UNIFI INC
Form 10-Q
May 04, 2007

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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 March 25, 2007

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 Exchange Act). Yeso No þ

The number of shares outstanding of the issuer s common stock, par value $.10 per share, as of May 3, 2007 was 60,541,800.

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Part. 1 Financial Information
Item. 1 Financial Statements

UNIFI, INC.
Condensed Consolidated Balance Sheets

	March 25, 2007 (Unaudited)	June 25, 2006
	(Amounts in thousands)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 26,780	$ 35,317
Receivables, net	99,442	93,236
Inventories	129,059	116,018
Deferred income taxes	14,060	11,739
Assets held for sale	7,346	17,418
Restricted cash	1,000	
Other current assets	10,360	9,229
Total current assets	288,047	282,957
Property, plant and equipment	923,765	914,283
Less accumulated depreciation	(694,958)	(676,586)
	228,807	237,697
Investments in unconsolidated affiliates	184,249	190,217
Intangible assets, net	31,450	
Other noncurrent assets	21,699	21,766
Total assets	$ 754,252	$ 732,637
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 59,922	$ 68,916
Accrued expenses	27,897	23,869
Income taxes payable	503	2,303
Current maturities of long-term debt and other current liabilities	9,047	6,330
Total current liabilities	97,369	101,418
Long-term debt and other liabilities	243,593	202,405
Deferred income taxes	43,328	45,861
Commitments and contingencies		
Shareholders equity:		
Common stock	6,054	5,220
Capital in excess of par value	23,478	929
Retained earnings	341,268	382,082

Accumulated other comprehensive loss	(838)	(5,278)
	369,962	382,953
Total liabilities and shareholders equity	$ 754,252	$ 732,637

See accompanying notes to condensed consolidated financial statements.

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

	For the Quarters Ended		For the Nine-Months Ended	
	Mar. 25, 2007	Mar. 26, 2006	Mar. 25, 2007	Mar. 26, 2006
	(Amounts in thousands, except per share data)			
Net sales	$ 178,202	$ 181,398	$ 505,041	$ 555,617
Cost of sales	164,752	168,261	479,931	524,707
Selling, general & administrative expenses	11,177	10,184	32,854	31,132
Provision for bad debts	2,274	218	2,872	1,349
Interest expense	6,610	4,606	18,786	14,063
Interest income	(707)	(1,542)	(2,217)	(5,012)
Other (income) expense, net	(2,462)	(589)	(2,705)	(1,138)
Equity in (earnings) losses of unconsolidated affiliates	(352)	564	4,473	(1,278)
Write down of long-lived assets	12,870	815	16,072	2,315
Restructuring charges				29
Loss from continuing operations before income taxes	(15,960)	(1,119)	(45,025)	(10,550)
Provision (benefit) for income taxes	(2,075)	208	(3,748)	(1,023)
Loss from continuing operations	(13,885)	(1,327)	(41,277)	(9,527)
Income (loss) from discontinued operations - net of tax	666	(790)	463	556
Net loss	$ (13,219)	$ (2,117)	$ (40,814)	$ (8,971)
Earnings (losses) per common share (basic and diluted):				
Net loss continuing operations	$ (.23)	$ (.03)	$ (.75)	$ (.18)
Net income (loss) discontinued operations	.01	(.01)		.01
Net loss basic and diluted	$ (.22)	$ (.04)	$ (.75)	$ (.17)
Weighted average outstanding shares of common stock (basic and diluted)	59,803	52,177	54,733	52,144

See accompanying notes to condensed consolidated financial statements.

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

	For the Nine-Months Ended March 25, 2007	March 26, 2006
Cash and cash equivalents at the beginning of period	$ 35,317	$ 105,621
Operating activities:		
Net loss	(40,814)	(8,971)
Adjustments to reconcile net loss to net cash provided by continuing operating activities:		
(Income) loss from discontinued operations	(463)	(556)
Net (earnings) losses of unconsolidated equity affiliates, net of distributions	4,473	850
Depreciation	31,701	36,911
Amortization	1,967	962
Stock based compensation	1,433	421
Net (gain) loss on asset sales	(1,593)	(180)
Non-cash write down of long-lived assets	16,072	2,315
Non-cash portion of restructuring charges		29
Deferred income tax	(5,342)	(3,797)
Provision for bad debt	2,872	1,349
Split dollar life insurance proceeds, net	1,761	1,661
Other	93	(44)
Change in assets and liabilities, excluding effects of acquisitions and foreign currency adjustments	(15,771)	(7,531)
Net cash provided by (used in) continuing operating activities	(3,611)	23,419
Investing activities:		
Capital expenditures	(5,502)	(9,767)
Acquisitions	(42,831)	(30,188)
Investment of foreign restricted assets		171
Collection of notes receivable	766	
Change in restricted cash	(1,000)	2,766
Proceeds from sale of capital assets	2,399	2,395
Return of capital from equity affiliates	229	
Split dollar life insurance premiums	(217)	(217)
Other	(60)	155
Net cash used in investing activities	(46,216)	(34,685)
Financing activities:		
Payment of long-term debt		(24,407)
Net borrowings of long-term debt	40,000	
Other	(1,168)	277
Net cash provided by (used in) financing activities	38,832	(24,130)

Cash flows of discontinued operations:		
Operating cash flow	463	(9,259)
Investing cash flow		25,987
Net cash provided by discontinued operations	463	16,728
Effect of exchange rate changes on cash and cash equivalents	1,995	1,470
Net decrease in cash and cash equivalents	(8,537)	(17,198)
Cash and cash equivalents at end of period	$ 26,780	$ 88,423

See accompanying notes to condensed consolidated financial statements.

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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 March 25, 2007, and the results of operations and cash flows for the periods ended March 25, 2007 and March 26, 2006. 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):

	March 25, 2007	June 25, 2006
Raw materials and supplies	$ 52,189	$ 48,594
Work in process	7,781	10,144
Finished goods	69,089	57,280
	$ 129,059	$ 116,018

3. Accrued Expenses

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

	March 25, 2007	June 25, 2006
Payroll and fringe benefits	$ 9,069	$ 11,112
Workers compensation	2,170	2,269
Severance	1,102	576
Interest	8,169	1,984
Property taxes	869	1,722
Accrued utilities	4,140	3,225
Other	2,378	2,981
	$ 27,897	$ 23,869

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4. Income Taxes

The Company s income tax benefit for the quarter ended March 25, 2007 resulted in an effective tax rate of 13.0% compared to an 18.6% income tax expense for the quarter ended March 26, 2006. The Company s income tax benefit for the year-to-date period ended March 25, 2007 resulted in an effective tax rate of 8.3% compared to a 9.7% benefit for the year-to-date period ended March 26, 2006. The primary differences between the Company s income tax benefit and the U.S. statutory rate for the quarter and year-to-date periods ended March 25, 2007 are due to losses from certain foreign operations taxed at a lower effective rate and an increase in the valuation allowance for 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 net increases of $2.9 million and $8.0 million for the quarter and year-to-date periods ended March 25, 2007, respectively, compared to increases of $0.0 million and $0.4 million for the quarter and year-to-date periods ended March 26, 2006, respectively. The increases for the quarter and year-to-date periods ended March 25, 2007 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 $10.4 million and $36.4 million for the third quarter and year-to-date periods of fiscal year 2007, respectively, compared to a comprehensive income of $2.9 million and $3.9 million for the third quarter and year-to-date periods of fiscal year 2006. Comprehensive losses were comprised of net losses of $13.2 million and $40.8 million for the third quarter and year-to-date periods of fiscal year 2007, respectively, and foreign translation gains of $2.8 million and $4.4 million, respectively. Comprehensive income for the corresponding periods in the prior year was derived from net losses of $2.1 million and $9.0 million, and foreign translation gains of $5.0 million and $12.9 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 February 2007, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 159, Fair Value Option for Financial Assets and Financials Liabilities-Including an Amendment to FASB Statement No. 115 that expands the use of fair value measurement of various financial instruments and other items. This statement permits entities the option to record certain financial assets and liabilities, such as firm commitments, non-financial insurance contracts and warranties, and host financial instruments at fair value. Generally, the fair value option may be applied instrument by instrument and is irrevocable once elected. The unrealized gains and losses on elected items would be recorded as earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007. While the Company is currently evaluating the provisions of SFAS No. 159, it has not determined if it will make any elections for fair value reporting of its assets.

In June 2006, the FASB issued Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48) which is an interpretation of 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. 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 ended 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 nine-month periods ended March 25, 2007 and March 26, 2006 (amounts in thousands):

	Polyester	Nylon	Total
Quarter ended March 25, 2007:			
Net sales to external customers	$138,167	$ 40,035	$178,202
Intersegment net sales	1,421	587	2,008
Write down of long-lived assets	4,927	7,943	12,870
Segment operating loss	(3,740)	(6,857)	(10,597)
Total assets	415,465	118,110	533,575
Quarter ended March 26, 2006:			
Net sales to external customers	$141,626	$ 39,772	$181,398
Intersegment net sales	1,346	1,984	3,330
Write down of long-lived assets		815	815
Segment operating income (loss)	3,977	(1,839)	2,138
Total assets	375,025	134,509	509,534

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

	For the Quarters Ended	
	March 25, 2007	March 26, 2006
Reconciliation of segment operating income (loss) to net loss from continuing operations before income taxes:		
Reportable segments operating income (loss)	$ (10,597)	$ 2,138
Provision for bad debts	2,274	218
Interest expense, net	5,903	3,064
Other (income) expense, net	(2,462)	(589)
Equity in (earnings) losses of unconsolidated affiliates	(352)	564
Loss from continuing operations before income taxes	$ (15,960)	$ (1,119)

	Polyester	Nylon	Total
Nine-Months ended March 25, 2007:			
Net sales to external customers	$387,145	$117,896	$505,041
Intersegment net sales	5,335	3,683	9,018
Write down of long-lived assets	6,929	7,943	14,872
Segment operating loss	(14,359)	(8,257)	(22,616)
Nine-Months ended March 26, 2006:			
Net sales to external customers	$422,581	$133,036	$555,617
Intersegment net sales	4,103	4,390	8,493
Write down of long-lived assets		2,315	2,315
Restructuring charges (recovery)	47	(18)	29
Segment operating income (loss)	2,500	(5,066)	(2,566)

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

	For the Nine-Months Ended	
	March 25, 2007	March 26, 2006
Reconciliation of segment operating loss to net loss from continuing operations before income taxes:		
Reportable segments operating loss	$ (22,616)	$ (2,566)
Provision for bad debts	2,872	1,349
Interest expense, net	16,569	9,051
Other (income) expense, net	(2,705)	(1,138)
Equity in (earnings) losses of unconsolidated affiliates	4,473	(1,278)
Write down of long-lived assets	1,200	
Loss from continuing operations before income taxes	$ (45,025)	$ (10,550)

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 provision for bad debts of $2.3 million and $0.2 million for the current and prior year third quarter periods, respectively, and a provision of $2.9 million and $1.3 million for the current and prior year-to-date periods, respectively.

The total assets for the polyester segment increased from $359.2 million at June 25, 2006 to $415.5 million at March 25, 2007 due primarily to increases in other assets, inventory, accounts receivable, fixed assets, cash, other current assets, and deferred taxes of $33.4 million, $8.0 million, $7.7 million, $4.0 million, $2.2 million, $1.7 million, and $0.4 million, respectively. The increase is primarily attributable to the Dillon acquisition discussed in Footnote 14 Asset Acquisition. These increases were offset by decreases in assets held for sale of $1.1 million. The total assets for the nylon segment decreased from $128.2 million at June 25, 2006 to $118.1 million at March 25, 2007 due primarily to decreases in fixed assets and assets held for sale of $10.1 million and $7.6 million, respectively. These decreases were offset by increases in inventory, accounts receivable, deferred income taxes, cash, and other current assets of $4.9 million, $1.5 million, $0.7 million, $0.4 million, and $0.1 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 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. As a result of these grants, the Company incurred $0.2 million in the third quarter and $1.4 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.

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9. Derivative Financial Instruments

The Company accounts for derivative contracts and hedging activities under SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities which requires all derivatives to be recorded on the balance sheet at fair value. 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 100% of the asset cost may be covered by contracts in certain instances. Forward contracts are matched with the anticipated date of delivery of the assets and gains and losses are recorded as a component of the asset cost for purchase transactions when the Company is firmly committed. The latest maturity date for all outstanding purchase and sales foreign currency forward contracts is June 2007.

The dollar equivalent of these forward currency contracts and their related fair values are detailed below (amounts in thousands):

	March 25, 2007	June 25, 2006
Foreign currency purchase contracts:		
Notional amount	$ 870	$ 526
Fair value	882	535
Net (gain) loss	$ (12)	$ (9)
Foreign currency sales contracts:		
Notional amount	$ 576	