UNIFI INC
Form 10-Q
February 02, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended December 24, 2006

OR

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

For the transition period from __________to __________

Commission File Number: 1-10542

UNIFI, INC.

(Exact name of registrant as specified in its charter)

New York	**11-2165495**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
P.O. Box 19109 7201 West Friendly Avenue Greensboro, NC	**27419**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: **(336) 294-4410**

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer þ Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes o Noþ

The number of shares outstanding of the issuer s common stock, par value $.10 per share, as of February 1, 2007 was 60,541,800.

UNIFI, INC.
Form 10-Q for the Quarterly Period Ended December 24, 2006

INDEX

Table of Contents

Part. 1 Financial Information
Item. 1 Financial Statements

UNIFI, INC.
Condensed Consolidated Balance Sheets

	December 24, 2006 (Unaudited)	June 25, 2006
	(Amounts in thousands)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 35,612	$ 35,317
Receivables, net	77,486	93,236
Inventories	115,386	116,018
Deferred income taxes	11,982	11,739
Assets held for sale	15,419	15,419
Other current assets	11,287	9,229
Total current assets	267,172	280,958
Property, plant and equipment	911,953	916,337
Less accumulated depreciation	(692,492)	(676,641)
	219,461	239,696
Investments in unconsolidated affiliates	184,210	190,217
Other noncurrent assets	22,766	21,766
Total assets	$ 693,609	$ 732,637
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 60,518	$ 68,916
Accrued expenses	18,569	23,869
Income taxes payable	373	2,303
Current maturities of long-term debt and other current liabilities	8,056	6,330
Total current liabilities	87,516	101,418
Long-term debt and other liabilities	203,691	202,405
Deferred income taxes	44,159	45,861
Commitments and contingencies Shareholders equity:		
Common stock	5,220	5,220
Capital in excess of par value	2,167	929
Retained earnings	354,487	382,082
Accumulated other comprehensive loss	(3,631)	(5,278)
	358,243	382,953

Total liabilities and shareholders equity	$ 693,609	$ 732,637

See accompanying notes to condensed consolidated financial statements.

Table of Contents

UNIFI, INC.
Condensed Consolidated Statements of Operations
(Unaudited)

	For the Quarters Ended		For the Six-Months Ended	
	Dec. 24, 2006	Dec. 25, 2005	Dec. 24, 2006	Dec. 25, 2005
	(Amounts in thousands, except per share data)			
Net sales	$ 156,895	$ 191,117	$ 326,839	$ 374,219
Cost of sales	154,275	181,747	315,179	356,446
Selling, general & administrative expenses	10,388	10,461	21,677	20,948
Provision (recovery) for bad debts	(1,012)	604	598	1,131
Interest expense	6,111	4,681	12,176	9,457
Interest income	(1,066)	(2,189)	(1,510)	(3,470)
Other (income) expense, net	236	303	(243)	(549)
Equity in (earnings) losses of unconsolidated affiliates	2,876	(18)	4,825	(1,842)
Write down of long-lived assets	2,002		3,202	1,500
Restructuring charges				29
Loss from continuing operations before income taxes and extraordinary item	(16,915)	(4,472)	(29,065)	(9,431)
Benefit for income taxes	(540)	(1,079)	(1,673)	(1,231)
Loss from continuing operations before extraordinary item	(16,375)	(3,393)	(27,392)	(8,200)
Income (loss) from discontinued operations net of tax	(167)	(583)	(203)	1,346
Extraordinary gain net of taxes of $0		208		
Net loss	$ (16,542)	$ (3,768)	$ (27,595)	$ (6,854)
Earnings (losses) per common share (basic and diluted):				
Net loss continuing operations	$ (.32)	$ (.06)	$ (.53)	$ (.16)
Net income (loss) discontinued operations		(.01)		.03
Extraordinary gain				
Net loss basic and diluted	$ (.32)	$ (.07)	$ (.53)	$ (.13)
Weighted average outstanding shares of common stock (basic and diluted)	52,198	52,127	52,198	52,127

See accompanying notes to condensed consolidated financial statements.

Table of Contents

UNIFI, INC.
Condensed Consolidated Statements of Cash Flows
(Unaudited) (Amounts in thousands)

	For the Six-Months Ended	
	December 24, 2006	December 25, 2005
Cash and cash equivalents at the beginning of period	$ 35,317	$ 105,621
Operating activities:		
Net loss	(27,595)	(6,854)
Adjustments to reconcile net loss to net cash provided by continuing operating activities:		
(Income) loss from discontinued operations	203	(1,346)
Net (earnings) losses of unconsolidated equity affiliates, net of distributions	4,825	288
Depreciation	21,449	24,688
Amortization	557	642
Stock based compensation	1,238	289
Net (gain) loss on asset sales	241	(365)
Non-cash write down of long-lived assets	3,202	1,500
Non-cash portion of restructuring charges		29
Deferred income tax	(1,945)	(2,533)
Provision for bad debt	598	1,131
Split dollar life insurance proceeds, net		983
Other	20	(1,275)
Change in assets and liabilities, excluding effects of acquisitions and foreign currency adjustments	1,357	443
Net cash provided by continuing operating activities	4,150	17,620
Investing activities:		
Capital expenditures	(3,341)	(7,614)
Acquisition	(393)	(30,388)
Investment of foreign restricted assets		158
Collection of notes receivable	734	236
Change in restricted cash		2,766
Proceeds from sale of capital assets	30	2,376
Return of capital from equity affiliates	229	
Split dollar life insurance premiums	(166)	
Other	(362)	(210)
Net cash used in investing activities	(3,269)	(32,676)
Financing activities:		
Payment of long-term debt	(290)	(24,407)
Other	(309)	40
Net cash used in financing activities	(599)	(24,367)

Cash flows of discontinued operations:		
Operating cash flow	(50)	(4,640)
Investing cash flow		23,062
Net cash provided by (used in) discontinued operations	(50)	18,422
Effect of exchange rate changes on cash and cash equivalents	63	399
Net increase (decrease) in cash and cash equivalents	295	(20,602)
Cash and cash equivalents at end of period	$ 35,612	$ 85,019

See accompanying notes to condensed consolidated financial statements.

Table of Contents

UNIFI, INC.
Notes to Condensed Consolidated Financial Statements

1. Basis of Presentation

The Condensed Consolidated Balance Sheet at June 25, 2006, has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by U.S. generally accepted accounting principles (U.S. GAAP) for complete financial statements. Except as noted with respect to the balance sheet at June 25, 2006, the information furnished is unaudited and reflects all adjustments which are, in the opinion of management, necessary to present fairly the financial position at December 24, 2006, and the results of operations and cash flows for the periods ended December 24, 2006 and December 25, 2005. Such adjustments consisted of normal recurring items necessary for fair presentation in conformity with U.S. GAAP. Preparing financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from these estimates. Interim results are not necessarily indicative of results for a full year. The information included in this Form 10-Q should be read in conjunction with Management s Discussion and Analysis of Financial Condition and Results of Operations and the financial statements and notes thereto included in the Company s Form 10-K for the fiscal year ended June 25, 2006. Certain prior year amounts have been reclassified to conform to the current presentation.

The significant accounting policies followed by the Company are presented on pages 57 to 62 of the Company s Annual Report on Form 10-K for the fiscal year ended June 25, 2006. These policies have not changed from the disclosure in that report.

2. Inventories

Inventories were comprised of the following (amounts in thousands):

	December 24, 2006	June 25, 2006
Raw materials and supplies	$ 52,210	$ 48,594
Work in process	6,204	10,144
Finished goods	56,972	57,280
	$ 115,386	$ 116,018

3. Accrued Expenses

Accrued expenses were comprised of the following (amounts in thousands):

	December 24, 2006	June 25, 2006
Payroll and fringe benefits	$ 6,785	$ 11,112
Severance	216	576
Interest	2,608	1,984
Property taxes	48	1,722
Accrued utilities	4,331	3,225
Other	4,581	5,250

	$	18,569	$ 23,869

6

Table of Contents

4. Income Taxes

The Company s income tax benefit for the quarter ended December 24, 2006 resulted in an effective tax rate of 3.0% compared to a 24.1% benefit for the quarter ended December 25, 2005. The Company s income tax benefit for the year-to-date period ended December 24, 2006 resulted in an effective tax rate of 5.8% compared to a 13.0% benefit for the year-to-date period ended December 25, 2005. The primary differences between the Company s income tax benefit and the U.S. statutory rate for the quarter and year-to-date period ended December 24, 2006 were due to losses from certain foreign operations taxed at a lower effective rate and increases in the valuation allowance for North Carolina income tax credit carryforwards and capital losses.

Deferred income taxes have been provided to account for the temporary differences between financial statement carrying amounts and the tax basis of existing assets and liabilities. The Company has established a valuation allowance against deferred tax assets for North Carolina income tax credit carryforwards and capital losses. The valuation allowance had a net increase of $5.1 million for both the quarter and year-to-date period ended December 24, 2006 compared to increases of $0.1 million and $0.4 million for the quarter and year-to-date period ended December 25, 2005, respectively. The increases for the quarter and year-to-date period ended December 24, 2006 resulted from lower estimates of future utilization of North Carolina income tax credit carryforwards as well as a complete offset of deductible temporary differences with respect to certain capital losses.

5. Comprehensive Income/Loss

Comprehensive losses amounted to $15.2 million and $25.9 million for the second quarter and year-to-date periods of fiscal year 2007, respectively, compared to a comprehensive loss of $7.1 million for the second quarter and comprehensive income of $1.0 million for the year-to-date periods of fiscal year 2006. Comprehensive losses were comprised of net losses of $16.5 million and $27.6 million for the current second quarter and year-to-date periods of fiscal year 2007, respectively, and foreign translation gains of $1.3 million and $1.7 million, respectively. Comparatively, comprehensive income and loss for the corresponding periods in the prior year were derived from net losses of $3.7 million and $6.8 million, and foreign translation losses of $3.4 million and gains of $7.8 million. The Company does not provide income taxes on the impact of currency translations as earnings from foreign subsidiaries are deemed to be permanently invested.

6. Recent Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48) which is an interpretation of Statement of Financial Accounting Standards (SFAS) No. 109 Accounting for Income Taxes. The pronouncement creates a single model to address accounting for uncertainty in tax positions. FIN 48 prescribes a minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. FIN 48 also provides guidance on derecognition, measurement, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company will adopt FIN 48 as of the first day of fiscal year 2008 and it has not determined the impact of FIN 48 on its results of operations and financial condition.

In September 2006, the FASB issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans. SFAS No. 158 amends SFAS No. 87, Employers Accounting for Pensions, SFAS No. 88, Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits, SFAS No. 106, Employers Accounting for Postretirement Benefits Other than Pensions and SFAS No. 132, Employers Disclosures about Pensions and Other Postretirement Benefits. The amendments retain most of the existing measurement and disclosure guidance and will not change the amounts recognized in the

Company s statements of operations. SFAS No.

Table of Contents

158 requires companies to recognize a net asset or liability with an offset to equity relating to post retirement obligations. This aspect of SFAS No. 158 is effective for fiscal years ending after December 15, 2006. The Company currently does not expect that SFAS No. 158 will have a material effect on its consolidated balance sheet.

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements. This new standard provides guidance for measuring the fair value of assets and liabilities and is intended to provide increased consistency in how fair value determinations are made under various existing accounting standards. SFAS No. 157 also expands financial statement disclosure requirements about a company s use of fair value measurements, including the effect of such measures on earnings. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. While the Company is currently evaluating the provisions of SFAS No. 157 it has not determined the impact it will have on its results of operations or financial condition.

7. Segment Disclosures

The following is the Company s selected segment information for the quarters and six-month periods ended December 24, 2006 and December 25, 2005 (amounts in thousands):

	Polyester	Nylon	Total
Quarter ended December 24, 2006:			
Net sales to external customers	$118,507	$ 38,388	$156,895
Intersegment net sales	1,485	1,268	2,753
Write down of long-lived assets	2,002		2,002
Segment operating loss	(8,940)	(830)	(9,770)
Total assets	337,251	119,497	456,748
Quarter ended December 25, 2005:			
Net sales to external customers	$146,789	$ 44,328	$191,117
Intersegment net sales	1,076	1,227	2,303
Segment operating loss	(279)	(812)	(1,091)
Total assets	375,716	134,900	510,616

The following table represents reconciliations from segment data to consolidated reporting data (amounts in thousands):

	For the Quarters Ended	
	December 24, 2006	December 25, 2005
Reconciliation of segment operating loss to net loss from continuing operations before income taxes and extraordinary item:		
Reportable segments operating loss	$ (9,770)	$ (1,091)
Provision (recovery) for bad debts	(1,012)	604
Interest expense, net	5,045	2,492
Other (income) expense, net	236	303
Equity in (earnings) losses of unconsolidated affiliates	2,876	(18)
Loss from continuing operations before income taxes and extraordinary item	$ (16,915)	$ (4,472)

Table of Contents

	Polyester	Nylon	Total
Six-Months ended December 24, 2006:			
Net sales to external customers	$248,978	$77,861	$326,839
Intersegment net sales	3,914	3,096	7,010
Write down of long-lived assets	2,002		2,002
Segment operating loss	(10,619)	(1,400)	(12,019)
Six-Months ended December 25, 2005:			
Net sales to external customers	$280,957	$93,262	$374,219
Intersegment net sales	2,756	2,406	5,162
Write down of long-lived assets		1,500	1,500
Restructuring charges (recovery)	47	(18)	29
Segment operating loss	(1,475)	(3,229)	(4,704)

The following table represents reconciliations from segment data to consolidated reporting data (amounts in thousands):

	For the Six-Months Ended	
	December 24, 2006	December 25, 2005
Reconciliation of segment operating loss to net loss from continuing operations before income taxes and extraordinary item:		
Reportable segments operating loss	$ (12,019)	$ (4,704)
Provision for bad debts	598	1,131
Interest expense, net	10,666	5,987
Other (income) expense, net	(243)	(549)
Equity in (earnings) losses of unconsolidated affiliates	4,825	(1,842)
Write down of long-lived assets	1,200	
Loss from continuing operations before income taxes and extraordinary item	$ (29,065)	$ (9,431)

For purposes of internal management reporting, segment operating loss represents net sales less cost of sales and allocated selling, general and administrative expenses. Certain indirect manufacturing and selling, general and administrative costs are allocated to the operating segments based on activity drivers relevant to the respective costs. Intersegment sales of the Company s polyester partially orientated yarn (POY) business are recorded at market value whereas all other intersegment sales are recorded at cost.

The primary differences between the segmented financial information of the operating segment as reported to management and the Company s consolidated reporting relate to intersegment sales of yarn and the associated fiber costs, the provision for bad debts, an d certain unallocated selling, general and administrative expenses.

Fiber costs of the Company s domestic operating divisions are valued on a standard cost basis, which approximates first-in, first-out accounting. For those components of inventory valued utilizing the last-in, first-out (LIFO) method, an adjustment is made at the segment level to record the difference between standard cost and LIFO. Segment operating loss excluded the recovery for bad debts of $1.0 million and a provision of $0.6 million for the current and prior year second quarter periods, respectively, and a provision of $0.6 million and $1.1 million for the current and prior year-to-date periods, respectively.

The total assets for the polyester segment decreased from $359.2 million at June 25, 2006 to $337.3 million at December 24, 2006 due primarily to decreases in accounts receivable, fixed assets, inventory, and deferred taxes of $11.5 million, $10.2 million, $2.3 million, and $0.1 million, respectively. These decreases were offset by increases in other current assets, other assets, and cash of $1.2 million, $0.9 million, and $0.1 million, respectively. The total assets for the nylon segment decreased from $128.2 million at June 25, 2006 to $119.5 million at December 24, 2006 due primarily to decreases in fixed assets and accounts receivable of $6.9 million and $3.9 million, respectively. These decreases were offset by increases in inventory, cash, deferred income taxes, and other current assets of $1.5 million, $0.2 million, $0.2 million, and $0.2 million, respectively.

8. Stock-Based Compensation

During the fourth quarter of fiscal year 2006, the Board authorized the issuance of one hundred fifty thousand stock options from the 1999 Long-Term Incentive Plan. During the first half of fiscal year 2005, the Board authorized the issuance of approximately 2.1 million stock options from the 1999 Long-Term Incentive Plan to certain key employees. The stock options granted in fiscal years 2006 and 2005 vest in three equal installments: the first one-third at the time of grant, the next one-third on the first anniversary of the grant and the final one-third on the second anniversary of the grant.

During the first quarter of fiscal year 2007, the Board authorized the issuance of approximately 1.1 million stock options from the 1999 Long-Term Incentive Plan to certain key employees. With the exception of the immediate vesting of three hundred thousand stock options granted to the CEO, the remaining stock options vests in three equal installments: the first one-third at the time of grant, the next one-third on the first anniversary of the grant and the final one-third on the second anniversary of the grant. As a result of these grants, the Company incurred $0.2 million in the second quarter and $1.2 million for the year-to-date period in stock-based compensation charges which were recorded as selling, general and administrative expense with the offset to additional paid-in-capital.

9. Derivative Financial Instruments

The Company accounts for derivative contracts and hedging activities under Statement of Financial Accounting Standards No. 133, Accounting for Derivative Instruments and Hedging Activities (SFAS No. 133) which requires all derivatives to be recorded on the balance sheet at fair value. If the derivative is a hedge, changes in the fair value of derivatives are either offset against the change in fair value of the hedged assets, liabilities or firm commitments through earnings. The Company does not enter into derivative financial instruments for trading purposes nor is it a party to any leveraged financial instruments.

The Company conducts its business in various foreign currencies. As a result, it is subject to the transaction exposure that arises from foreign exchange rate movements between the dates that foreign currency transactions are recorded (export sales and purchase commitments) and the dates they are settled (cash receipts and cash disbursements in foreign currencies). The Company utilizes some natural hedging to mitigate these transaction exposures. The Company also enters into foreign currency forward contracts for the purchase and sale of European, Canadian, Brazilian and other currencies to hedge balance sheet and income statement currency exposures. These contracts are principally entered into for the purchase of inventory and equipment and the sale of Company products into export markets. Counterparties for these instruments are major financial institutions.

Currency forward contracts are entered into to hedge exposure for sales in foreign currencies based on specific sales orders with customers or for anticipated sales activity for a future time period. Generally, 50% of the sales value of these orders is covered by forward contracts. Maturity dates of the forward contracts attempt to match anticipated receivable collections. The Company marks the outstanding accounts receivable and forward contracts to market at month end and any realized and unrealized gains or losses are recorded as other income and expense. The Company also enters currency forward contracts for committed or anticipated equipment and inventory purchases. Generally, 50% of the asset cost is covered by forward contracts although 10