

Tight Knit

It's unlikely that investors would imagine the U.S. textiles industry as fertile ground for potential opportunity. Which is exactly why North Carolina synthetic-yarn producer Unifi Inc. may be worth trying on for size.

Just as it upended the domestic cotton-yarn industry, North Carolina-based Unifi Inc., a leading manufacturer of polyester and nylon yarns, was nearly upended itself following the 1997 devaluation of the Chinese yuan and subsequent rise of lower-cost Chinese synthetic-yarn competitors. By 2007 its revenues over ten years had fallen 60%. Its share price from the end of 1997 to the end of 2007 fell 95%.

As any long-lived company must, Unifi adapted. It cut costs, opened promising new markets in Central America and developed innovative “premium value added” [PVA] yarns offering differentiated comfort, texture, wearability and durability. One stand-out new line, called Repreve, adds a sustainability twist, as it is produced from recycled plastic bottles and post-industrial plastic waste.

From less than \$2 in February 2009, Unifi's shares hit \$37 a year ago as increasing demand from large customers such as Nike, North Face, Ford and Target pushed higher-margin PVA sales to a third of total revenues. EBITDA, \$23 million in the fiscal year ending June 2009, hit nearly \$64 million in fiscal 2015, or \$3.42 per share, on revenues of \$687 million.

The question today, however, is whether Unifi's story is starting to unravel. Revenue growth has stalled and Clay Dunnagan of Anchor Capital Management expects the company's free cash flow to come in at \$22 million this fiscal year, half the level of three years ago. The stock, now \$23, is off 37% over the past year.

Dunnagan, for one, believes the company is actually just hitting its stride. Revenue issues don't reflect product demand, he says, but result primarily from a decline in the Brazilian real – the company has a

large operation in Brazil – as well as end-market pricing pressures tied to declining raw-materials costs. Free cash flow is down mainly due to heavy capital spending to add needed Repreve manufacturing capacity, including backward integration

into plastics recycling. As those issues normalize and PVA products climb toward 50% of total revenues, he expects free cash flow to rebound to \$66 million by fiscal 2018 and EBITDA to rise at a 10% annual clip, hitting almost \$4.40 per share.

INVESTMENT SNAPSHOT

Unifi
(NYSE: UFI)

Business: Manufacture and sale of polyester and nylon yarns for apparel, hosiery, automotive, home-furnishings and other end markets.

Share Information (@3/30/16):

Price	22.91
52-Week Range	20.85 – 37.54
Dividend Yield	0.0%
Market Cap	\$408.7 million

Financials (TTM):

Revenue	\$665.6 million
Operating Profit Margin	6.0%
Net Profit Margin	6.0%

Valuation Metrics
(@3/30/16):

	UFI	S&P 500
P/E (TTM)	10.7	23.5
Forward P/E (Est.)	11.6	17.5

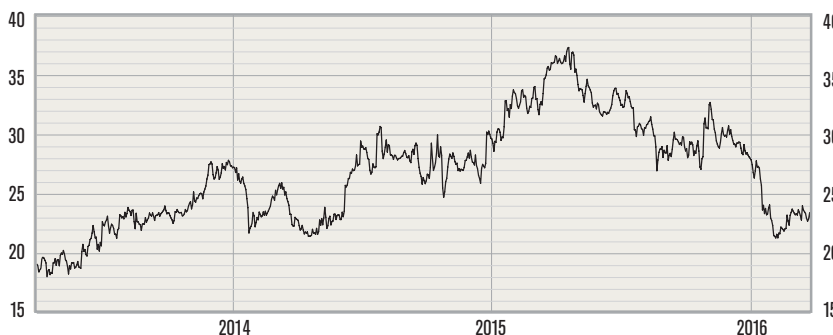
Largest Institutional Owners
(@12/31/15):

Company	% Owned
Dimensional Fund Adv	9.0%
BlackRock	7.7%
Impala Asset Mgmt	6.4%

Short Interest (as of 3/15/16):

Shares Short/Float	2.5%
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UFI PRICE HISTORY



THE BOTTOM LINE

Despite currency and end-market pricing trends working against it today, the company continues to transition to a higher-value-added product mix and increase earnings power, says Clay Dunnagan. He believes its operating business, at 10x EV/EBITDA on his 2016 estimates, and a stake in a cotton-product producer are currently worth \$39 per share.

Sources: Company reports, other publicly available information

Given its earnings-growth prospects, Dunnagan believes Unifi's core synthetic-yarn business on his estimates for this year deserve a 10x EV/EBITDA multiple, which translates into just under \$30 per share in equity value. On top of that he

adds \$9 per share for the company's 34% stake in Parkdale Mills, a leading global maker of cotton fabrics and yarns, which he values at a discounted-for-liquidity 7x EV/EBITDA on its current earnings.

"In many ways Unifi is a forgotten

company in a forgotten industry," says Dunnagan. "But it has a strong cash-flow story, durable competitive advantages and a great balance sheet. When neglect combines with potential like this, we try to take advantage." ^{vii}



Anchor Capital

Anchor Capital Management Company, LLC is an active and concentrated long-only investor in small capitalization U.S. companies. The firm seeks to produce superior long-term returns by investing in companies with healthy financial profiles, durable competitive positions and excellent leadership teams at significant discounts to intrinsic values. The firm was founded in 2008 and is based in Raleigh, North Carolina.

For more information, please visit the firm's web site at www.anchorcap.us, or contact us at (919) 755-0602.