ACSTAR INSURANCE COMPANY

___________________________ By: __________________________

Its

___________________________ Duly Authorized

ATTEST: ICF KAISER INTERNATIONAL , INC.

___________________________ By: __________________________

Its

_________________________ Duly Authorized

SCHEDULE "A"

Contract/PO	Number	Payor	Value
Adrian	3003	EDNC	$20,708.48
Cajun	3004	EDNC	41,657.00
Cooper Heat	3019	EDNC	17,616.0
Epcon	3103	EDNC	145,930.50
Grinnel	3015	EDNC	17,488.00
Tracer	3016	EDNC	103,518.81
Pace		EDNC	100,000.00
Pipe Tech	3018	EDNC	114,671.74
Marley	3005	EDNC	18,736.00
Phillips	3007	EDNC	18,501.22
League City	3011	KAISER	6,843.00
Plant Maint. Service	3105	KAISER	1,568.00
Misc. Equip.		KAISER	7,061.00
Heat Exchangers		KAISER	1,872.00
Filters		KAISER	7,588.00
Pumps		KAISER	7,157.00
Electrical Equip.		KAISER	17,684.00
Structural		KAISER	3,487.00
Expansion Joints		KAISER	14,865.00
Pipe/Fittings/Etc.		KAISER	26,323.00
Pipe Supports		KAISER	5,747.00
Start-Up Vendor PO's		KAISER	102,092.00
TOTAL			$801,114.80

SCHEDULE "B"

Contract/PO	Number	Value
Shaw	3009	$11,624,600.93
ISC	3013	896,920.33
Insulation Inc.	3017	378,478.74
TOTAL		$12,900,000.00

SCHEDULE "C"

Contract/PO	Number	Value
		April
Insulation Inc.	3017	$212,812.19
Adrian		37,187.81
SUBTOTAL - APRIL		$250,000.00
		May
Adrian	3003	$250,000.00
SUBTOTAL - MAY		$250,000.00
TOTAL -- APRIL & MAY		$500,000.00

EXHIBIT "A"
ESCROW AGREEMENT

Escrow Agreement, dated as of March 23, 1999 (the "Escrow Agreement"), by and among El Dorado Nitrogen Company, an Oklahoma corporation ("EDNC"), as construction agent; El Dorado Chemical Company, an Oklahoma corporation ("EDCC"); and Bayer Corporation, an Indiana corporation ("Bayer"); and Wilmington Trust Company, as escrow agent (the "Escrow Agent").

PRELIMINARY STATEMENT

WHEREAS, EDNC, EDCC, Bayer, ICF Kaiser Engineers, Inc., an Ohio corporation ("Kaiser"), ICF Kaiser International, Inc., a Delaware corporation ("Kaiser International"), and Acstar Insurance Company, a Connecticut corporation ("Acstar"), are parties to a certain Agreement dated as of March 23, 1999 (the "Global Agreement"), pursuant to which certain funds are to be held in escrow and disbursed in conformity with the terms hereof; and

WHEREAS, the Escrow Agent is willing to act as escrow agent hereunder;

NOW, THEREFORE, in consideration of the foregoing premises and the respective agreements of the parties hereinafter set forth, and intending to be legally bound, the parties hereto agree as follows:

ARTICLE I
APPOINTMENT OF ESCROW AGENT;
DEPOSIT OF ESCROW AMOUNT

Section 1.1 Escrow Agent. The parties hereto hereby appoint Wilmington Trust Company, as escrow agent hereunder and Wilmington Trust Company hereby accepts such appointment and agrees to serve as escrow agent, establish the Escrow Account (as defined below) and to hold and dispose of the Escrow Amount (as defined below) exclusively in accordance with the terms of this Escrow Agreement.

Section 1.2 Deposit of Escrow Amount.

(a) Acstar shall deliver to the Escrow Agent immediately available funds in the amount of One Million Three Hundred Seventy-Four Thousand Six Hundred and 93/100 Dollars ($1,374,600.93) ("Escrow Amount") for deposit in trust account #48183-0 (the "Escrow Account") at Wilmington Trust Company, to be held in escrow and in trust by the Escrow Agent; and

(b) The Escrow Agent will act as custodian of the Escrow Amount. The Escrow Agent will receive, hold, invest and release the Escrow Amount in accordance with the terms of this Escrow Agreement.

Section 1.3 Investment of Escrow Amount.

(a) Until such time as the entire Escrow Amount has been released pursuant to the terms hereof, the Escrow Agent shall invest the Escrow Amount in the Money Market Portfolio of the Rodney Square Fund, a mutual fund managed by Rodney Square Management Corporation, a subsidiary of Escrow Agent. The parties acknowledge that shares in this mutual fund are not obligations of Wilmington Trust Company, are not deposits and are not insured by the FDIC. Escrow Agent or its affiliate is compensated by the mutual fund for services rendered in its capacity as investment advisor, custodian and/or transfer agent, and such compensation is both described in detail in the prospectus for the fund under the heading "Management of the Fund", and is in addition to the compensation, if any, paid to Wilmington Trust Company in its capacity as Escrow Agent hereunder. The Escrow Agent shall have the power to sell or liquidate the foregoing investments whenever the Escrow Agent shall be required to distribute all or any portion of the Escrow Amount pursuant to Section 2.1 hereof.

(b) Interest earned and credited on the Escrow Amount, less escrow fees payable under Section 3.7 hereof, shall be added to the principal deposited in the Escrow Account with the Escrow Agent hereunder and distributed in conformity with the provisions of Article II hereof. EDNC shall be liable for and pay all taxes due and payable on any interest earned and credited on the Escrow Amount. In connection with any investment of the Escrow Amount, EDNC shall provide the Escrow Agent with its taxpayer identification number.

(c) The Escrow Agent shall not have any liability for any loss sustained as a result of any investment made in accordance with this Section 1.3 (including as a result of any liquidation of any such investment prior to its maturity), except as a result of the Escrow Agent's bad faith, gross negligence or willful misconduct.

Section 1.4 Manner of Payment. The Escrow Agent shall release the Escrow Amount and any interest earned thereon in accordance with the provisions of this Section 1.4 and Article II hereof. Whenever the Escrow Agent shall be required by this Escrow Agreement to deliver any Escrow Amount in conformity with any disbursement request delivered by EDNC, EDCC and Bayer, the Escrow Agent shall make such payment as provided in Article II from any available Escrow Amount. All cash payments required to be made hereunder by the Escrow Agent from the Escrow Amount shall be made in United States Dollars by wire transfer or other immediately available funds to the account and payee designated by EDNC, EDCC and Bayer in the relevant Disbursement Request (defined below).

ARTICLE II
RELEASE OF ESCROW AMOUNT

Subject to Section 3.1 hereof, the Escrow Agent shall release the Escrow Amount and any interest earned thereon only as follows:

Section 2.1 Release of Escrow Amount.

(a) Within seven (7) business days of the date hereof, Kaiser is required pursuant to the terms of that certain Agreement (the "Kaiser Agreement") of even date herewith between Kaiser and Shaw Constructors (a/k/a United Crafts, Inc., a Shaw Group Company) ("Shaw"), to commence an audit of certain outstanding invoices of Shaw related to the performance of work at the El Dorado Nitrogen nitric acid plant site in Baytown, Texas (the "Project') prior to January 30, 1999 (the "Audit"). Subject to Sections 2.1(b) and (c), following completion of the Audit, Kaiser is required pursuant to the Kaiser Agreement to notify EDNC in writing (a "Kaiser Disbursement Notice") that certain funds in the Escrow Account are to be released and paid to Shaw, if the results of the Audit indicate that amounts are undisputed and are due and payable to Shaw. Upon EDNC's receipt of a Kaiser Disbursement Notice indicating that any portion of the Escrow Funds is to be paid to Shaw, EDNC, EDCC and Bayer shall in writing promptly advise the Escrow Agent ("Escrow Release Notice") that the amount set forth in such Kaiser Disbursement Notice shall be paid to Shaw by the Escrow Agent by the second business day following receipt by the Escrow Agent of such Escrow Release Notice.

(b) The Kaiser Agreement provides that in the event that amounts payable to Shaw remain in dispute after completion of the Audit, Kaiser and Shaw shall have thirty days to attempt to resolve such dispute, and if the dispute is resolved within such thirty day period, then the procedures described in clause (a) above following completion of the Audit shall apply.

(c) The Kaiser Agreement provides that in the event that Kaiser and Shaw are unable to resolve their dispute within the thirty-day period described in clause (b) above, the dispute shall be submitted to binding arbitration, and upon receipt of a certified copy of the decision of the arbitrator(s), EDNC, EDCC and Bayer shall promptly provide the Escrow Agent with an Escrow Release Notice, directing the Escrow Agent to pay to Shaw on the second business day following receipt by the Escrow Agent of such Escrow Release Notice, the amount that the arbitrator(s) have awarded to Shaw, to the extent not in excess of the Escrow Amount.

(d) Following resolution of the amounts in dispute between Kaiser and Shaw and payment to Shaw by the Escrow Agent pursuant to clause (a), (b) or (c) above, as applicable, the Escrow Agent shall distribute the remainder of the funds constituting the Escrow Amount to EDNC, and EDNC shall pay such funds to itself or Kaiser, as required pursuant to Section 5 of the Global Agreement. In addition, such distributions may be made to EDNC at any time prior to the resolution of the dispute between Kaiser and Shaw if EDNC directs the Escrow Agent to make such distributions pursuant to an Escrow Release Notice and certifies to the Escrow Agent in writing that Shaw has provided written consent to such release of funds to EDNC and that the results of the Audit provide that such distributions should be made to EDNC or Kaiser. EDNC shall immediately pay to Kaiser any portion of such distributions to which it is entitled in accordance with the results of the Audit.

ARTICLE III
ESCROW AGENT; RIGHTS AND OBLIGATIONS

Section 3.1 Resignation. Except as otherwise expressly provided in this Section 3.1, the Escrow Agent may resign and be discharged from its duties hereunder at any time by giving notice of such resignation to the parties hereto specifying a date (not less than thirty (30) days after the date of receipt by the parties of such notice) when such resignation shall take effect. Upon such notice, a successor escrow agent shall be appointed with the mutual consent of the remaining parties, such successor escrow agent to become Escrow Agent hereunder upon the resignation date specified in such notice. If the parties are unable to agree upon a successor Escrow Agent within thirty (30) days after delivery of such notice, then anything to the contrary in Article II hereof notwithstanding, the Escrow Agent may deposit the Escrow Amount with a court of competent jurisdiction in the State of Delaware. In such event, the Escrow Agent shall have no further liability under this Escrow Agreement. The Escrow Agent shall continue to serve until its successor accepts the escrow and receives the Escrow Amount or the Escrow Amount is deposited in a court of competent jurisdiction in the State of Delaware. The parties (excluding the Escrow Agent) shall have the right at any time upon their unanimous consent to appoint a new escrow agent by giving notice thereof to the then-acting Escrow Agent.

Section 3.2 Limitation of Duties. The duties and obligations of the Escrow Agent shall be determined solely by the express provisions of this Escrow Agreement. Except as otherwise expressly set forth herein, the Escrow Agent shall not be bound in any way by any other agreement or contract among any of the parties.

Section 3.3 Reliance. The Escrow Agent may act in reliance upon any writing, instrument or signature which it in good faith believes to be genuine, may assume the validity and accuracy of any statement or assertion contained in such writing or instrument and may assume that any person purporting to give any writing, notice, advice or instructions in connection with the provisions hereof has been duly authorized to do so. The Escrow Agent shall not be liable in any manner for the sufficiency or correctness as to form, manner of execution, content or validity of any instrument deposited in escrow, nor as to the identity, authority or right of any person executing the same; and its duties hereunder shall be limited to the safekeeping of such certificates, moneys, instruments or other documents received by it as such escrow holder, and for the disposition of the same in accordance with the terms of this Escrow Agreement.

Section 3.4 Indemnification. Each party hereto jointly and severally agrees to indemnify and hold harmless the Escrow Agent from and against all claims, liabilities, losses, actions, suits or proceedings at law or in equity, or any other expenses, fees or charges of any character or nature, which the Escrow Agent may incur or with which the Escrow Agent may be threatened by reason of its acting as Escrow Agent under this Escrow Agreement and in connection therewith to indemnify the Escrow Agent against any and all expenses, including reasonable attorneys' fees of one firm and the cost of defending any action, suit or proceedings or resisting any claim under this Escrow Agreement. Notwithstanding the foregoing, it is specifically understood and agreed that in the event the Escrow Agent is determined to have acted in bad faith, gross negligence or willful misconduct in the exercise of its responsibilities hereunder or negligence in the handling of funds, the indemnification provisions of this Escrow Agreement shall to that extent not apply. Escrow Agent shall have a first lien against the Escrow Account to secure the obligations of the parties hereunder. The terms of this paragraph shall survive termination of this Escrow Agreement.

Section 3.5 Parties Proceeding. If any two parties (considering EDNC and EDCC as a single party) shall be in disagreement about the interpretation of this Escrow Agreement, or rights or obligations hereunder, or the propriety of any action taken by the Escrow Agent hereunder, any one of the parties (including the Escrow Agent) may, in its discretion, commence a proceeding pursuant to Section 4.2 below to resolve said disagreement. The Escrow Agent shall be indemnified for all costs, including reasonable attorneys' fees, in connection with such proceeding, and shall be fully protected in suspending all or a part of its activities under this Escrow Agreement until an order or judgment is received.

Section 3.6 Counsel. The Escrow Agent may consult with independent counsel of its own choosing and shall have full and complete authorization and protection for any action taken or suffered by it hereunder in good faith in accordance with the opinion of such counsel. The Escrow Agent shall otherwise not be liable for any mistakes of fact or error of judgment or for any acts or omissions of any kind unless caused by its gross negligence or willful misconduct.

Section 3.7 Fees. The Escrow Agent shall be paid a fee of U.S. $2,000.00, which shall be paid 50% by EDNC and 50% by Kaiser. In addition, the Escrow Agent shall be reimbursed by the parties for all reasonable expenses, disbursements and advances incurred or made by the Escrow Agent in performance of its duties hereunder. Expenses, disbursements and advances shall be paid solely out of the Escrow Amount, on a quarterly basis. Escrow Agent shall have a first lien against the Escrow Account to secure the obligations of the parties hereunder. The terms of this paragraph shall survive termination of this Escrow Agreement.

ARTICLE IV
MISCELLANEOUS

Section 4.1 Termination. This Escrow Agreement shall terminate upon the disbursement of all of the Escrow Amount pursuant to the terms hereof.

Section 4.2 Governing Law and Dispute Resolution.

(a) The construction and interpretation of this Agreement shall be governed by the internal laws of the State of Delaware, without regard to its conflicts of laws provisions.

(b) The parties hereto hereby irrevocably submit to the jurisdiction of the United States District Court for the District of Delaware (or, if subject matter jurisdiction in that court is not available, in any state court located within the City of Wilmington, Delaware) over any dispute arising out of or relating to this Agreement or any of the transactions contemplated hereby and each party hereby irrevocably agrees that all claims in respect of such dispute or proceeding shall be heard and determined in such court. The parties hereby irrevocably waive, to the fullest extent permitted by applicable Law, any objection which they may now or hereafter have to the laying of venue of any such dispute brought in such court or any defense of inconvenient forum.

(c) Each of the parties hereto hereby consents to process being served by any party to this Escrow Agreement in any suit, action or proceeding of the nature specified in subsection (b) above by mailing of a copy thereof in accordance with the provisions of Section 4.3 of this Escrow Agreement.

Section 4.3 Notices. All notices, requests, demands and other communications made hereunder shall be in writing and shall be deemed duly given when delivered by overnight delivery or personally against receipt or on the third day after deposit with the post office by registered or certified mail, postage prepaid and return receipt requested, as follows, or to such other address or person as a party may hereafter designate by notice to the other party:

Wilmington Trust Company
Rodney Square North
1100 North Market Street
Wilmington, Delaware 19890-0001
Attention: Corporate Trust Department

If to El Dorado Nitrogen and/or El Dorado Chemical:

16 South Pennsylvania Avenue
Oklahoma City, Oklahoma 73107
Attention: President

With copies to:

16 South Pennsylvania Avenue
Oklahoma City, Oklahoma 73107
Attention: General Counsel

If to Bayer:

Bayer Corporation
100 Bayer Road
Pittsburgh, Pennsylvania 15205-9741
Attention: Barry Phillips, Ph.D.
Paul Berry, Esq.

With copies to:

Christopher B. Carson, Esq.
Cohen & Grigsby, P.C.
11 Stanwix Street
Pittsburgh, Pennsylvania 15222

Section 4.4 Amendments. This Escrow Agreement and the provisions hereof, may be amended or modified only by a written document specifically referring to this Escrow Agreement and signed by the parties hereto.

Section 4.5 Entire Agreement. This Escrow Agreement constitutes the entire agreement among the parties with respect to the subject matter hereof and supersedes all prior agreements and understandings, oral and written, among the parties hereto with respect to the subject matter hereof, except for the Global Agreement.

Section 4.6 Counterparts. This Escrow Agreement may be executed in two or more counterparts, each of which shall be deemed an original, but all of which together shall constitute but one and the same instrument. Facsimile copies of the signed original of this Agreement with originals to follow shall constitute execution of this Escrow Agreement.

IN WITNESS WHEREOF, the parties hereto have caused this Escrow Agreement to be executed and delivered on the date first-above written,

EL DORADO CHEMICAL COMPANY

By:_________________________________
Its:_________________________________

EL DORADO NITROGEN COMPANY,
Construction Agent

By:_________________________________
Its:_________________________________

WILMINGTON TRUST COMPANY
As Escrow Agent:

By:_________________________________
Its:_________________________________

BAYER CORPORATION

By:_________________________________
Its:_________________________________

EXHIBIT "B"

I. DOCUMENTATION REQUIRED FOR TURNOVER TO EDNC BEFORE "INITIAL PRODUCTION OF ACID" DATE:

1. Piping and Instrument (P&I) Diagrams Fully updated, hand-corrected version.
2. Hydrostatic Test Records
3. Pneumatic Test Records
4. Radiograph Reeder Sheets
5. Welder Certifications
6. Authorized Inspector (AI) Report of Boiler Code Facilities (required before inspection by EDNC's insurer, see attached information from Arkwright on insurer's documentation requirements which also must be provided by ICF Kaiser)
7. Grounding Test Records
8. Loop Check Sheets (Certain non-critical loops may be waived by EDNC to category II)
9. Relief Valve Certifications
10. List of Spare Parts Provided by ICF Kaiser
11. Electrical Breaker Settings
12. Preliminary Alarm and Trip Settings
13. Logic Diagrams
14. Instrument Locations and Tag Numbers (Acceptable as part of P&I diagrams)
15. Letter from ICF Kaiser Attesting that all Required Certified Drawings are Available.
16. Y2K Compliance Letters
17. Operating Manuals
18. Complete Set of Maintenance Manuals
19. Completed Process Hazards Review Documentation as Required by OSHA
20. Completed Pre-Start-Up Safety Review Documentation as Required by OSHA.

* Records must be submitted in a timely fashion to allow review by EDNC prior to "Initial Production of Acid" date.

II. Documentation Required for Turnover to EDNC by the later of "Final Acceptance" Date, or if such is impractical and not necessary for "Final Acceptance", by no later than June 1, 1999.

21. "As Built" Drawings and Final P&I Diagrams (Paper and CAD versions)
22. Three Dimensional Model of Phase 2 Facilities (current version)
23. Piping Isometrics (all existing drawings)
24. All Radiograph Records Records must be complete (actual radiographs may be retained at ICF Kaiser or the Subcontractor)
25. Weld Maps
26. All Other Applicable Non-Destructive Examination (NDE) Documentation (to be determined)

EXHIBT "B" CONTINUED

27. Instrument Calibration Records (or within 48 hours of subsequent tests)
28. Punchlist (Final Status)
29. Records of Initial Equipment Preparation (e.g. Alignment,
30. Lubrication, Rotation, Test Records)
    Equipment Maintenance Procedures (if not included in maintenance manuals)
31. Mil Test Reports (may be retained by Subcontractor)
32. Final Alarm and Trip Settings
33. Certified Equipment Drawings as required by Code
    Available Mil Thickness Reports on Protective Coatings (as available)
34. Concrete and Masonry Compaction Reports (as available)
35. "As-Built" Drawings for Field-Constructed Vessels such as Storage
36. Tanks (including API certificates)
37. PLC Final Documentation

AGREEMENT

between

EL DORADO CHEMICAL COMPANY

and

INTERNATIONAL ASSOCIATION OF
MACHINISTS AND AEROSPACE WORKERS,
AFL-CIO
LOCAL NO. 224

Effective: August 1, 1998

EL DORADO CHEMICAL COMPANY
El Dorado, Arkansas

TABLE OF CONTENTS

PREAMBLE

This Agreement is made and entered into by and between EL DORADO CHEMICAL COMPANY (hereinafter referred to as the "Company"), and the INTERNATIONAL ASSOCIATION OF MACHINISTS AND AEROSPACE WORKERS, AFL-CIO, LOCAL NO. 224 (hereinafter referred to as the "Union"), which the Company recognizes as the sole bargaining agency for the Maintenance employees of the Company at its chemical plant located north of El Dorado, Arkansas, who are eligible for membership in the Union in accordance with the Labor Management Relations Act of 1947.

ARTICLE I
APPLICATION OF AGREEMENT

The Company hereby recognizes the Union as the exclusive bargaining agency for the employees of the Company at said plant who work in the capacities hereinafter stated in this Article I.

(a) All Maintenance employees, as described in Exhibit "A", engaged in the installation, maintenance and repair of machinery and equipment, but excluding all production, chemical and operating employees, shipping attendants, office and clerical employees, managers, supervisors and guards.

ARTICLE II
PERIOD OF AGREEMENT

This Agreement shall remain in full force and effect for a 3-year contract term
commencing August 1, 1998, at 12:01 a.m., and ending 12:00 Midnight, August 3, 2001. At reasonable times after June 1, 2001, the parties will meet to attempt to negotiate a new contract to be effective for a period beginning after 12:01 a.m., August 4, 2001.

ARTICLE III
MANAGEMENT RIGHTS CLAUSE

The Union expressly recognizes that the Company has the exclusive responsibility for and authority over (whether or not the same was exercised heretofore) the management, operation and maintenance of its facilities and, in furtherance thereof, has, subject to the terms of this Agreement, the right to determine policy affecting the selection, hiring, and training of employees; to direct the work force and to schedule work; to institute and enforce reasonable rules of conduct; to assure discipline and efficient operations; to determine what work is to be done, what is to be produced and by what means; to determine the quality and quantity of workmanship; to determine the size and composition of the work force; to determine the allocation and assignment of work to employees; to determine the location of the business, including the establishment of new locations or departments, divisions, or subdivisions thereof; to arrange for work to be done by other companies or other divisions of the Company; to alter, combine, or eliminate any job, operation, service, or department; to sell, merge or discontinue the business or any phase thereof; provided, however, in the exercise of these prerogatives, none of the specific provisions of the Agreement shall be abridged. The Company will not use the vehicle of subcontracting for the sole purpose of laying off employees or reducing the number of hours available to them.

ARTICLE IV
CHECK-OFF OF UNION DUES

Upon receipt of a signed authorization by an employee requesting deductions from his wages for his monthly union dues, the Company agrees to honor such authorization according to its terms during the life of this Agreement. The form of such individual authorization shall be as set forth in Exhibit "D" hereto.

The Financial Secretary of Local 224, IAM-AW, shall, from time to time, notify the Company in writing of the amount of the monthly deduction to be made, from time to time, under this authorization. All money so deducted by the Company shall be paid to the Union on or before the end of the month during which deductions are made. Upon receipt of written request by an employee, the Company shall, after thirty (30) days' notice, discontinue dues deduction.

ARTICLE V
SENIORITY

Section 1. Length of Service.

Length of service in the bargaining unit and with the El Dorado Plant shall, in that order, govern the promotion, demotion, and transfer of employees.

Section 2. Order of Seniority.

An employee's seniority shall be determined as follows:

Order of Importance	Seniority
1st	Bargaining Unit
2nd	Plant

Section 3. Eligibility for Seniority.

An employee shall be first entitled to seniority in the bargaining unit when he has been continuously employed in that unit for 180 days; his seniority dating from the date of the beginning of such employment.

However, an employee who has been employed in the bargaining unit, who has been laid off prior to his having been employed therein for 180 days continuously, and who is reemployed in the bargaining unit within 180 days from the date upon which he is laid off, shall, upon such reemployment, be entitled to have the number of days which he has worked in the bargaining unit, during the period of his most recent previous employment herein, included in any subsequent computation of his seniority in the bargaining unit and shall be entitled to seniority when he has accrued 180 days on that basis.

The Company shall have the right to layoff or discharge, without cause, any employee who has not worked in the bargaining unit a sufficient length of time to gain seniority, and such action on the part of the Company shall not be the subject of a grievance on the part of the Union under any provision of this Agreement.

Section 4. Filling Vacancies.

(a) Temporary and permanent vacancies will be filled only when the Company sees a need to fill the vacancy. In the event the Company sees a need to fill a vacancy, it will be filled by the employee having the most bargaining unit seniority, who desires the job, and who possesses a skill of the group in which the vacancy occurs. Any person so promoted must accept the duties and responsibilities of the job.

(b) When there is a permanent vacancy in a group and the Company sees a need to fill that vacancy, the Company shall post promptly, and keep posted for fifteen (15) days, notice on its bulletin board of the job vacancy. It shall be the duty of an employee who feels himself entitled to such job on account of his seniority to file his sealed bid for such job with the Plant Manager or his representative, and send a copy thereof to the Chairman of the Shop Committee within said 15-day period. In order to be considered valid, a bid must be signed, dated, and deposited in a locked box marked "I.A. of M. and A.W. Bids" located at the plant entrance gate.

Immediately upon expiration of the posting period of fifteen (15) days, the names of all bidders will be posted on the bulletin board, and the bidder having the most seniority and who desires the job shall be assigned to the group and receive the "C" Mechanic rate of pay if he possesses the necessary skill. In the event no qualified bidder possessing the necessary skill bids on the vacancy, the Company may hire a qualified employee from the outside.

If he does not possess the skill, he will be reduced to the rate that compares to his previous experience beginning not later than the beginning of the work week following the week in which the successful bidder is determined, provided the successful bidder is available to report for work on that day.

If the group vacancy is not filled by the procedure set forth above and the Company sees the need to fill the vacancy, a first-year "E" Mechanic job will be posted for filling outside the bargaining unit.

Notwithstanding any other provisions of this subsection (b), it is agreed that the Company shall have the right at any time during said 15-day posting period to withdraw the posting of a new job in the event the Company decides that such job need not be filled.

(c) Should an employee within a group who is entitled to a promotion desire to waive his opportunity for that promotion, he shall do so by signing a waiver.

(d) In the event that it becomes necessary to establish a permanent rotating shift the Company will notify the Shop Committee to discuss the procedure and shift to be implemented at least thirty (30) calendar days before establishing such shift.

Section 5. Qualifications for Job.

(a) It is not the intention of the parties to this Agreement that any employee shall be permitted to work on a job when he is not qualified to perform the work which that job requires. However, if, in the opinion of the Company, an employee is not qualified for a particular job to which he would otherwise be entitled by virtue of his seniority, and the Company determines that an employee's application for the job shall be denied on the basis of his lack of qualifications, the Company shall notify the Chairman of the Shop Committee and the employee involved of their decision, at least five (5) days prior to the date upon which any other employee is permanently assigned to the job.

Section 6. Seniority List.

Seniority lists will be compiled on April 1 and October 1 and will be available to all employees. One copy of each seniority list will be furnished to the Shop Committee.

Section 7. Seniority Accrued.

Each employee shall retain the seniority accrued to him based upon actual service at the El Dorado Plant.

Section 8. Seniority - Outside Assignments.

Any employee, after having established seniority under the provisions of this Agreement, who is temporarily assigned to another job by the Company (outside the bargaining unit) shall continue, for not more than ninety (90) days per calendar year, on a cumulative basis, to accrue seniority on his regular classifica tion during such period of temporary assignment. If such employee works more than ninety (90) days per calendar year on a cumulative basis, he shall forfeit one (1) day of bargaining unit seniority for each day in excess of ninety (90) days worked outside of the bargaining unit during that calendar year.

Section 9. Discharges and Reemployment.

When there is a reduction in the number of employees in the bargaining unit, the employee last employed in the bargaining unit shall be the first employee laid off. The employee laid off through no fault of his own, who has the greatest bargaining unit seniority, shall (subject to the following provisions of this Article) be the person first reemployed in the event additional employees are employed, provided that the person is qualified to perform the duties of the job to which he would be assigned on reemployment.

A person who has worked in the bargaining unit sufficiently long to be entitled to seniority in that unit, and who is laid off through no fault of his own, who has kept his current address on file with the Company, and who continues to be entitled to seniority under the terms of this Agreement shall (subject to the following provisions of this Article) be given first consideration for reemployment.

If reemployment is available for any such person, the Company shall so notify him by letter (with a copy of such letter to the Chairman of the Shop Committee), addressed to him at his address then on file with the Company, and he shall be allowed fifteen (15) days from the date upon which said letter was mailed, or until he no longer retains his accrued seniority as provided in Section 10 of this Article V (whichever is the shorter period), in which to notify the Company in writing of his desire to return to work. In the event he delivers such notice, he shall be allowed seven (7) days from the date of the delivery thereof to report for work; provided, however, if the employee involved is, on the date which he would otherwise be required to report for work totally disabled to work, he shall, on or before that date, deliver to the Company a statement in writing from a licensed physician stating that he is so disabled, in which event the period within which he shall be permitted to return to work shall be extended ninety (90) days.

Section 10. Status of Employees Laid Off.

The accrued seniority of an employee who has been laid off through no fault of his own shall continue to exist from the date of his layoff for the following periods:

Years of Service	Period Seniority to Exist
0-180 days	-0-
181 days to 2 years	Length of previously accrued seniority
2 years or more	2 years

Section 11. Loss of Seniority.

Seniority shall be lost and employment terminated for any of the following reasons:

(a) Quitting.

(b) Absence from work for three (3) consecutive days without having notified the Company, unless physically impossible to do so.

(c) Discharge for just cause.

(d) Failure to return at the expiration of a leave of absence or vacation.

(e) If an employee misrepresents the reason for requesting a leave of absence.

(f) If an employee fails to file for reinstatement within ninety (90) days following discharge from the U.S. Military Service.

(g) Failure to return to work from layoff within the time specified in Section 9 of this Article.

(h) At the end of the period specified in Section 10 of this Article, or upon earlier rejection after layoff of an offer of reemployment in a classification equal to the classification from which laid off.

ARTICLE VI
HOURS OF WORK AND OVERTIME

Section 1. Hours of Work.

(a) Regular base hours of work shall be eight (8) hours per day and forty (40) hours per week.

(b) The work week shall begin at 12:01 a.m. each Monday and end at 12:00 midnight the following Sunday. The work day shall begin at 12:01 a.m. and end at 12:00 midnight.

(c) The work week shall normally be five (5) consecutive 8-hour days, Monday through Friday, and will normally begin work at 7:00 a.m. and end at 3:30 p.m. with a 30-minute lunch period from 12:00 noon to 12:30 p.m.

(d) No employee shall be required to work more than twelve (12) hours during any normal work day except in case of an emergency.

(e) All employees shall be expected to report to work promptly at the scheduled time. No employee shall be permitted to work if such employee reports for work more than one and one-half (1-1/2) hours after his regular scheduled reporting time, unless such delay has been previously excused by the Company.

(f) No employee shall be allowed to work more than sixteen (16) continuous hours nor more than sixteen (16) hours in any one day except in the case of an emergency. However, an employee will be allowed to complete his regularly scheduled hours of work as provided in Sections 5, 8 and 10 of this Article VI.

(g) Maintenance overhauls may be staffed on 8-hour, 10-hour, or 12-hour shifts as may be necessitated by the needs of the operation.

The Company will specify and select the number and classifica-

tions of personnel on each shift by work group classification for each particular overhaul on a shift basis. Preference to shifts will be governed by the employee's bargaining unit seniority. Shift change notice will be handled as outlined in Article VI, Section 3. In the event there are insufficient qualified personnel on each shift, the Company shall have the right to assign qualified personnel as needed.

Section 2. Overtime and Call-Out Pay Rates.

(a) Overtime and call-out rates shall be one and one-half (1-1/2) times the regular rate and shall be paid for all work performed in excess of forty (40) hours per week, continuous actual work in excess of eight (8) hours, and for all work performed as a result of call-out and for hours worked outside an employee's regularly scheduled hours.

(b) Any employee who works over, beyond his regular scheduled work day, shall be paid a minimum of three (3) hours at straight time. If the employee is required to stay over beyond his regular scheduled work day to attend meetings or to receive training, and no production work is involved, he will receive pay for actual time spent at one and one-half (1-1/2) times his regular rate of pay, providing he has received a minimum of twenty-four (24) hours' notice in advance.

(c) No employee shall work overtime without the approval of his Foreman.

Section 3. Shift Change Notice.

(a) The Company shall pay each employee one and one-half (1-1/2) times his regular rate of pay for the first shift of a rearranged work schedule if the employee whose shift is changed shall not have been notified of the change at least twenty-four (24) hours prior to the beginning of said first shift. If notice of employee's shift change shall be posted on his regular day off, notice of the change shall be posted at least seventy-two (72) hours prior to the beginning of said first shift. Any notice required to be given to an employee under the provisions of this Section 3 may be given by written notice posted on the general bulletin board of the Company and the bulletin board of the Union, and each employee named in any notice shall be deemed to have received the notice at the time copies of said notices are posted on said boards.

(b) The changing of an employee's shift, incident to the return of an employee from sickness or accident, shall not be considered a change in shift within the meaning of this Section 3, unless the absent employee has given the Company at least seventy-two (72) hours' notice of his intention to return to work and the time at which he will return to work by notifying his supervisor.

(c) The changing of an employee's shift from 7:00-3:30 to 7:00-3:00, or from 7:00-3:00 to 7:00-3:30 will not constitute a shift change.

(d) A change in shift at the request of an employee shall not be considered a change in shift for the purpose of this Section 3.

(e) No employee shall lose any time from his normally scheduled 40-hour week occasioned by any shift change.

Section 4. Meal Time.

(a) If a "Day Man" is instructed to and continues to work overtime past 6:00 p.m., he shall be allowed a 30-minute period beginning at 6:00 p.m. for supper on Company time; and if said "Day Man" then continues to work additional overtime, he shall be allowed a 30-minute lunch period on Company time; each such period to begin at the end of four (4) hours of additional continuous overtime worked after 6:30 p.m.

(b) Any employee called for work outside of his regular working hours, who is required to work more than four (4) consecutive hours outside his regular hours, shall be allowed a 30-minute period for a meal on Company time at the end of the fourth consecutive hour and at the end of each consecutive 4-hour period thereafter that said employee continues to work outside his regular hours.

Section 5. No Reduction of Work Week as Result of Overtime.

No employee will be required to take any time off from his regular work week because of overtime worked in that or any other week. If an employee is required to work on his day off, he shall not be forced to take another day off in lieu thereof.

Section 6. Computation of Overtime.

For the purpose of computing overtime under this Article, the exact time worked, rounded to the nearest quarter hour, shall be accounted for, which shall be paid for at the overtime rate.

There shall be no duplicate payment for daily overtime and weekly overtime. If daily overtime is greater in any one work week, only daily overtime shall be paid, or if weekly overtime is greater in any one work week, only weekly overtime shall be paid. There shall be no pyramiding of overtime.

Section 7. Distribution of Overtime and Call-Out Time.

Overtime work opportunities shall initially be distributed, as equitably as practicable, within each work group where the overtime is required in accord with the Company's distribution policy. The Company may then offer such work to employees in other work groups who are qualified.

For the purpose of distributing overtime, the Company will submit a list, biweekly, to the work group steward showing the overtime worked, refused and overtime standing of each employee covered within the group.

Each employee who is requested to report for overtime duty shall report at the required time unless he shall first obtain permission from his supervisor to be relieved of such duty.

Section 8. Call-Out.

An employee who is called out and reports for work outside his regular working hours shall work until excused by the person then supervising his work; provided that no one shall be required to work longer than is provided in Section 1(d) of this Article. An employee who is called out and reports for work shall be paid a minimum for four (4) hours at time and one-half (1-1/2), even though the full four (4) hours may not be worked because no work is available, or he does not work at all because no work is available. An employee called for such work, who works continuously until the beginning of his regular hours of work and continues to work during the regular hours of his scheduled work, shall not be considered to have had a change in shift within the meaning of Section 3 of this Article VI.

A description of the work or jobs to be done, or the problem necessitating the call-out, is provided as accurately as possible by the supervisor in order that the person being called may judge: (a) whether or not he has the ability to do the work, and (b) about how long he may have to work. It is not intended to have a person come out on one job, then surprise him with a list of additional jobs to be done. However, due to emergencies, it cannot be guaranteed that he will only be required to do what he was called for.

Notwithstanding the fact that an employee has been called out for work, such employee shall perform his regular work schedule during the remainder of the work week in which such call-out occurs unless excused from such work.

If an employee is called out for work and works until the beginning of his regular work schedule, the call-out will be considered as ending at the beginning of his regular schedule.

Section 8A. Advance Scheduling of Overtime.

Overtime may be scheduled up to three (3) weeks in advance of the actual time required. In the event the scheduled overtime is cancelled, eight (8) hours' notice will be given or a call-out will be paid.

Section 8B. Right to Assign Qualified Personnel.

In the event overtime distribution and call-out procedures do not provide the Company with sufficient, qualified personnel to perform the overtime work, the Company shall have the right to assign such work to qualified personnel. The performance of such work is mandatory.

Section 9. Holiday Pay.

The following days shall be considered holidays and normally no work will be performed on the designated holidays except in cases of emergency, around-the-clock shift work, and in those crafts where work is necessary for continued operations:

1. New Year's Day
2. Good Friday
3. Memorial Day
4. July Fourth
5. Labor Day
6. Columbus Day
7. Thanksgiving Day
8. Day after Thanksgiving
9. Last work day before Christmas holiday
10. Christmas Day

When any of these holidays fall on Sunday, the following Monday will be observed as the holiday.

When any of these holidays fall on Saturday, the preceding Friday will be observed as the holiday.

Each employee who is not required to work and who does not work on a holiday shall be paid a bonus equivalent to eight (8) hours at his regular rate at straight time pay, providing he has worked his last scheduled work day immediately preceding the holiday and his first scheduled work day following the holiday unless the failure to work these days is because of confirmed illness or accident no more than five (5) work days before or after the holiday, unless the employee was excused in advance by the Company.

Each employee who works on a holiday will be paid, in addition to the 8-hour bonus mentioned above, one and one-half (1-1/2) times his regular rate of pay.

Section 10. Reporting for Work and Not Used.

Except when no work is available due to Act of God, such as fire, flood, explosion, or tornado, an employee who reports for duty on his regular schedule shall be given the opportunity of working a full 8-hour shift.

ARTICLE VII
WAGE RATES AND CLASSIFICATIONS

Section 1. Wages and Pay Period.

The regular pay periods for employees subject to this Agreement will cover every two (2) scheduled work weeks, and checks will be available to the men on their regular shifts on the Friday following completion of the 2-week period.

Each employee who works during the period beginning 12:01 a.m., August 1, 1998, and ending 12:00 Midnight, August 3, 2001, shall be paid for his work in that classification on the basis of the basic hourly wage rate for that classification shown on Exhibit "A" to this Agreement. Each employee will be paid the applicable clothing allowances provided on Exhibit "B" to this Agreement.

Section 2. Changes in Classification of Work.

(a) Each employee covered by any classification is expected to perform any duties to which he may be assigned within his classification or lower classification.

(b) It is understood and agreed by the parties hereto that two (2) work groups shall be recognized under this Agreement. A tabulation of the groups with explanatory notes is made in Exhibit "C", Part 1, which is a part of this Agreement.

(c) All Maintenance personnel may be assigned to do any jobs that they have the ability to perform subject to the provisions of Article V, Section 5, and Article XIV, Section 5, of the current contract.

(d) The Company reserves the right to increase or reduce, at any time and from time to time, the number of men employed in any group mentioned in Exhibit "C", Part 1, to that number of men which, in the opinion of the Company, are required to perform work in that group for maintaining the plant. Any such increase or reduction of force in any group shall be made on the basis of bargaining unit seniority in that group. The Company shall advise the employee(s) affected seventy-two (72) hours in advance of any permanent change in the number of persons who shall work in any classification.

ARTICLE VIII
HANDLING OF GRIEVANCES

Section 1. Routine Submission.

(a) For the purpose of adjusting a grievance arising out of the application or interpretation of a written provision of the Agreement, it is agreed that an employee, and/or with his Steward, shall first seek adjustment of the matter with his Foreman; and, if not resolved, the employee, and/or with his Steward, may submit the grievance in writing to his Foreman. No grievance will be considered unless it has been submitted to his Foreman within five (5) working days after the employee knew or should have known that the grievance occurred.

The Foreman shall advise the employee and/or the Steward, in writing, within five (5) days (Saturdays, Sundays and holidays excluded) of his decision on the grievance, if submitted. The grievance must be filed, in writing, on grievance forms provided by the Company and signed by the individual grievant.

If the grievance is not satisfactorily adjusted with the Foreman, the employee and the Steward may submit the grievance to the Shop Committee for handling with the Department Head.

(b) If the Shop Committee elects to process the grievance, it shall submit the grievance to the Department Head, along with a factual statement of the reasons that the Foreman's answer was not satisfactory. The grievance must be submitted to the Department Head within five (5) days (excluding Saturdays, Sundays and holidays) after the date the Foreman advised the Steward and/or employee of his decision. The Department Head shall, within seven (7) calendar days following receipt of the grievance, meet with the designated members of the Shop Committee at a time to be mutually agreed upon. The Department Head shall advise the Shop Committee, in writing, within five (5) days following this meeting (excluding Saturdays, Sundays and holidays) of his decision regarding the grievance.

(c) If the response of the Department Head is not satisfac-

tory, the Shop Committee may submit the matter, in writing, to the Plant Manager within ten (10) days (excluding Saturdays, Sundays and holidays) after the date the Department Head furnishes his grievance response to the Committee. The Plant Manager shall, within ten (10) calendar days following receipt of such grievance (and documentation) meet with the designated members of the Shop Committee, at a time to be mutually agreed upon. The Plant Manager, or his authorized representative, shall render a decision on the grievance, in writing, within ten (10) days (Saturdays, Sundays and holidays excluded) following this meeting.

Section 2. Arbitration.

If the grievance is not adjusted satisfactorily through the procedure hereinbefore mentioned, the issue may be referred to an arbitrator. If the Union desires to submit such grievance to an impartial arbitrator (providing the grievance is one which does not involve matters in which arbitration is specifically prohibited under the terms of this Agreement, and which the Company and Union have mutually agreed to submit to arbitration) it must notify the Company of that fact, in writing, within thirty (30) days after the date the Plant Manager, or other duly authorized representative, advised the Workmen's Committee of his decision.

The Union and the Company shall make written application to the Federal Mediation & Conciliation Service requesting a seven-name arbitrator panel from which the parties shall select one (1) arbitrator. The parties shall alternately each strike one name until only one (1) name remains who shall act as Arbitrator. It is understood that, starting with the first arbitration case following the date of the execution of this Agreement, the Union shall strike the first name. In the next case, the first name shall be stricken by the Company, and alternately the Union and the Company thereafter. Both the Company and the Union shall have the right to reject two (2) panels submitted by the Federal Mediation & Conciliation Service.

When the Arbitrator has been selected, he shall meet for the consideration of the grievance as soon thereafter as is practical. Any such procedure shall be held in El Dorado, Arkansas, unless the parties unanimously decide otherwise.

The expense of the Arbitrator shall be shared equally by the Company and the Union.

The Arbitrator shall decide only the grievance submitted to him upon testimony presented to him by the Union and the Company, and shall render his decision in writing.

Except as otherwise specifically provided in this Agreement, the Arbitrator shall have no power to change the wages, hours, or conditions of employment set forth in this Agreement; he shall have no power to add to, subtract from or modify any of the terms of this Agreement; he shall deal only with the grievance which occasioned his appointment. He will require that the Union has the burden of establishing its position on behalf of the employee, except in a discipline and/or discharge case when the burden will be on management.

The parties hereto shall comply fully with the award or decision made by any such Arbitrator, and the decision of the Arbitrator will be final and binding on both parties.

No provisions of this Article, or of any other Article of this Agreement, shall deprive any employee covered by the terms of this Agreement of any rights to which he may be entitled under Section 9(a) of the Labor Management Relations Act of 1947, or any other Statute of the United States.

The Union has the authority to process, abandon, or settle grievances on behalf of employees. It is provided, however, that no grievance as to wage scales that shall be paid to all or any group of the employees in the bargaining unit shall be submitted to an arbiter, in any event.

The question as to whether a person has been paid the rate to which he is entitled, in accordance with the wage rates set forth in Exhibit "A" to this Agreement, for work which he has performed shall be a subject for arbitration.

The grievance and arbitration provisions provided for herein, in addition to any other right or obligation under the Agreement, are limited to grievances or clams arising and actually filed in writing during the term of this Agreement.

In the event a grievance arises over a discharge or layoff, the first and second steps of the grievance procedure may be bypassed.

ARTICLE IX
SHOP COMMITTEE AND STEWARDS

Section 1. Shop Committee.

The Shop Committee, composed of four (4) members from the employee work force, and management representatives, shall hold regular meetings on a bimonthly basis. It shall be the responsibility of the Shop Committee to submit a written agenda of each subject it wishes to discuss with the Company no less than forty-eight (48) hours before the day of any such meeting. Only three (3) employees in any one group at any one time shall be a member of the Committee.

Section 2. Stewards.

(a) A Steward and an assistant Steward may be elected in each work group by the employees of that group, and the Union shall submit to the Company, in writing, the names of each person so designated. The Company shall consider the person so designated as Steward and assistant Steward of each work group until notified, in writing, to the contrary.

(b) Duly-elected Stewards or Committeemen shall be deemed to possess top ranking seniority for purposes of layoff and recall rights within his respective work group or classification while acting as such.

ARTICLE X
LEAVE OF ABSENCE

Section 1. Personal Business.

If an employee desires to be off on personal business (not emergencies), he may do so with the consent of the Company so long as he does not desire to be off over two (2) work weeks and provided that he gives the Company forty-eight (48) hours' notice of his desire to be absent and the length of time he desires to be off. Upon completion of such leave, he will resume employment on the basis of uninterrupted service.

Section 2. Union Business.

(a) The Company shall, upon a minimum of thirty (30) days' prior written request from an employee and the President of Local No. 224 of International Association of Machinists and Aerospace Workers, grant a leave of absence, extending not longer than fourteen (14) days, to the employee applying for such leave in order that he may, during that leave, engage in work pertaining to the business of Local No. 224 of International Association of Machinists and Aerospace Workers.

Such a leave shall not be granted to more than one (1) employee at any one time. Such employee shall not be granted such a leave for more than an aggregate of thirty(30) days in any one (1) calendar year.

(b) The Company shall grant (upon a minimum of sixty (60) days advance prior written request of an employee and the President or Vice President of International Association of Machinists and Aerospace Workers) a leave of absence for a period not to exceed one (1) year in order that the employee requesting such leave may, during the period of such leave, work as any employee of Interna-

tional Association of Machinists and Aerospace Workers. Not more than one (1) employee shall be permitted to be absent from work at any one time on any such leave.

Section 3. Sickness or Accident.

If an employee who has established seniority is out of service due to occupational injury or occupational disease suffered or contracted while he is in the employment of the Company, he shall retain his seniority accrued at the date of his disability and continue to accrue seniority for a period of twenty-four (24) months or length of previously-accrued seniority, whichever is less, during the period of his disability as a result thereof. If an employee who has established seniority is out of service due to nonoccupational injury or disease suffered while he was in the employment of the Company, he shall retain his accrued seniority for a period of twenty-four (24) months and will accrue seniority in the classification in which he was last regularly employed for a period of one (1) year.

Under either of the above conditions, if an employee should accept an equal or better job elsewhere, his seniority shall be cancelled.

Section 4. Notice to the Company.

When an employee becomes aware of the fact that he is going to be absent from work due to sickness, accident, or other emergency, he must notify his supervisor as far in advance of his scheduled shift as he/she has knowledge of such intended absence, but no less than one (1) hour before the time he is due to report to work. In the event the employee cannot contact his Supervisor, it is permissible to contact any member of Management.

Section 5. Military Reserve Training.

(a) Any regular employee (not probationary) may be granted a special leave of absence for a period not to exceed fourteen (14) days, plus a reasonable period to cover travel time, when required for the purpose of engaging in a training program for Enlisted Reserve, Reserve Officers, or National Guard Encampment, provided:

1. He furnishes the Company with a copy of orders from the military authorities calling him for duty; and

2. He gives advance notice to his immediate supervisor so that arrangements may be made for his replacement during the period of his leave.

(b) Only one (1) leave of absence for Military Reserve Training shall be granted to any employee during a calendar year.

ARTICLE XI
VACATIONS

Section 1.

Normal vacation accruals will be computed in accordance with the following provisions:

(a) Two weeks (80 hours) - after having accrued one (1) year's Company seniority;

(b) Three weeks (120 hours) - during the calendar year in which an employee accrues six (6) year's plant seniority;

In computing length of service for vacations, time spent working at the El Dorado Plant will be used.

Section 2.

Those employees who had previously accrued or who will accrue, during the term of this Agreement, twelve (12) years or more Company seniority shall be entitled to a vacation accrual of four weeks (160 hours). Thereafter, and for all other employees, the maximum vacation accrual shall be as provided in Section 1.

Section 3.

(a) Normally, all vacations will begin with the first work day of the work week schedule.

(b) Vacation pay shall be based upon the straight time rate of an employee's regular classification at the beginning of the vacation and will be taken in accordance with his established work schedule. If a holiday, as defined in Article VI, occurs during an employee's vacation period, the employee will receive pay for said holiday as defined in Article VI.

(c) Each employee must take his vacation during the vacation year (January 1-December 31) in which it falls due, subject to subsections (d) and (i) below.

(d) If an employee is not permitted to take his vacation in any calendar year in which it is due because the Company finds it not convenient to excuse him from work, he shall be paid a sum equal to the sum to which he would have been entitled for working at his regular job based on straight-time pay at normal working schedule during the last part of that year equal to the number of weeks' vacation to which he is entitled.

(e) Except with special permission of the Company, no employee shall be permitted to begin a vacation in any year within three (3) months of the date of the end of the vacation taken by him during the preceding calendar year, and any employee who has received pay in lieu of vacation for one (1) calendar year shall be entitled to his next annual vacation before March 1 of the following year, if it is practical for the Company to give him a vacation.

(f) An employee who (a) resigns, (b) retires, (c) is laid off as part of a reduction in forces, or (d) is granted a military leave under the provisions of Article XII, at a time when he has earned vacation to that date but has not taken, nor previously received pay in lieu of, shall be paid in lieu of any vacation he has earned to that date but has not taken, nor previously received pay in lieu of.

Computation of vacation under this section will be earned at the rate of one-twelfth (1/12th) for each month from employee's anniversary date. Sixteen (16) or more calendar days of employment in any calendar month will be considered a full month in computing vacation accruals.

(g) An employee will not be eligible for overtime or call-out during the period beginning with the first day of his vacation and until his first scheduled work day following completion of his vacation.

(h) In the event of the death of any employee who was then otherwise eligible for a vacation but who had not taken it, a sum of money equal to pay in lieu of such vacation shall be paid to the person(s) who shall be entitled to the personal property of such decedent.

(i) No employee shall receive pay in lieu of vacation except as provided in Article XI, Section 2(d). However, when an employee is absent from work due to authorized occupational injury or illness, or personal sick leave, and has not returned to work by December 31, he may, at the Company's option, be permitted to take his vacation or receive vacation pay between January 1, and April 1 of the following year.

Section 4.

The vacation schedule will be initiated January 2nd of each year for those eligible for vacation in that year. Employees shall choose their vacation periods in order of their bargaining unit seniority. The Company will, insofar as operations permit, arrange by choice and by seniority the employee's request in the vacation schedule. An employee not submitting his vacation preference within a reasonable time after being contacted will have his vacation scheduled during the year at a time convenient to the plant operations.

Normally, subject to operational requirements, the Company will permit from each Maintenance Work Group, a maximum of twenty (20%) percent of the active available employees to be on vacation at the same time.

ARTICLE XII
MILITARY LEAVE

Section 1. Military Selective Service Act.

The rights of employees of the Company who enter Military Service during the term of this Agreement will be governed in all respects by the Military Selection Service Act including amendments.

Section 2. Pay in Lieu of Vacation.

Each such employee who is entitled to a vacation under the vacation policy of the Company at the time he leaves to enter the Armed Forces, who elects not to take the vacation but to receive pay in lieu thereof, shall, upon furnishing to the Company a certificate from his commanding officer establishing the fact that he had been inducted into the military service, be paid the amount of money he would have received had he taken his vacation just prior to the beginning of his military leave.

ARTICLE XIII
PHYSICAL EXAMINATIONS

Section 1. Periodical Examinations.

The Company may, from time to time, require all employees to have periodical physical examinations by a doctor selected by the Company. However, such examinations shall not be used for the purpose of discriminating against an employee. Each employee shall receive his regular rate of pay for all time required to be examined as provided in this Section 1.

Section 2. Certificate of Physical Fitness.

In the case of an employee being absent from work due to illness or physical impairment, he may be required to present a certificate of physical fitness, signed by a licensed physician, before being readmitted to work. This rule, however, shall not limit the right of the Company to require physical examination by a physician in the Company's service in exceptional cases of constantly recurring absence from duty.

Section 3. Dispute Resolution.

Notwithstanding any of the provisions of Article VIII of this Agreement, in case a dispute arises over the physical fitness of an employee to return to work or continue to work, a board of three (3) physicians shall be selected; one by the Company, one by the employee, and one selected by the two so named. The decisions of the majority of this board shall be final and binding.

ARTICLE XIV
MISCELLANEOUS AND GENERAL

Section 1. Tool Check-in Time.

Employees will be allowed fifteen (15) minutes time to clean and check in their tools before quitting time, if such action is required by them.

Section 2. Bulletin Board.

The Company shall maintain at the plant entrance gate at the Chemical Plant a bulletin board which shall be designated as "Local No. 224 Bulletin Board" and shall be for the use of the Union for posting -- subject to the approval of the Company -- of any matters of interest to or affecting the business of the Union. It is understood and agreed that the posting of notices by the Union within the plant area will be on this bulletin board only and will be posted by the Chairman of the Shop Committee or his recognized representative. This bulletin board will be locked with a key, released to the Chairman of the Shop Committee and to the Company.

Section 3. Discrimination.

There shall be no discrimination by the Company against any employee with respect to any conditions of employment on account of his membership in this labor union, or on account of any activity undertaken in good faith in his capacity as a representative of other employees. The Union shall not discriminate against any employee who is not a member of the Union.

Where the male gender is used in this contract, it is intended to refer to both male and female. It is a continuing policy of the Company and the Union that the provisions of this Agreement shall be applied to all employees without regard to race, color, religion, sex, physical disability, national origin, or age.

Section 4. Wage Rate Changes.

There shall be no change in the basic hourly wage rates set forth in Exhibit "A" to this Agreement, or in the clothing allowance set forth in Exhibit "B" to this Agreement, during the term of this Agreement.

Section 5. Safety Provisions.

The Company shall continue to make reasonable provisions for the safety and the health of its employees at the plant during hours of their employment. Protective devices from injury shall be provided by the Company. Employees, subject to this Agreement, will abide by safe practice rules and regulations of the Company, and failure to do so may be considered grounds for dismissal.

No employee shall be required to perform services which, in the considered judgment of the Company and the Union, seriously endanger his physical safety; his refusal to do such work shall not warrant or justify discharge. If any employee refused to perform such work, representatives of the Company and the Union shall immediately attempt to decide the safety factor. Should they be unable to agree, the decision of a representative of the Safety Department of the Company shall be obtained. If the employee still feels an unsafe condition exists, he will not be required to perform that given job, and the Company will have the work done by any means it elects.

Section 6. Discharges.

It is agreed by and between the Company and the Union that the Company may, without limitation upon its right to discharge an employee for any other valid reason, discharge any employee, subject to this Agreement, for the violation of any of the Company's rules or regulations, which said rules and regulations heretofore have been approved by both the Company and the Union.

Section 7. Recess Period (Smoking).

Where men are required to work continuously in restricted and confined areas where smoking is not permitted, the Foreman is authorized to grant a recess of not longer than ten (10) minutes to employees upon request, providing in his judgment, work conditions permit; however, no employee shall be granted more than two (2) such recesses in any one (1) normal work day.

Section 8. Jury Duty.

Each employee of the Company who is called for service upon any grand jury, petit jury or coroner jury shall, after furnishing to his Foreman, a certificate in evidence of his jury service, be paid by the Company for each day which he serves upon said jury a sum equal to the difference between the amount he would have earned if he had been required to work for the Company on that day for the number of hours of his regular work schedule and the jury pay he received, with the provision that no such payment shall be made to an employee for jury service on any day during which, in accordance with his regular work schedule, he would not have worked for the Company.

Section 9. Termination Pay.

An hourly employee whose work comes within the scope of the Fair Labor Standards Act, and who has been continuously employed by the Company for one (1) year, shall, if discharged through no fault of his own, receive a sum equivalent to forty (40) hours' straight time pay at his regular rate, based upon his normal schedule of work, and twice that amount if he has been employed by the Company for a period of five (5) years. No employee shall receive such termination pay more than once in any one (1) calendar year.

Section 10. Contract Work.

It is agreed that any classified work covering maintenance and repair of equipment and machinery now being done by employees of the Company shall not be contracted out as long as the Company has the necessary equipment and as long as there are qualified men available to do the work.

Section 11. Technical and Supervisory Employees.

The Company may use technical and supervisory employees to install temporary test equipment to be used in evaluating conditions and/or performance of plant facilities.

Section 12. Minor Maintenance.

It is agreed that Operating Department personnel will perform minor maintenance functions. Minor maintenance functions shall be similar in scope but not limited to the following examples:

1. Tightening loose mechanical connections.

2. Tightening leaking packing.

3. Changing instrument charts.

4. Tightening piping fittings to stop minor leaks.

5. Changing light bulbs.

6. Hooking up loading and unloading lines.

Section 13. Minor Operating Functions.

Maintenance personnel may perform minor operating functions when requested by production supervision, but only when accompanied by a qualified member of the operations group. Typical example: Assisting in closing or opening large block valves that are difficult for one person to handle.

ARTICLE XV
VALIDITY OF CONTRACT

If any court shall hold any provision of this contract invalid, such decision shall not invalidate the other provisions.

ARTICLE XVI
NOTICE

Any notice to the Company provided herein may be given by depositing same in the U.S. Mail in a sealed envelope, registered, postage prepaid, and addressed to:

El Dorado Chemical Company
P.O. Box 231
El Dorado, Arkansas 71731
Attention: Plant Manager

Any notice to be given to the Union may be given by depositing same in the U.S. Mail in a seal envelope, registered, postage prepaid, and addressed to:

Recording Secretary
International Association of Machinists
and Aerospace Workers, AFL-CIO,
Local No. 224
Box 1332
El Dorado, Arkansas

A copy of notices should be likewise mailed to:

President, International Association of
Machinists and Aerospace Workers
AFL-CIO Machinists Building
9000 Machinist Place
Upper Marlboro, Maryland 20772-2687

ARTICLE XVII
FUNERAL LEAVE

Any employee in the bargaining unit shall be allowed to be absent from work to arrange for or attend the funeral of any one of the relatives of the employee hereinafter stated:

(a) If the deceased relative was the husband, wife, child, father, mother, brother, sister, grandfather, grandmother, or grandchild of the employee, the employee shall be permitted to be absent from work for a period not to exceed two (2) continuous days. One of these days shall be the day of the funeral. The other day may be the day before the funeral or the day after the funeral. If either or both of these days are scheduled working days, he shall be allowed pay for the day(s) off during his regular working schedule.

(b) If the deceased relative was the father-in-law, mother-in-law, brother-in-law, sister-in-law, son-in-law, or daughter-in-law of the employee, the employee shall be permitted to be absent from work with pay for the purposes stated for one (1) scheduled working day if the funeral is held on a scheduled working day. Brother-in-law and sister-in-law will be interpreted as (i) the spouse of an employee's brother or sister; (ii) the brother or sister of an employee's spouse; or (iii) the spouse of an employee's spouse's brother or sister.

(c) If, to attend the funeral for the deceased relative, the employee travels to a point more than 100 miles from El Dorado, Arkansas, he shall be allowed such leave for an additional day with pay.

The pay for each day's leave which the employee receives under the provisions of this Article shall be a sum equal to straight time for his regular schedule of work on the day involved. There shall be no duplication of payment under provisions of this Article for any other employee benefits such as vacation pay, holiday pay, or sickness benefits payments.

Any request for such time off with pay based on false statements will subject the employee making the request to immediate disciplinary action or discharge.

ARTICLE XVIII
GROUP INSURANCE

The Company agrees to provide group insurance benefits. Employees participating in these plans will be furnished a booklet explaining the provisions of the agreements.

Section 1. Group Insurance and Retirement.

Effective with the date of this Agreement the Company and employees will share the cost of employee and employee dependent group insurance coverage on the following basis:

Company 75%
Employee 25%

Effective with the date of this Agreement the Company agrees to pay the cost of employee long-term disability insurance and basic life insurance.

Dental insurance coverage will be made available as an option. The employee may elect to purchase the insurance by paying the premium each month, or by increasing the deductible amounts of the current group medical plan.

The Savings Incentive Plan for Employees, adopted effective December 1, 1985, shall be continued during the term of this Agreement.

ARTICLE XIX
NO STRIKE OR LOCKOUT

There shall be no strike, sympathy strike, or lockout during the term of this Agreement for any reason.

ARTICLE XX
SERVICE WITH COMPANY

The Company shall honor previous service at the El Dorado Chemical Company for purposes of seniority and vacation eligibility only. Previous service at the plant, or any predecessor of the Company, shall not be credited for purposes of pension benefits.

ARTICLE XXI
RETIREMENT AGE

The mandatory retirement age for employees shall be in accord with federal law.

The seniority of each employee whose services are terminated under the provisions of this Article shall cease as of the date of such retirement.

IN WITNESS HEREOF, this instrument is executed on the 1st day of August, 1998, to be effective as of August 1, 1998, at 12:00 a.m.

EL DORADO CHEMICAL COMPANY

By: ________________________________

R.L. Milliken
Senior Vice President,
Manufacturing

INTERNATIONAL ASSOCIATION OF MACHIN-
ISTS AND AEROSPACE WORKERS AFL-CIO,
LOCAL NO. 224

By:

____
Randolph Jiles
Directing Business Representative

Members of the Shop Committee:

____
Jim McKnight

____
Todd Lambert

____
Edward Johnson

____
Wayne Husbands

____
Larry Cannon

EXHIBIT "A"

BASIC HOURLY WAGE RATE

Classification	08/01/98	08/01/99	08/01/00
*"A" Mechanic	$16.71	$17.13	$17.47
*"B" Mechanic	$15.97	$16.13	$16.45
*"C" Mechanic	$15.59	$15.75	$16.07
*"D" Mechanic	$11.70	$11.82	$12.06
*"E" Mechanic-New Hire	**	**	**

*(First 180 Days)
** Rate of pay determined by Company on basis of employees qualifications.

The Company shall have the right to select and appoint employee(s) as Lead. In addition to the regular work of their classification, a Lead may be assigned to train, assist, assign employees, carry out the instructions of supervision, and to perform any other duties pertaining to the maintenance department, which may be assigned by management. The selection of Lead personnel and the duration of their appointment is within the sole discretion of management. While so assigned, Lead(s) shall receive a premium of one dollar ($1.00) above their regular hourly rate.

EXHIBIT "B"

CLOTHING ALLOWANCE

In addition to the hourly rates set forth in Exhibit "A", there shall be paid a clothing allowance of each hour worked, as indicated below:

Clothing Allowance
Per Hour
$.16

EXHIBIT "C"
Part 1

RECOGNIZED MAINTENANCE WORK GROUPS

Group I - Mechanical

Includes work ordinarily done by:

Pipefitter, Plumber
Welder, Lead Burner
Heavy Duty Operator
Rigger
Machinist
General Mechanic
Tank Car Repairman
Carpenter
Painter
Mason, Insulator, Concrete Finisher

Group II - Electrical/Instrumentation

Includes work ordinarily done by:

Electrician
Instrument Repairman

EXHIBIT "D"

EMPLOYEE DUES AUTHORIZATION LETTER

DATE:__________________________

TO: EL DORADO CHEMICAL COMPANY
El Dorado, Arkansas

Until further notice, you are hereby requested and authorized to deduct from wages due me, and payable on the first regular pay day of each month, the sum equal to my monthly dues as set by Local 224, IAM & AW, AFL-CIO, for my account on or before the end of the month during which deductions are made.

"Contributions or gifts to Local Lodge 224, International Association of Machinists and Aerospace Workers are not deductible as charitable contributions for federal income tax purposes. However, they may be tax deductible under other provisions of the Internal Revenue Code."

____
Employee

AMERICANS WITH DISABILITIES ACT
LETTER OF UNDERSTANDING

The Company and Union recognize the provisions of the American's with Disabilities Act may impact the terms of this Agreement, and thus agree to discuss each instance individually in order to reach a mutual understanding.

Dated this 1st day of August, 1998.

EL DORADO CHEMICAL COMPANY

By:_________________________________
R.L. Milliken
Senior Vice President, Manufacturing

INTERNATIONAL ASSOCIATION OF MACHINISTS AND
AEROSPACE WORKERS AFL-CIO, LOCAL NO. 224

By:_________________________________
Randolph Jiles
Directing Business Representative

Members of the Shop Committee:

____
Jim McKnight

____
Todd Lambert

____
Edward Johnson

____
Wayne Husbands

____
Larry Cannon

SHIFT DIFFERENTIAL
LETTER OF UNDERSTANDING

Effective August 1, 1998, in addition to the foregoing hourly rates, employees who are regularly assigned to a specific shift shall be paid a shift differential of forty cents ($.40) for each hour worked on the evening shift and eighty cents ($.80) for each hour worked on the graveyard shift. For payroll purposes, employees who are regularly assigned to a three shift rotating schedule shall receive shift pay averaged over all three shifts (forty cents ($.40) per hour).

NOTE: Maintenance personnel who are not regularly assigned on a rotating shift basis or to the evening or graveyard shift will receive shift differential in accordance with the August 3, 1989, Letter of Understanding (regarding turnarounds and major maintenance projects).

EL DORADO CHEMICAL COMPANY

By:_________________________________

R.L. Milliken
Senior Vice President, Manufacturing

INTERNATIONAL ASSOCIATION OF MACHINISTS AND
AEROSPACE WORKERS AFL-CIO, LOCAL NO. 224

By:_________________________________

Randolph Jiles
Directing Business Representative

Members of the Shop Committee:

____
Jim McKnight

____
Todd Lambert

____
Edward Johnson

____
Wayne Husbands

____
Larry Cannon

NON-QUALIFIED STOCK OPTION AGREEMENT
(Non-Employee Directors - 1998)

THIS NON-QUALIFIED STOCK OPTION AGREEMENT ("Agreement") is made this 22nd day of April, 1998, between LSB Industries, Inc., a Delaware corporation (the "Company"), and Robert C. Brown (the "Optionee");

W I T N E S S E T H:

In consideration of the mutual covenants and conditions herein set forth and for good and valuable consideration, the Company and the Optionee agree as follows:

1. Recitations. The closing price of the Company's common stock, par value $0.10 per share (the "Common Stock") on April 22, 1998 was $4.1875. The "Date of Grant" of this Option is April 22, 1998. This option is not an "incentive stock option" as such term is defined under Section 422 of the Internal Revenue code of 1986, as amended. This option has been approved by the Board of Directors of the Company.

2. Grant of Option. The Company hereby grants to Optionee, as of the 22nd day of April, 1998, the right, privilege and option to purchase an aggregate of Fifteen Thousand (15,000) shares of its Common Stock at $4.1875 per share, under and subject to the terms and conditions of this Agreement.

3. Time and Exercise Option.

3.1 Vesting of Exercise Rights. If this option has not been terminated pursuant to Section 6 hereof, the option herein granted may be exercised by Optionee as hereinafter provided. The option granted hereunder may not be exercised prior to the expiration of six (6) months from the date this option is granted. At any time after the expiration of six (6) months from the date this option is granted, the option may be exercised, in whole or in part, at any time during the remaining term of the option. No option may be exercised at any time unless the Optionee is then a member of the Board of Directors of the Company, except as provided for in paragraph 5.4 hereof.

4. Methods of Exercise and Payment of Exercise Price.

4.1 Notice and Payment. Subject to the terms hereof, this option shall be exercised by the Optionee giving to the Company written notice at the Company's principal place of business setting forth the exact number of shares under this option that the Optionee is purchasing, which may not exceed the number of shares that Optionee is eligible to purchase under this option. Such written notice shall be accompanied by the payment to the Company of the full option price for such number of shares Optionee desires to purchase as specified in such written notice. Further, Optionee shall

comply with such other reasonable requirements as the Committee may establish.

4.2 Method of Payment. Subject to the terms and conditions of this Agreement, payment by the Optionee of the option price may be made in cash or by wire transfer or certified check or bank check or personal check, in each case payable to the order of the Company.

4.3 Withholding. The Optionee understands that, on the exercise of this option, the excess of the fair market value of the Common Stock over its option price is taxable remuneration to him subject to federal income tax withholding by the Company. Not later than the date as of which an amount first becomes includible in the gross income of the Optionee for federal income tax purposes with respect to any award under this Agreement, the Optionee shall pay to the Company, or make arrangements satisfactory to the Company, regarding the payment of any federal, state and local taxes of any kind required by law to be withheld or paid with respect to such amount. The obligations of the Company under this Agreement shall be conditional upon such payment or arrangements and the Company shall, to the extent permitted by law, have the right to deduct any such taxes from any payment of any kind otherwise due to the Optionee from the Company.

4.4 Issuance of Shares. As soon as practicable after its receipt of the notice and payment pursuant to this Section 4, the Company shall cause one or more certificates for the shares so purchased to be delivered to the Optionee or his or her estate, as the case may be; provided that if any law or regulation requires the Company to take any action with respect to the shares specified in such written notice before the issuance thereof, then the date of issuance of such shares shall be extended for a period necessary to take such action.

5. Termination of Option. This Agreement and option granted hereunder, to the extent not theretofore exercised, shall terminate as follows:

5.1 Cessation as Director. Except as otherwise provided in Section 5.4 hereof, upon the cessation of Optionee as a member of the Board of Directors of the Company; or

5.2 Surrender of Options. Upon the Optionee's surrender to the Company for cancellation of this Agreement and the option granted hereunder; or

5.3 Five-Year Term. Upon the fifth (5th) anniversary of the date this option was granted, notwithstanding any provision of this Agreement to the contrary, including, but not limited to, Sections 5.1, 5.2 and 5.4 of this Agreement.

5.4 In Case of Death. If the Optionee dies prior to the termination of this Option, the Option may be exercised within one (1) year after the death of the Optionee by the personal representative of the Optionee's estate, or by a person who acquired the right to exercise the Option by bequest, inheritance, or by reason of the death of the Optionee, provided that the Optionee died while a Director of the Company. The Option may be exercised only as to the number of shares for which the Optionee could have exercised at the time the Optionee died. In no event may the Option be exercised after the expiration of five (5) years from the Date of Grant.

6. Non-Transferability.

6.1 The option will not be transferrable otherwise than by will or the laws of descent and distribution, and the Option may be exercised, during the lifetime of the Optionee, only by Optionee and upon the death of Optionee, as set forth in Section 5.4 hereof. More particularly (but without limiting the generality of the foregoing), the Option may not be assigned, transferred (except as provided above), pledged, or hypothecated in any way, will not be assignable by operation of law and will not be subject to execution, attachment, or similar process. Any attempted assignment, transfer, pledge, hypothecation, or other disposition of the Option contrary to the provisions hereof, and the levy of any execution, attachment or similar process upon the Option, will be null and void and without effect.

6.2 Optionee shall have no right as a stockholder with respect to any shares covered by this Agreement until the date of issuance of a stock certificate to him for such shares. No adjustment shall be made for dividends or other rights for which the record date is prior to the date such stock certificate is issued.

7. Adjustments In the event of a subdivision or consolidation of shares of Common Stock of the Company, the payment of a stock dividend (but only on the Common Stock), a reorganization, consolidation, merger or any other increase or decrease in the number of shares affected without receipt of consideration by the Company, the number of shares of Common Stock then subject to this option and the price per share payable upon exercise of this option shall be proportionately adjusted by the Board of Directors of the Company, whose determination of such adjustment shall be final, binding and conclusive.

8. Rights as a Shareholder. Optionee shall have no rights as a shareholder with respect to any shares covered by this Agreement or the option granted under this Agreement until the date of issuance of a stock certificate to him for such shares. No adjustment shall be made for dividends or other rights for which the record date is prior to the date such stock certificate is issued.

9. Investment Representations. The Optionee hereby represents, warrants, covenants, agrees and acknowledges as follows:

9.1 Restricted Shares. The Optionee represents and warrants that if he acquires any of the shares under this Agreement he will acquire such shares for his own account and for the purpose of investment and not with a view to the sale or distribution thereof, except for sales pursuant to an effective registration statement under the Securities Act of 1933 (the "Act") or pursuant to an exemption from registration under the Act. The Optionee understands that these shares have not and will not have been registered under the Act (the Company being under no obligation to effect such registration) and that such shares must be held indefinitely unless a subsequent disposition thereof is registered under the Act or is exempt from registration. The Optionee further understands that the exemption from registration afforded by Rule 144 under the Act depends upon the satisfaction of various conditions and that, if applicable, Rule 144 affords the basis for sale of such shares only in limited amounts.

9.2 Disposition of Restricted Shares. The Optionee represents, covenants, and agrees that it will not sell or otherwise dispose of the shares acquired under this Agreement in the absence of (a) an effective registration statement under the Act, (b) an opinion acceptable in form and substance to the Company from Optionee's counsel satisfactory to the Company, or an option of counsel to the Company, to the effect that no registration is required for such disposition or (c) a "no-action" letter from the staff of the Securities and Exchange Commission ("SEC") to the effect that such staff will not recommend any action to the SEC if such a disposition takes place without registration.

9.3 Legend. The certificates representing shares covered by this Agreement shall upon issuance thereof have stamped or imprinted thereon or affixed thereto a legend to the following effect:

> The registered holder hereof has acquired the shares represented by this certificate for investment and not for resale in connection with a distribution thereof. Accordingly, such shares have not been registered under the Securities Act of 1933 and may not be sold, transferred or otherwise disposed of except pursuant to a currently effective registration statement under said Act or otherwise in a transaction exempt from the provisions of Section 5 of said Act.

10. Binding Effect. This Agreement shall be binding upon the heirs, executors, administrators and successors of the parties hereto.

11. Subsidiary. The term "Subsidiary" means any present or future subsidiary corporation of the Company, as such term is defined in Section 424(f) of the Code.

12. Governing Law. This Agreement shall be governed by and construed in accordance with the laws of the State of Delaware (without regard to choice of law provisions).

13. Amendments. Subject to the terms of this Agreement, the Board of Directors of the Company may amend any of the provisions of this Agreement, and may at any time terminate this Agreement. However, no amendment may be made to this Agreement which in any material respect impairs the rights of the Optionee under this Agreement without the Optionee's consent.

14. Interpretation. The Board of Directors shall construe and interpret the terms and provisions of this Agreement and shall, at its discretion, make general and special rules and regulations for administering this Agreement, which construction, interpretation, rules and regulations shall be binding and conclusive upon all persons granted option pursuant to this Agreement.

IN WITNESS WHEREOF, the parties hereto have caused this Agreement to be executed the day and year first above written.

LSB INDUSTRIES, INC.

ATTEST:

______________________________ By:________________________________

Assistant Secretary Jack E. Golsen, President

[S E A L]

"Optionee"

____

Robert C. Brown

LSB INDUSTRIES, INC.

1998 STOCK OPTION AND INCENTIVE PLAN

The Board of Directors of LSB Industries, Inc., a Delaware corporation (the "Company"), has adopted this 1998 Stock Option and Incentive Plan (the "Plan"), effective the 13th day of August, 1998, as follows:

1. Purpose. This Plan permits selected officers and employees, prospective employees, consultants and independent contractors of the Company or any Subsidiary who bear a large measure of responsibility for the success of the Company to acquire and retain a proprietary interest in the Company and to participate in the future of the Company as shareholders. The purpose of this Plan is to advance the interests of the Company and its shareholders by enabling the Company and the subsidiaries to offer to its employee-directors, officers, employees, consultants and independent contractors, long-term performance-based stock and/or other equity interests in the Company, thereby enhancing its ability to attract, retain and reward such individuals, and by providing an incentive for employee-directors, officers, employees to render outstanding service to the Company and to the Company's shareholders.

2. Definitions. For purposes of the Plan, the following terms shall be defined as set forth herein:

2.1 "Act" means the Securities Act of 1933, as amended from time to time, or any successor statute or statutes thereto.

2.2 "Agreement" means the agreement between the Company and the Holder setting forth the terms and conditions of an award under the Plan.

2.3 "Board" means the Board of Directors of the Company.

2.4 "Change of Control" means a change of control of the Company pursuant to Section 8.2 hereof.

2.5 "Code" means the Internal Revenue Code of 1986, as amended from time to time, and any successor statute or statutes thereto.

2.6 "Committee" means the Stock Option Committee of the Board or any other committee of the Board which the Board may designate. In all events, the Committee shall consist only of non-employee directors of the Company.

2.7 "Common Stock" means the Common Stock of the Company, par value $.10 per share.

2.8 "Disability" means disability as determined under the procedures established by the Committee for purposes of the Plan.

2.9 "Exchange Act" means the Securities Exchange Act of 1934, as amended from time to time, or any successor statute or statutes thereto.

2.10 "Fair Market Value", unless otherwise required by any applicable provision of the Code or any regulations issued thereunder, means, as of any given date:

2.10.1 the closing price of the Common Stock on the last preceding day on which the Common Stock was traded, as reported on a national securities exchange; and,

2.10.2 if the fair market value of the Common Stock cannot be determined pursuant to clause (i) hereof, such price as the Committee shall determine.

2.11 "Formula Price Per Share" means the highest gross price (before brokerage commissions, soliciting dealers' fees and similar charges) paid for any share of Common Stock at any time during the ninety (90) day period immediately prior to the Change of Control (whether by way of exchange, conversion, distribution, liquidation or otherwise) paid or to be paid for any share of Common Stock in connection with a Change of Control. If the consideration paid or to be paid in any transaction that results in a Change of Control consists, in whole or in part, of consideration, other than cash, the Board shall take such action, as in its judgment it deems appropriate, to establish the cash value of such consideration, but such valuation shall not be less than the value, if any, attributed to such consideration by any other party to such transaction that results in a Change of Control.

2.12 "Holder" means an eligible employee-director, officer, employee, consultant or independent contractor of the Company or a Subsidiary who has received an award under the Plan.

2.13 "Incentive Stock Option" or "ISO" means any Stock Option intended to be and designated as an "incentive stock option" within the meaning of Section 422 of the Code.

2.14 "Non-Qualified Stock Option" means any Stock Option that is not an Incentive Stock Option.

2.15 "SAR Value" means the excess of the Fair Market Value of one share of Common Stock over the exercise price per share specified in a related Stock Option in the case of a Stock Appreciation Right granted in tandem with a Stock Option and the Stock Appreciation Right price per share in the case of a Stock Appreciation Right awarded on a free-standing basis multiplied by the number of shares in respect of which the Stock Appreciation Right shall be exercised, on the date of exercise.

2.16 "Section 16(b) Holder" means such officer or director or ten percent (10%) beneficial owner of Common Stock subject to Section 16(b) of the Exchange Act.

2.17 "Stock Appreciation Right" means the right, pursuant to an award granted under Section 7 hereof, to recover an amount equal to the SAR Value.

2.18 "Stock Option" means any Incentive Stock Option or Non-Qualified Stock Option to purchase shares of Common Stock which is awarded pursuant to this Plan.

2.19 "Subsidiary" means any present or future subsidiary corporation of the Company, as such term is defined in Section 424(f) of the Code.

3. Administration.

3.1 Board; Committee. The Board shall create a committee consisting of three members of the Board. The Board may also appoint one member of the Board as an alternate member of the Committee. Upon such appointment, the Committee shall have all the powers, privileges and duties set forth herein. The Board may, from time to time, appoint members of any such Committee in substitution for, or in addition to, members previously appointed, may fill vacancies in the Committee and may discharge the Committee. The Committee shall select one of its members as its Chairman and shall hold its meetings at such times and places as it shall deem advisable. A majority of its members shall constitute a quorum and all determinations shall be made by a majority of such quorum. Any determination reduced to writing and signed by a majority of the members of the Committee, shall be fully effective and a valid act of the Committee as if it had been made by a majority vote at a meeting duly called and held. The membership of the Committee shall at all times be constituted so as to not adversely affect the compliance of the Plan with the requirements of Rule 16b-3 under the Exchange Act, to the extent it is applicable, or with the requirements of any other applicable law, rule or regulation.

3.2 Power and Authority. The Committee shall have full power and authority to do all things necessary or appropriate to administer this Plan according to its terms and provisions (excluding the power to appoint members of the Committee and to terminate, modify, or amend the Plan, except as otherwise authorized by the Board), including, but not limited to the full power and authority (subject to the express provisions of this Plan):

3.2.1 to award Stock Options and Stock Appreciation Rights, pursuant to the terms of this Plan, to eligible individuals described under Section 5 hereof;

3.2.2 to select the eligible individuals to whom Stock Options or Stock Appreciation Rights, or any combination thereof, if any, may from time to time be awarded hereunder;

3.2.3 to determine the Incentive Stock Options, Non-Qualified Stock Options, Stock Appreciation Rights, or any combination thereof, if any, to be awarded hereunder to one or more eligible employees or persons;

3.2.4 to determine the number of shares to be covered by each award granted hereunder;

3.2.5 to determine the terms and conditions not inconsistent with the terms of the Plan, of any award hereunder (including, but not limited to, share price, any restrictions or limitations, and any vesting, exchange, surrender, cancellation, acceleration, termination, exercise or forfeiture provisions, as the Committee shall determine);

3.2.6 to determine any specified performance goals or such other factors or criteria which need to be attained for the vesting of an award granted hereunder;

3.2.7 to determine the terms and conditions under which awards hereunder are to operate on a tandem basis and/or in conjunction with or apart from other equity awarded under this Plan and cash awards made by the Company or any Subsidiary outside of this Plan;

3.2.8 to determine the extent and circumstances under which Common Stock and other amounts payable with respect to an award hereunder shall be deferred, which may be either automatic or at the election of the Holder; and

3.2.9 to substitute (i) new Stock Options for previously granted Stock Options, which previously granted Stock Options have higher option exercise prices and/or contain other less favorable terms, and (ii) new awards of any other type for previously granted awards of the same or other type, which previously granted awards are upon less favorable terms.

3.3 Interpretation of Plan.

3.3.1 Subject to Sections 3.2 and 9 hereof, the Committee shall have the authority at its discretion to adopt, alter and repeal such general and special administrative rules, regulations, and practices governing the Plan as it shall, from time to time, deem advisable, to construe and interpret the terms and provisions of this Plan and any award issued under this Plan (and to determine the form and substance of all Agreements relating thereto), and to otherwise supervise the administration of this Plan.

3.3.2 Anything in this Plan to the contrary notwithstanding, no term of this Plan relating to Incentive Stock Options shall be interpreted, amended or altered, nor shall any discretion or authority granted under this Plan be so exercised, so as to disqualify the Plan under Section 422 of the Code, or, without the consent of the Holder(s) affected, to disqualify any Incentive Stock Option under Section 422 of the Code.

3.3.3 Subject to Sections 3.2 and 9 hereof, all decisions made by the Committee pursuant to the provisions of this Plan shall be made in the Committee's sole discretion and shall be final and binding upon all persons granted options pursuant to the Plan.

4. Shares Subject to Plan.

4.1 Number of Shares. The aggregate number of shares of Common Stock reserved and available for distribution under this Plan shall be 850,000 shares. If any shares of Common Stock that are subject to a Stock Option or Stock Appreciation Right cease to be subject to such Stock Option or Stock Appreciation Right, or any such award otherwise terminates without a payment being made to the Holder in the form of Common Stock, such shares shall again be available for distribution in connection with future grants and awards under this Plan. The number of shares available for distribution under this Plan shall be reduced by the number of shares of Common Stock issued under this Plan upon the exercise of a Stock Option.

4.2 Character of Shares. The Company may elect to satisfy its obligations to a Holder exercising a Stock Option entirely by issuing authorized and unissued shares of Common Stock to such Holder, entirely by transferring treasury shares to such Holder, or in part by the issue of authorized and unissued shares and the balance by the transfer of treasury shares.

5. Eligibility.

5.1 General. Awards under this Plan may be made to: (i) officers and other employees of the Company or any Subsidiary who are at the time of the grant of an award under this Plan regularly employed by the Company or any Subsidiary, including any full time salaried officer or employee who is a member of the Board (except as provided in the last sentence under Section 3.1); and, (ii) consultants or independent contractors whom the Board believes have contributed or will contribute to the success of the Company.

5.2 Multiple Awards. The Committee shall from time to time designate such employees, consultants or independent contractors to whom options are to be granted, and the number of shares to be subject to each option. The Committee may at any time grant one or more Stock Options or Stock Appreciation Rights or a combination thereof to an individual to whom a Stock Option or Stock Appreciation Right has previously been granted under this or any other stock option plan of the Company, whether or not such previously granted Stock Option or Stock Appreciation Right has been fully exercised.

5.3 Ineligibility for Awards. No person designated by the Board to serve on the Committee, effective at such future time so that he qualifies as a "disinterested person" within the meaning of Rule 16b-3(c) of the Exchange Act, shall be eligible to receive any awards under the Plan during the period from the date such designation is made to the date such designation becomes effective. Notwithstanding Section 5.1 hereof, no member of the Committee, while serving as such, shall be eligible to receive an award under the Plan.

6. Stock Options.

6.1 Grant and Exercise. Stock Options granted under the Plan may be of two types: (i) Incentive Stock Options and (ii) Non-Qualified Stock Options. Only full-time salaried officers or employees may be granted

Incentive Stock Options. Any individual eligible to participate under this Plan may be granted Non-Qualified Stock Options. Any Stock Option granted under the Plan shall contain such terms, not inconsistent with this Plan, as the Committee may from time to time approve. The Committee shall have the authority to grant to any eligible individual Incentive Stock Options, Non-Qualified Stock Options, or both types of Stock Options and, in each case, may be granted alone, in tandem with, or without, or in addition to Stock Appreciation Rights. To the extent that any Stock Option (or portion thereof) does not qualify as an Incentive Stock Option, it shall constitute a separate Non-Qualified Stock Option. Unless granted in substitution for another outstanding award, Stock Options shall be granted for no consideration other than services to the Company or a Subsidiary.

6.2 Exercise Price.

6.2.1 Less Than 10% Shareholder. The exercise price in any option granted under this Plan to an individual who, at the time the Stock Option is granted, does not own stock possessing more than ten percent (10%) of the total combined voting power of all classes of stock of the Company or of any Subsidiary (computed in accordance with the provisions applicable to Section 422(b)(6) of the Code) (a "less than 10% Shareholder") shall be not less than the Fair Market Value of the shares of Common Stock subject to the Stock Option at the time the Stock Option is granted, determined by the Committee in accordance with the applicable regulations and rulings of the Commissioner of the Internal Revenue Service in effect at the time the Stock Option is granted.

6.2.2 10% Shareholder. The exercise price in any option granted under the Plan to an individual who is not a less than ten percent (10%) Shareholder (a "10% Shareholder") shall be not less than one hundred ten percent (110%) of the Fair Market Value of the shares of Common Stock subject to the Stock Option at the time the Stock Option is granted, determined in accordance with the applicable regulations and rulings of the Commissioner of the Internal Revenue Service in effect at the time the Stock Option is granted.

6.3 Option Term. The term of each Stock Option shall be fixed by the Board, but no Stock Option shall be exercisable more than ten (10) years (five (5) years, in the case of an Incentive Stock Option granted to a 10% Shareholder) after the date on which the Stock Option is granted.

6.4 Exercise of Non-Qualified Stock Options. Non-Qualified Stock Options shall be exercisable at such time or times and subject to such terms and conditions as shall be determined by the Committee; provided, however, that no Non-Qualified Stock Option granted under this Plan may be exercised until after the expiration of six (6) months from the date the Stock Option is granted. If the Committee provides, in its discretion, that any Stock Option is exercisable only in installments, the Committee may waive such installment exercise provisions at any time at or after the time of grant in whole or in part, based upon such factors as the Committee shall determine; provided that the Committee cannot waive the requirement that the Stock Option may not be exercised until after the expiration of six (6) months from the date the Stock Option is granted.

6.5 Exercise of Incentive Stock Options.

6.5.1 By an Employee. No Incentive Stock Option granted under this Plan shall be exercisable after the expiration of ten (10) years from the date such ISO is granted, except that no ISO granted to a person who is not a less than 10% Shareholder shall be exercisable after the expiration of five (5) years from the date such option is granted. Employment by a Subsidiary shall be employment by the Company. Unless such requirements are waived by the Committee, the employee, while still in the employment of the Company, may exercise the options as follows:

6.5.1.1 at any time after one (1) year of continuous employment from the date such ISO is granted, as to twenty percent (20%) of the shares subject to the option;

6.5.1.2 at any time after two (2) years of such continuous employment from the date such ISO is granted, as to an additional twenty percent (20%) of the shares subject to the option;

6.5.1.3 at any time after three (3) years of such continuous employment from the date such ISO is granted, as to an additional thirty percent (30%) of the shares subject to the option; and

6.5.1.4 at any time after four (4) years of such continuous employment from the date such ISO is granted, as to all of the shares remaining subject to the option.

The Committee may decide in each case to what extent leaves of absence for government or military service, illness, temporary disability, or other reasons, shall not interrupt continuous employment.

6.5.2 Termination of Employment. Except as otherwise expressly provided in Sections 6.5.3 and 6.5.4 of this Plan or in the Agreement, no Stock Option may be exercised at any time unless the Holder thereof is then an employee of the Company or a Subsidiary.

6.5.3 By a Former Employee. No person may exercise an ISO after he is no longer an employee of the Company or any Subsidiary; except that if an employee ceases to be an employee on account of physical or mental disability as defined in Section 22(e)(3) of the Code ("Former Employee"), he may exercise the ISO within twelve (12) months after the date on which he ceased to be an employee, for the number of shares for which he could have exercised at the time he ceased to be an employee. No ISO granted under this Plan shall in any event be exercised by such Former Employee after the expiration of ten (10) years from the date such ISO is granted, except that no ISO granted to a person who is a 10% Shareholder may be exercisable after the expiration of five (5) years from the date such ISO is granted.

6.5.4 In Case of Death. If any employee or Former Employee who was granted an ISO dies prior to the termination of such ISO, such ISO may be exercised within twelve (12) months after the death of the employee or Former Employee by his estate, or by a person who acquired the right to exercise such ISO by bequest or inheritance, or by reason of the death of such employee or Former Employee, provided that:

6.5.4.1 such employee died while an employee of the Company or a Subsidiary; or

6.5.4.2 such Former Employee had ceased to be an employee of the Company or a Subsidiary on account of physical or mental disability and died within three (3) months after the date on which he ceased to be such employee.

Such ISO may be exercised only as to the number of shares for which he could have exercised at the time the employee or Former Employee died. No ISO granted under this Plan shall in any event be exercised in case of death of an employee or Former Employee after the expiration of ten (10) years from the date such ISO is granted, except that no ISO granted to a 10% Shareholder shall be exercisable after the expiration of five (5) years from the date such ISO is granted.

6.5.5 The Committee may, in its discretion, waive the installment exercise provisions at any time at or after the time of grant, in whole or in part, based on such factors as the Committee shall determine; provided that at all times no ISO may be exercised until the expiration of six (6) months from the date that the Stock Option was granted.

6.6 Termination of Options. A Stock Option granted under this Plan shall be considered terminated, in whole or in part, to the extent that it can no longer be exercised for shares originally subject to it, provided that a Stock Option granted shall be considered terminated at an earlier date upon surrender for cancellation by the Holder to whom such Stock Option was granted.

6.7 Notice of Exercise and Payment. Subject to any installment, exercise and waiting period provisions that are applicable in a particular case, Stock Options granted under this Plan may be exercised, in whole or in part, at any time during the term of the Stock Option, by giving written notice of such exercise to the Company identifying the Stock Option being exercised and specifying the number of shares then being purchased. Such notice shall be accompanied by payment in full of the exercise price, which shall be in cash or, unless otherwise provided in the Agreement, in whole shares of Common Stock which are already owned by the Holder of the Stock Option or, unless otherwise provided in the Agreement, partly in cash and partly in such Common Stock. Cash payments shall be made by wire transfer, certified check or bank check or personal check, in each case payable to the order of the Company; provided, however, that the Company shall not be required to deliver certificates for shares of Common Stock with respect to which a Stock Option is exercised until the Company has confirmed the receipt of good and valuable funds in payment of the purchase price thereof. Payments in the form of Common Stock (which shall be valued at the Fair Market Value of a share of Common Stock on the date of exercise) shall be made by delivery of stock certificates in negotiable form which are effective to transfer good and valid title thereto to the Company, free of any liens or encumbrances, with signature guaranteed by a bank or investment banking firm.

6.8 Issuance of Shares. As soon as practicable after its receipt of such notice and payment, the Company shall cause one or more certificates for the shares so purchased to be delivered to the Holder or his or her estate, as the case may be. No Holder or estate shall have any of the rights of a shareholder with reference to shares of Common Stock subject to a Stock Option until after the Stock Option has been exercised in accordance with Section 6.7 and certificates representing the shares of Common Stock so purchased by the Holder pursuant to the Stock Option have been delivered to the Holder or estate.

6.9 Partial Exercise. A Stock Option granted under this Plan may be exercised as to any part of the shares for which it could be exercised. Such a partial exercise of a Stock Option shall not affect the right to exercise the Stock Option from time to time in accordance with this Plan as to the remaining shares of Common Stock subject to the Stock Option.

6.10 $100,000 Per Year Limitation. To the extent that the aggregate Fair Market Value of Common Stock with respect to which Incentive Stock Options are exercisable for the first time by a Holder during any calendar year (under all of the Company's plans) exceeds $100,000, such excess Stock Options shall be treated as Non-Qualified Stock Options for purposes of Section 422 of the Code.

6.11 Buyout and Settlement Provisions. The Committee may at any time offer to buy out for cash or otherwise settle a Stock Option previously granted, based upon such terms and conditions as the Committee shall establish and communicate to the Holder at the time that such offer is made, including a settlement for exchange of a different award under the Plan for the surrender of the Stock Option.

7. Stock Appreciation Rights.

7.1 Grant and Exercise. Stock Appreciation Rights may be granted in tandem with ("Tandem Stock Appreciation Right") or in conjunction with all or part of any Stock Option granted under this Plan or may be granted on a free-standing basis. In the case of a Non-Qualified Stock Option, a Tandem Stock Appreciation Right may be granted either at or after the time of the grant of such Non-Qualified Stock Option. In the case of an Incentive Stock Option, a Tandem Stock Appreciation Right may be granted only at the time of the grant of such Incentive Stock

Option. Unless granted in substitution for another outstanding award, Stock Appreciation Rights shall be granted for no consideration other than services to the Company or a Subsidiary.

7.2 Termination. A Tandem Stock Appreciation Right shall terminate and shall no longer be exercisable upon the termination or exercise of the related Stock Option, except that, unless otherwise determined by the Board, a Tandem Stock Appreciation Right granted with respect to less than the full number of shares covered by a related Stock Option shall not be reduced until after the number of shares remaining under the related Stock Option equals the number of shares covered by the Tandem Stock Appreciation Right.

7.3 Method of Exercise. A Tandem Stock Appreciation Right may be exercised by a Holder, in accordance with Section 7.4 hereof, by surrendering the applicable portion of the related Stock Option. Upon such exercise and surrender, the Holder shall be entitled to receive such amount in the form of payment determined in the manner prescribed in Section 7.5 hereof. Stock Options which have been so surrendered, in whole or in part, shall no longer be exercisable to the extent Tandem Stock Appreciation Rights have been exercised.

7.4 Exercisability. Tandem Stock Appreciation Rights shall be exercisable only at such time or times and to the extent that the Stock Options to which they relate shall be exercisable in accordance with the provisions of Section 6 hereof and this Section 7, and may be subject to such additional limitations on exercisability as shall be determined by the Committee and set forth in the Agreement. Other Stock Appreciation Rights shall be exercisable at such time or times and subject to such terms and conditions as shall be determined by the Committee and set forth in the Agreement. Notwithstanding anything to the contrary contained herein (including the provisions of Section 8.1 hereof), any Stock Appreciation Right granted to a Section 16(b) Holder to be settled wholly or partially in cash (i) shall not be exercisable during the first six (6) months of the term of such Stock Appreciation Right, except that this special limitation shall not apply in the event of death or disability of such Holder prior to the expiration of the six (6) month period, and (ii) shall only be exercisable during the period beginning on the third business day following the date of release for publication of the Company of quarterly or annual summary statements of sales and earnings and ending on the twelfth (12) business day following such date.

7.5 Receipt of SAR Value. Upon the exercise of a Stock Appreciation Right, a Holder shall be entitled to receive up to, but not more than, an amount in cash and/or shares of Common Stock equal to the SAR Value with the Committee having the right to determine the form of payment.

7.6 Shares Affected Under Plan. Upon the exercise of a Tandem Stock Appreciation Right, the Stock Option or part thereof to which such Tandem Stock Appreciation Right is related shall be deemed to have been exercised for the purpose of the limitation set forth in Section 4.1 hereof on the number of shares of Common Stock to be issued under the Plan, but only to the extent of the number of shares, if any, issued under the Tandem Stock Appreciation Right at the time of exercise based upon the SAR Value.

7.7 Limited Stock Appreciation Rights. The Committee may grant "Limited Stock Appreciation Rights", i.e., Stock Appreciation Rights that become exercisable upon the occurrence of one or more of the events which trigger a Change of Control as defined in Section 8.2 hereof, and shall be settled in an amount equal to the Formula Price Per Share, subject to such other terms and conditions as the Committee may specify; provided, however, if any Limited Stock Appreciation Right is granted to a Section 16(b) Holder such Limited Stock Appreciation Right (i) shall only be exercisable within sixty (60) days after the event triggering the Change of Control; and (ii) may not be exercised during the first six (6) months after the date of grant of such Limited Stock Appreciation Right (except in the event of death or disability of such Holder prior to the expiration of the six (6) month period); and (iii) shall only be exercisable in the event that the date of the Change of Control was outside the control of such Holder; and (iv) shall only be settled in cash in an amount equal to the Formula Price Per Share.

8. Acceleration.

8.1 Acceleration Upon Change of Control. Unless the award Agreement provides otherwise or unless the Holder waives the application of this Section 8.1 prior to a Change of Control (as hereinafter defined), in the event of a Change of Control, each outstanding Stock Option, Stock Appreciation Right and Limited Stock Appreciation Right granted under the Plan shall immediately become exercisable in full notwithstanding the vesting or exercise provisions contained in the Agreement.

8.2 Change of Control Defined. A "Change of control" shall be deemed to have occurred upon any of the following events:

8.2.1 The consummation of any of the following transactions: any merger, reverse stock split, recapitalization or other business combination of the Company, with or into another corporation, or an acquisition of securities or assets by the Company, pursuant to which the Company is not the continuing or surviving corporation or pursuant to which shares of Common Stock would be converted into cash, securities or other property, other than a transaction in which the majority of the holders of Common Stock immediately prior to such transaction will own at least fifty percent (50%) of the total voting power of the then-outstanding securities of the surviving corporation immediately after such transaction; or

8.2.2 A transaction in which any person (as such term is defined in Sections 13(d)(3) and 14(d)(2) of the Exchange Act), corporation or other entity (other than the Company, or any profit-sharing, employee ownership or other employee benefit plan sponsored by the Company or any Subsidiary, or any trustee of or fiduciary with respect to any such plan when acting in such capacity, or any group comprised solely of such entities): (i) shall purchase any Common Stock (or securities convertible into Common Stock) for cash, securities or any other consideration pursuant to a tender offer or exchange offer, without the prior consent of the Board, or (ii) shall become the "beneficial owner" (as such term is defined in Rule 13d-3 under the Exchange Act), directly or indirectly (in one transaction or a series of transactions), of securities of the Company representing fifty percent (50%) or more of the total voting power of the then-outstanding securities of the Company ordinarily (and apart from the rights accruing under special circumstances) having the right to vote in the election of directors (calculated as provided in Rule 13d-3(d) in the case of rights to acquire the Company's securities); or

8.2.3 If, during any period of two consecutive years, individuals who at the beginning of such period constituted the entire Board and any new director whose election by the Board, or nomination for election by the Company's stockholders was approved by a vote of at least two-thirds of the directors then still in office who either were directors at the beginning of the period or whose election or nomination for election by the stockholders was previously so approved, cease for any reason to constitute a majority thereof.

8.3 General Waiver by Board. The Committee may, after grant of an award, accelerate the vesting of all or any part of any Stock Option, and/or waive any limitations or restrictions, if any, for all or any part of an award.

8.4 Acceleration Upon Termination of Employment. In the case of a Holder whose employment or affiliation with the Company or a Subsidiary is involuntarily terminated for any reason (other than for cause), the

Committee may, at its option and in its sole discretion, accelerate the vesting of all or any part of any award and/or waive, in whole or in part, any or all of the remaining deferral limitations or restrictions imposed hereunder or pursuant to the Agreement.

9. Amendments and Termination.

9.1 Amendments to Plan; Termination. The Board may at any time, and from time to time, amend any of the provisions of the Plan, and may at any time suspend or terminate the Plan; provided, however, that no such amendment shall be effective unless and until it has been duly approved by the stockholders of the outstanding shares of Common Stock if (i) such amendment materially increases the benefits accruing to participants under this Plan; (ii) such amendment materially increases the number of securities which may be issued under this Plan; (iii) such amendment materially modifies the requirements as to eligibility for participation in this Plan; or, (iv) the failure to obtain such approval would adversely affect the compliance of the Plan with the requirements of Rule 16b-3 under the Exchange Act, or with the requirements of any other applicable law, rule or regulation.

9.2 Amendments to Individual Awards. The Board may amend the terms of any award granted under the Plan; provided, however, that subject to Section 11 hereof, no such amendment may be made by the Board which in any material respect impairs the rights of the Holder without the Holder's consent.

10. Term of Plan.

10.1 Effective Date. The Plan shall be effective as of August 13, 1998 ("Effective Date"), subject to the approval of the Plan by the stockholders of the Company within one year after the Effective Date. Any awards granted under the Plan prior to such approval shall be effective when made (unless otherwise specified by the Committee at the time of grant) but shall be conditioned upon, and subject to, such approval of the Plan by the Company's stockholders and approval of the Company's application to list the shares of the Company's Common Stock covered by the Plan on the New York Stock Exchange (and no awards shall vest or otherwise become free of restrictions prior to such approvals).

10.2 Termination Date. No award shall be granted pursuant to the Plan on or after the tenth (10th) anniversary of the Effective Date, but awards granted prior to such tenth (10th) anniversary may extend beyond that date. The Plan shall terminate at such time as no further awards may be granted and all awards granted under the Plan are no longer outstanding.

11. Adjustment Upon Change of Shares. Subject to any required action by the stockholders of the Company, the number of shares of Common Stock for which Stock Options may thereafter be granted, and the number of shares of Common Stock then subject to Stock Options previously granted, and the price per share payable upon exercise of such Stock Option and the number of shares and exercise price relating to Stock Appreciation Rights, shall be proportionately adjusted for any increase or decrease in the number of issued shares of Common Stock of the Company resulting from a subdivision or consolidation of shares of Common Stock or the payment of a stock dividend (but only on the Common Stock) or any other increase or decrease in the number of shares of Common Stock effected without receipt of consideration by the Company.

11.1 If the Company is reorganized or consolidated or merged with another corporation, in which the Company is the non-surviving corporation, a Holder of an outstanding Stock Option and/or Stock Appreciation Right granted under this Plan shall be entitled (subject to the provisions of this Section 11) to receive options and/or stock appreciation rights covering shares of such reorganized, consolidated or merged corporation in the same proportion as granted to Holder prior to such reorganization, consolidation or merger at an equivalent exercise price, and subject to the same terms and conditions as this Plan. For purposes of the preceding sentence, the excess of the aggregate Fair Market Value of shares subject to the option immediately after the reorganization, consolidation or merger over the aggregate exercise price of such shares shall not be more than the excess of the aggregate Fair Market Value of all shares of Common Stock subject to the option or Stock Appreciation Right immediately before such reorganization, consolidation or merger over the aggregate exercise price of such shares of Common Stock, and the new stock option or stock appreciation right or assumption of the old Stock Option or old Stock Appreciation Right by any surviving corporation shall not give the Holder additional benefits which he did not have under the old Stock Option or Stock Appreciation Right.

11.2 To the extent that the foregoing adjustments relate to the shares of Common Stock of the Company, such adjustments shall be made by the Committee, whose determination in that respect shall be final, binding and conclusive, provided that each Incentive Stock Option granted pursuant to this Plan shall not be adjusted in a manner that causes the Incentive Stock Option to fail to continue to qualify as an incentive stock option within the meaning of Section 422 of the Code.

11.3 Except as expressly provided in this Section 11, the Holder shall have no rights by reason of any subdivision or consolidation of shares of stock of any class or the payment of any stock dividend or any other increase or decrease in the number of shares of stock of any class or by reason of any dissolution, liquidation, merger, consolidation, reorganization or spin-off of assets or stock of another corporation, and any issue by the Company of shares of stock of any class, or securities convertible into shares of stock of any class, shall not affect, and no adjustment by reason thereof shall be made with respect to, the number or price of shares of Common Stock subject to the Stock Option or the number or price of Stock Appreciation Rights granted under this Plan.

11.4 The grant of a Stock Option or Stock Appreciation Right pursuant to this Plan shall not affect in any way the right or power of the Company to make adjustments, reclassifications, reorganizations or changes of its capital or business structure or to merge or to consolidate or to dissolve, liquidate or sell, or transfer all or any part of its business or assets.

12. General Provisions.

12.1 Investment Representations. The Committee may require each person acquiring shares of Common Stock pursuant to an award under this Plan to represent to and agree with the Company in writing that the Holder is acquiring the shares for investment without a view to distribution thereof.

12.2 Additional Incentive Arrangements. Nothing contained in this Plan shall prevent the Board from adopting such other or additional incentive arrangements as it may deem desirable, including, but not limited to, the granting of Stock Options and the awarding of stock and cash otherwise than under this Plan; and such arrangements may be either generally applicable or applicable only in specific cases.

12.3 No Right of Employment. Nothing contained in this Plan or in any award hereunder shall be deemed to confer upon any employee of the Company or any Subsidiary any right to continued employment with the Company or any Subsidiary, nor shall it interfere in any way with the right of the Company or any Subsidiary to terminate the employment of any of its employees at any time.

12.4 Withholding Taxes. Not later than the date as of which an amount first becomes includible in the gross income of the Holder for federal income tax purposes with respect to any award under the Plan, the Holder shall pay to the Company, or make arrangements satisfactory to the Company regarding the payment of, any federal, state and local taxes of any kind required by law to be withheld or paid with respect to such amount. If permitted by the Board, tax withholding or payment obligations may be settled with Common Stock, including Common Stock that is part of the award that gives rise to the withholding requirement. The obligations of the Company under this Plan shall be conditional upon such payment or arrangements and the Company shall, to the extent permitted by law, have the right to deduct any such taxes from any payment of any kind otherwise due to the Holder from the Company.

12.5 Governing Law. This Plan and all awards made and actions taken thereunder shall be governed by and construed in accordance with the laws of the State of Delaware (without regard to choice of law provisions).

12.6 Other Benefit Plans. Any award granted under this Plan shall not be deemed compensation for purposes of computing benefits under any retirement plan of the Company or any Subsidiary and shall not affect any benefits under any other benefit plan now or subsequently in effect under which the availability or amount of benefits is related to the level of compensation (unless required by specific reference in any such other plan to awards under this Plan).

12.7 Employee Status. A leave of absence, unless otherwise determined by the Board prior to the commencement thereof, shall not be considered a termination of employment. Any awards granted under this Plan shall not be affected by any change of employment, so long as the Holder continues to be an employee of the Company or any Subsidiary.

12.8 Non-Transferability. Other than the transfer of a Stock Option or Stock Appreciation Right by will or by the laws of descent and distribution, no award under this Plan may be alienated, sold, assigned, hypothecated, pledged, exchanged, transferred, encumbered or charged, and any attempt to alienate, sell, assign, hypothecate, pledge, exchange, transfer, encumber or charge the same shall be void. No right or benefit hereunder shall in any manner be liable for or subject to the debts, contracts, liabilities or torts of the person entitled to such benefit. Unless otherwise provided in this Plan or the Agreement, any Stock Option or Stock Appreciation Right granted under this Plan is only exercisable during the lifetime of the Holder by the Holder or by his guardian or legal representative.

12.9 Applicable Laws. The obligations of the Company with respect to all awards under this Plan shall be subject to (i) all applicable laws, rules and regulations, including, without limitation, the requirements of all federal securities laws, rules and regulations and state securities and blue sky laws, rules and regulations, and such approvals by any governmental agencies as may be required, including, without limitation, the effectiveness of a registration statement under the Act, and (ii) the rules and regulations of any national securities exchange on which the Common Stock may be listed or the NASDAQ National Market System if the Common Stock is designated for quotation thereon.

12.10 Conflicts. If any of the terms or provisions of the Plan conflict with the requirements of Rule 16b-3 under the Exchange Act, or with the requirements of any other applicable law, rule or regulation, and/or with respect to Incentive Stock Options, Section 422 of the Code, then such terms or provisions shall be deemed inoperative to the extent they so conflict with the requirements of said Rule 16b-3, and/or with respect to Incentive Stock Options, Section 422 of the Code. With respect to Incentive Stock Options, if this Plan does not contain any provision required to be included herein under Section 422 of the Code, such provision shall be deemed to be incorporated herein with the same force and effect as if such provision had been set out at length herein.

12.11 Written Agreements. Each award granted under this Plan shall be confirmed by, and shall be subject to the terms of the Agreement approved by the Committee and executed by the Company and the Holder. The Committee may terminate any award made under this Plan if the Agreement relating thereto is not executed and returned to the Company within sixty (60) days after the Agreement has been delivered to the Holder for his or her execution.

12.12 Indemnification of Committee. In addition to such other rights of indemnification as they may have as directors or as members of the Committee, the members of the Committee shall be indemnified by the Company against the reasonable expenses, including attorneys' fees actually and necessarily incurred in connection with the defense of any action, suit or proceeding, or in connection with any appeal therein, to which they or any of them may be a party by reason of any action taken or failure to act under or in connection with the Plan or any award granted thereunder, and against all amounts paid by them in settlement thereof (provided such settlement is approved by independent legal counsel selected by the Company) or paid by them in satisfaction of a judgment in any such action, suit or proceeding, except in relation to matters as to which it shall be adjudged in such action, suit or proceeding that such Committee member is liable for negligence or misconduct in the performance of his duties; provided that within sixty (60) days after institution of any such action, suit or proceeding a Committee member shall in writing offer the Company the opportunity, at its own expense, to handle and defend the same.

12.13 Consideration for Common Stock. The Committee may not grant any awards under this Plan pursuant to which the Company will be required to issue any shares of Common Stock unless the Company will receive consideration for the shares of Common Stock sufficient under the laws of the State of Delaware so that such shares of Common Stock will be, when issued, validly issued and fully paid and nonassessable when issued.

12.14 Common Stock Certificates. All certificates for shares of Common Stock delivered under this Plan shall be subject to such stop-transfer orders and other restrictions as the Committee may deem advisable under the rules, regulations, and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Common Stock is then listed, any applicable federal or state securities law and any applicable corporate law, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate reference to such restrictions. Notwithstanding anything to the contrary contained herein, whenever certificates representing shares of Common Stock subject to an award are required to be delivered pursuant to the terms of this Plan, the Company may, in lieu of such delivery requirement, comply with the provisions of Section 158 of the Delaware General Corporation Law.

12.15 Unfunded Status of Plan. This Plan is intended to constitute an "unfunded" plan for incentive and deferred compensation. With respect to any payments not yet made to a Holder by the Company, nothing contained herein shall give any such Holder any rights that are greater than those of a general creditor of the Company.

March 12, 1999

Herman Meinders
3030 Northwest Expressway,
Suite 1407
Oklahoma City, OK 73112

Carlan K. Yates
14701 Coles Road
Edmond, OK 73013

Larry H. Lemon, Co-Trustee
Larry H. Lemon Living Trust
3840 Northwest 44th
Oklahoma City, OK 73112

Prime Financial Corporation
16 South Pennsylvania
Oklahoma City, OK 73107

LSB Industries, Inc.
16 South Pennsylvania
Oklahoma City, OK 73107

Gentlemen:

This letter will confirm that on Friday, March 12, 1999, Kestrel Aircraft Company ("Kestrel") voluntarily and peacefully surrendered possession of its assets, both tangible and intangible, more particularly described in the schedule attached hereto as Exhibit "A" (the "Collateral") to you as secured creditors.

Secondly, Kestrel hereby acknowledges and agrees that it is indebted to:

(1) Herman Meinders, for the sum of One Million Three Thousand Six Hundred Forty-Five and 83/100's Dollars ($1,003,645.83), the payment and performance of which is secured by a first priority security interest in an undivided 50% interest in the Collateral;

(2) Carlan K. Yates, for the sum of Two Hundred Fifty Thousand Nine Hundred Eleven and 46/100's Dollars ($250,911.46), the payment and performance of which is secured by a first priority security interest in an undivided 12.5% interest in the Collateral;

(3) Larry H. Lemon Living Trust, for the sum of Two Hundred Fifty Thousand Nine Hundred Eleven and 46/100's Dollars ($250,911.46), the payment and performance of which is secured by a first priority security interest in an undivided 12.5% interest in the Collateral;

(4) Prime Financial Corporation, for the sum of Five Hundred One Thousand Eighty Hundred Twenty-Two and 91/100's Dollars ($501,822.91), the payment and performance of which is secured by a first priority security interest in an undivided 25% interest in the Collateral; and

(5) LSB Industries, Inc. for the sum of Two Million Two Hundred Twenty-Five Thousand Nine Hundred Seventy-Two and 21/100's Dollars ($2,225,972.21), the payment and performance of which is secured by a junior, second priority security interest in the Collateral.

Kestrel hereby offers to renounce its rights in the Collateral pursuant to 12A O.S. Section 9-505(2) of Oklahoma's Uniform Commercial Code, and thereupon absolutely and unconditionally grant, bargain, sell, convey, transfer and set over to a nominee to be designated by you, all of its right, title and interest in and to the Collateral, subject only to certain purchase security interests granted to those secured parties with respect to specific items of equipment whose claims are identified on Exhibit "B" attached hereto, in full settlement and satisfaction of your respective claims as secured creditors.

Should you have any questions concerning any aspect of this proposal, please call.

KESTREL AIRCRAFT COMPANY, an
Oklahoma corporation

By: ______________________________________
Michael Humphreys, President

EXHIBIT "A"

(a) All cash, cash equivalents, accounts and accounts receivable of Kestrel and all other rights to payment of money held by Kestrel, now existing or hereafter arising;

(b) All inventory of Kestrel, now owned or hereafter acquired, and all additions, accessions and substitutions thereto and therefor, and all accessories, parts and equipment now or hereafter attached thereto or used in connection therewith, including (without limitation) any such inventory which is completed or is in the process of being completed;

(c) All goods, machinery, equipment, apparatus, work in progress, motor vehicles and airplanes of Kestrel and all other tangible personal property or every kind and description which is used in Kestrel's business operations or is owned by Kestrel;

(d) All contract rights of Kestrel;

(e) All general intangibles, chattel paper, securities, instruments, choses in action and causes of action of Kestrel and all other intangible personal property of Kestrel of every kind and nature, now existing or hereafter arising;

(f) All patents, trademarks, copyrights and other intellectual property rights (and all pending applications for any of the foregoing) now owned or hereafter acquired by Kestrel; and

(g) All other assets of Kestrel of any kind or nature.

EXHIBIT "B"

Schedule of Permitted Liens

	Creditor	Equipment Acquired With Purchase Money Financing
1)	Orix Credit Alliance, Inc.	Power MacIntosh Computer, Model #M2284LL-B; Apple Multi-Scan Monitor, Model #M2611-LL-A; Apple Tranceiver, Model #M04372-B; Insignia Software Package, Model #01705-1.0
2)	Advanta Leasing Corp.	Encad Cadjet Plotter 36"
3)	AT&T Capital Leasing Services, Inc.	Computer equipment and software described in Financing Statement No. 00208 filed on January 20, 1995 with the Oklahoma County Clerk, Oklahoma
4)	Clark Credit Corporation	1 used Clark Model C-500-30 LPG lift truck, S/N 235-161-5850
5)	Clark Credit Corporation	1 1995 Komatsu Model FG-15C, LPG powered, pneumatic tire lift truck, S/N 313075A
6)	AT&T Capital Leasing Services, Inc.	Gateway P5-90 Best Buy Computers 2565839 through 2565842
7)	Community Bank & Trust Company	Computer equipment, copier and software described in Financing Statement No. 065314 filed on December 15, 1995 with the Oklahoma County Clerk, Oklahoma
8)	LSB Industries, Inc.	Office work station partitions for 14 work stations
9)	MIS Systems Corporation	Equipment, computers and software described in Financing Statement No. 006059 filed on February 7, 1997 with the Oklahoma County Clerk, Oklahoma
10)	AT&T Capital Leasing Services, Inc.	OCE 7065 Copier SN 705509204

The CIT Group/
Equipment Financing
650 CIT Drive
P. O. Box 490
Livingston, NJ 07038-0480

April 13, 1999

THE
CIT
GROUP

Mr. Jim Jones
Vice President
LSB Industries
16 South Pennsylvania Avenue
Oklahoma City, Oklahoma 73107

Dear Mr. Jones

Reference is made to (a) that certain Loan Agreement dated October 31, 1994, as amended, (the "Agreement") between DSN Corporation, an Oklahoma corporation ("Debtor"), and THE CIT GROUP/EQUIPMENT FINANCING, INC., a New York corporation ("CIT"), and (b) the defined terms within. Debtor has advised CIT that LSB Industries (LSB), a guarantor of Debtor's obligations to CIT was not in compliance with:

Section 6.10 to the Agreement, in that as of December 31, 1998, LSB did not maintain a tangible net worth of $32,674,000.00. Further, LSB did not maintain a leverage requirement of 4.90x.

Debtor has requested that notwithstanding anything to the contrary in the Agreement, that CIT waive the above instances of non-compliance through June 30, 2000.

CIT hereby waives, as of this date, the above instances of noncompliance, provided that such waiver is subject to the following conditions:

(1) that this waiver is strictly limited to the specific covenants under section 6.10 of the Agreement, as amended, set forth above and is strictly limited only to such instances of noncompliance through and including June 30, 2000

(2) that Debtor pay a fee in the amount of $40,000.00 within 5 business days of the above date to cover the waiver

(3) CIT agrees to reset the covenants within 30 days of the date of this waiver.

Sincerely,
The CIT Group Equipment Financing, Inc.

By: /s/ Anthony Joseph

Title: Vice President

Acknowledged and Agreed:

DSN Corporation

By: /s/ Tony M. Shelby

Title: V.P.

LSB Industries

By: /s/ Tony M. Shelby

Title: S.V.P.

An affiliate of
The Dai-ichi Kagyo Bank, Limited

LSB INDUSTRIES, INC.
SUBSIDIARY LISTING
Revised February 26, 1999

LSB INDUSTRIES, INC. (Direct subsidiaries in bold italics)

- Prime Financial Corporation
    - Tower IV Corporation (f/k/a LSB Leasing Corp.)
    - Northwest Capital Corporation
    - Northwest Energy Enterprises, Inc.
    - Tower Land Development Corp.
    - ClimaChem, Inc. (5% stock ownership)

- LSB Holdings, Inc.
    - LSB-Europa Limited
    - Equipos Climatec S.A. de C.V. (97% stock ownership)
    - LSB Indonesia Corporation (f/k/a LSB Corporation)
    - Summit Machine Tool Inc. Corp.
        - Saffron Corporation
        - Explosives Equipment Corp.
            - Clipmate Corporation (20% held by Waldock and Starrett)
        - Equipos Climatec S.A. de C.V. (1% stock ownership)
    - LSB International Corp.
        - Equipos Climatec S.A. de C.V. (1% stock ownership)
    - L&S Automotive Technologies, Inc. (f/k/a L&S Automotive Products Co.)
    - Climatex, Inc.
    - LSB Financial Corp.
        - Equipos Climatec S.A. de C.V. (1% stock ownership)
    - Aerobit Industries, Limited (7.98% held by Horovitz and Landsome)
    - Climate Master International Limited
    - ROL-BIT Ltd. (5% held by Horovitz)

- ClimateCraft Technologies, Inc.

INDUSTRIAL PRODUCTS BUSINESS

- Summit Machine Tool Manufacturing Corp.
- Hercules Energy Mfg. Corporation
    - Morey Machinery Manufacturing Corporation (f/k/a Fertilizer Equipment Corp.) (10% held by Jonathon Morey)

ENVIRONMENTAL/CHEMICAL BUSINESS

- ClimaChem, Inc. (95% stock ownership)
  - Northwest Financial Corporation
  - Climate Mate, Inc.
  - The Environmental Group International Limited
  - LSB Chemical Corp.
    - Total Energy Systems Limited
      - Total Energy Systems (NZ) Limited
      - T.E.S. Mining Services Pty. Ltd.
      - Total Energy Systems (International) Pty Ltd
    - El Dorado Chemical Company
      - Slurry Explosive Corporation
    - El Dorado Nitrogen Company (f/k/a LSB Nitrogen Corporation, f/k/a LSB Import Corp.)
    - DSN Corporation
    - Universal Tech Corporation
  - The Environmental Group, Inc.
  - International Environmental Corporation
  - Climate Master, Inc.
  - CHP Corporation
    - Koax Corp.
  - APR Corporation
  - ClimateCraft, Inc. (f/k/a Summit Machine Tool Systems, Inc.)
  - ACP International Limited (f/k/a ACP Manufacturing Corp.)
  - ThermalClime, Inc. (f/k/a LSB South America Corporation)

AUTOMOTIVE PRODUCTS BUSINESS

- LSA Technologies Inc.
  - L&S Automotive Products Co. [DE]
    - L&S Bearing Co. (f/k/a L&S Automotive Products Co., f/k/a LSB Bearing Corp.)
      - International Bearings, Inc.
    - LSB Extrusion Co.
    - Rotex Corporation
    - Tribonetics Corporation

Consent of Independent Auditors

We consent to the incorporation by reference in the Registration Statement (Form S-8, No. 33-8302) pertaining to the 1981 and 1986 Incentive Stock Option Plans, the Registration Statement (Form S-8 No. 333-58225) pertaining to the 1993 Stock Option and Incentive Plan, the Registration Statements (Forms S-8 No. 333-62831, No. 333-62835, No. 333-62839, No. 333-62843, and No. 333-62841) pertaining to the registration of an aggregate of 225,000 shares of common stock pursuant to certain Non-qualified Stock Option Agreements for various employees, and the Registration Statement (Form S-3, No. 33-69800) and the related Prospectuses of LSB Industries, Inc. of our report dated February 19, 1999, except for paragraphs (A) and (C) of Note 5 and Note 14, as to which the date is April 14, 1999 with respect to the consolidated financial statements and schedule of LSB Industries, Inc. included in the Annual Report (Form 10-K) for the year ended December 31, 1998.

/s/ Ernst & Young LLP

ERNST & YOUNG LLP

Oklahoma City, Oklahoma
April 14, 1999

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