UNIFI INC
Form 10-Q
February 06, 2009

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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 December 28, 2008

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, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer þ Non-accelerated filer o Smaller Reporting Company o
(Do not check if a smaller reporting company)

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

The number of shares outstanding of the issuer s common stock, par value $.10 per share, as of February 3, 2009 was 62,057,300.

UNIFI, INC.
Form 10-Q for the Quarterly Period Ended December 28, 2008

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Part.1 Financial Information
Item.1 Financial Statements

UNIFI, INC.
Condensed Consolidated Balance Sheets
(Amounts in thousands)

	December 28, 2008 (Unaudited)	June 29, 2008
ASSETS		
Current assets:		
Cash and cash equivalents	$ 12,619	$ 20,248
Receivables, net	68,611	103,272
Inventories	127,107	122,890
Deferred income taxes	1,417	2,357
Assets held for sale	1,700	4,124
Restricted cash	5,970	9,314
Other current assets	5,330	3,693
Total current assets	222,754	265,898
Property, plant and equipment	782,227	855,324
Less accumulated depreciation	(619,932)	(678,025)
	162,295	177,299
Investments in unconsolidated affiliates	71,094	70,562
Restricted cash	13,817	26,048
Goodwill	18,579	18,579
Intangible assets, net	19,328	20,386
Other noncurrent assets	10,841	12,759
Total assets	$ 518,708	$ 591,531
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 28,505	$ 44,553
Accrued expenses	17,475	25,531
Income taxes payable	41	681
Current maturities of long-term debt and other current liabilities	6,313	9,805
Total current liabilities	52,334	80,570
Long-term debt and other liabilities	195,502	204,366
Deferred income taxes	477	926
Commitments and contingencies		

Shareholders equity:		
Common stock	6,206	6,069
Capital in excess of par value	29,447	25,131
Retained earnings	244,750	254,494
Accumulated other comprehensive income (loss)	(10,008)	19,975
	270,395	305,669
Total liabilities and shareholders equity	$ 518,708	$ 591,531

See accompanying notes to condensed consolidated financial statements.

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UNIFI, INC.
Condensed Consolidated Statements of Operations
(Unaudited) (Amounts in thousands, except per share data)

	For the Quarters Ended		For the Six-Months Ended	
	December 28, 2008	December 23, 2007	December 28, 2008	December 23, 2007
Net sales	$ 125,727	$ 183,369	$ 294,736	$ 353,905
Cost of sales	123,415	175,049	278,999	334,592
Selling, general & administrative expenses	9,304	12,008	19,849	26,462
Provision (recovery) for bad debts	501	(189)	1,059	65
Interest expense	5,748	6,578	11,713	13,290
Interest income	(680)	(746)	(1,593)	(1,580)
Other (income) expense, net	(5,212)	(2,192)	(5,773)	(3,190)
Equity in (earnings) losses of unconsolidated affiliates	(162)	21	(3,644)	(157)
Restructuring charges		4,205		6,837
Write down of long-lived assets		2,247		2,780
Write down of investment in unconsolidated affiliates	1,483		1,483	4,505
Loss from continuing operations before income taxes	(8,670)	(13,612)	(7,357)	(29,699)
Provision (benefit) from income taxes	614	(5,757)	2,499	(12,688)
Loss from continuing operations	(9,284)	(7,855)	(9,856)	(17,011)
Income from discontinued operations net of tax	216	109	112	77
Net loss	$ (9,068)	$ (7,746)	$ (9,744)	$ (16,934)
Losses per common share (basic and diluted):				
Net loss continuing operations	$ (.15)	$ (.13)	$ (.16)	$ (.28)
Net income discontinued operations				
Net loss basic and diluted	$ (.15)	$ (.13)	$ (.16)	$ (.28)
Weighted average outstanding shares of common stock (basic and diluted)	62,030	60,553	61,582	60,545

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 Six-Months Ended December 28, 2008	December 23, 2007
Cash and cash equivalents at beginning of year	$ 20,248	$ 40,031
Operating activities:		
Net loss	(9,744)	(16,934)
Adjustments to reconcile net loss to net cash used in continuing operating activities:		
Income from discontinued operations	(112)	(77)
(Earnings) losses of unconsolidated equity affiliates, net of distributions	(1,579)	303
Depreciation	15,832	18,850
Amortization	2,137	2,324
Stock-based compensation expense	622	392
Deferred compensation expense (recovery), net	(69)	173
Net gain on asset sales	(5,910)	(1,413)
Non-cash write down of long-lived assets		2,780
Non-cash write down of investment in unconsolidated affiliate	1,483	4,505
Non-cash portion of restructuring charges		6,837
Deferred income tax expense (benefit)	35	(14,699)
Provision for bad debts	1,059	65
Other	256	(568)
Change in assets and liabilities, excluding effects of acquisitions and foreign currency adjustments	(11,962)	(8,124)
Net cash used in continuing operating activities	(7,952)	(5,586)
Investing activities:		
Capital expenditures	(7,829)	(3,827)
Acquisition	(500)	
Change in restricted cash	10,118	(14,810)
Proceeds from sale of capital assets	6,950	10,560
Proceeds from sale of equity affiliate		8,750
Collection of notes receivable		267
Return of capital from equity affiliate		234
Net cash provided by investing activities	8,739	1,174
Financing activities:		
Borrowings of long-term debt	14,600	
Payments of long-term debt	(20,578)	(11,000)
Proceeds from stock option exercises	3,830	
Other	37	(708)
Net cash used in financing activities	(2,111)	(11,708)

Cash flows of discontinued operations:		
Operating cash flow	(162)	(201)
Net cash used in discontinued operations	(162)	(201)
Effect of exchange rate changes on cash and cash equivalents	(6,143)	2,065
Net decrease in cash and cash equivalents	(7,629)	(14,256)
Cash and cash equivalents at end of period	$ 12,619	$ 25,775

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 of Unifi, Inc. (the Company) at June 29, 2008 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by United States generally accepted accounting principles (U.S. GAAP) for complete financial statements. Except as noted with respect to the balance sheet at June 29, 2008, this information is unaudited and reflects all adjustments which are, in the opinion of management, necessary to present fairly the financial position at December 28, 2008, and the results of operations and cash flows for the periods ended December 28, 2008 and December 23, 2007. 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 29, 2008. Certain prior period amounts have been reclassified to conform to current year presentation.

The significant accounting policies followed by the Company are presented on pages 65 to 71 of the Company s Annual Report on Form 10-K for the fiscal year ended June 29, 2008.

2. Inventories

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

	December 28, 2008	June 29, 2008
Raw materials and supplies	$ 55,013	$ 51,407
Work in process	4,861	7,021
Finished goods	67,233	64,462
	$ 127,107	$ 122,890

3. Accrued Expenses

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

	December 28, 2008	June 29, 2008
Payroll and fringe benefits	$ 6,064	$ 11,101
Severance	1,562	1,935
Interest	2,705	2,813
Utilities	1,443	3,114
Closure reserve	619	1,414
Retiree benefits	1,617	1,733
Property taxes	2,383	1,132

Other	1,082	2,289
	$ 17,475	$ 25,531

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4. Other (Income) Expense, Net

The following table summarizes the Company s other (income) expense, net (amounts in thousands):

	For the Quarters Ended		For the Six-Months Ended	
	December 28, 2008	December 23, 2007	December 28, 2008	December 23, 2007
Gain on sale of fixed assets	$ (5,594)	$ (1,271)	$ (5,910)	$ (1,413)
Gain from sale of nitrogen credits		(807)		(1,614)
Technology fee from China joint venture		(250)		(688)
Currency losses	380	131	77	458
Other, net	2	5	60	67
Other (income) expense, net	$ (5,212)	$ (2,192)	$ (5,773)	$ (3,190)

5. Goodwill and Other Intangible Assets, Net

The Company accounts for its goodwill and other intangibles under the provisions of Statements of Financial Accounting Standard (SFAS) No. 142, Goodwill and Other Intangible Assets (SFAS 142). SFAS 142 requires that these assets be reviewed for impairment annually, unless specific circumstances indicate that a more timely review is warranted. This impairment test involves estimates and judgments that are critical in determining whether any impairment charge should be recorded and the amount of such charge if an impairment loss is deemed to be necessary. As a result of the significant decline in the Company s market capitalization during the second quarter, the Company determined that it was appropriate to perform an interim impairment analysis. Accordingly, the Company conducted an impairment test of its goodwill during the second quarter of fiscal year 2009 and concluded that no impairment was necessary.

Other intangible assets subject to amortization consisted of customer relationships of $22.0 million and non-compete agreements of $4.0 million which were entered in connection with an asset acquisition consummated in fiscal year 2007. The customer list is being amortized in a manner which reflects the expected economic benefit that will be received over its twelve year life and the non-compete agreement is being amortized using the straight-line method over six years. There are no residual values related to these intangible assets. Accumulated amortization at December 28, 2008 and June 29, 2008 for these intangible assets was $7.2 million and $5.6 million, respectively.

In addition, the Company allocated $0.5 million to customer relationships arising from a transaction that closed in the second quarter of fiscal year 2009. This customer list will be amortized using the straight-line method over a period of one and a half years.

The intangible assets discussed above both relate to the polyester segment.

The following table represents the expected intangible asset amortization for the next five fiscal years (amounts in thousands):

	Aggregate Amortization Expenses				
	2010	2011	2012	2013	2014
Customer list	$ 2,993	$ 2,173	$ 2,022	$ 1,837	$ 1,481
Non-compete contract	571	571	571	571	286

$ 3,564	$ 2,744	$ 2,593	$ 2,408	$ 1,767

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6. Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements . SFAS No. 157 addresses how companies should measure fair value when they are required to use a fair value measure for recognition or disclosure purposes under generally accepted accounting principles. As a result of SFAS No. 157 there is now a common definition of fair value to be used throughout GAAP. The FASB believes that the new standard will make the measurement of fair value more consistent and comparable and improve disclosures about those measures. The provisions of SFAS No. 157 were to be effective for fiscal years beginning after November 15, 2007. On February 12, 2008, the FASB issued Staff Position (FSP) FAS 157-2 which delays the effective date of SFAS No. 157 for all nonfinancial assets and nonfinancial liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (at least annually). This FSP partially defers the effective date of SFAS No. 157 to fiscal years beginning after November 15, 2008, and interim periods within those fiscal years for items within the scope of this FSP. Effective for fiscal year 2009, the Company adopted SFAS No. 157 except as it applies to those nonfinancial assets and nonfinancial liabilities as noted in FSP FAS 157-2 and the adoption of this standard did not have a material effect on its consolidated financial statements.

7. Comprehensive Income (Loss)

Comprehensive losses amounted to $23.2 million and $39.7 million for the second quarter and year-to-date periods of fiscal year 2009, respectively, compared to comprehensive losses of $4.7 million and $10.4 million for the second quarter and the year-to-date periods of fiscal year 2008. Comprehensive losses were comprised of net losses of $9.1 million and $9.7 million for the second quarter and year-to-date periods of fiscal year 2009, respectively, and negative cumulative translation adjustments of $14.1 million and $30.0 million, respectively. Comparatively, comprehensive losses for the corresponding periods in the prior fiscal year were derived from net losses of $7.7 million and $16.9 million, and positive cumulative translation adjustments of $3.0 million and $6.5 million, respectively. The Company does not provide income taxes on the impact of currency translations as earnings from foreign subsidiaries are deemed to be permanently invested.

8. Investments in Unconsolidated Affiliates

The following table represents the Company s investments in unconsolidated affiliates:

Affiliate Name	Date Acquired	Location	Percent Ownership
Yihua Unifi Fibre Company Limited	August 2005 (1)	Yizheng, Jiangsu Province, People s Republic of China	50%
Parkdale America, LLC	June 1997	North and South Carolina	34%
Unifi-SANS Technical Fibers, LLC	September 2000 (2)	Stoneville, North Carolina	50%
U.N.F. Industries, LLC	September 2000	Migdal Ha Emek, Israel	50%

(1) The Company is currently

negotiating the sale of YUFI and therefore the Company did not record its share of equity losses in YUFI for the year-to-date period ended December 28, 2008 since the carrying value of its investment reflects the lower fair value of $9.0 million after impairment charges. See Footnote 12 Impairment Charges for further discussion.

(2) Sold in the second quarter of fiscal year 2008

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Condensed income statement information for the quarters and six-months ended December 28, 2008 and December 23, 2007, of the combined unconsolidated equity affiliates, Yihua Unifi Fibre Company Limited (YUFI), UNIFI-SANS Technical Fibers, LLC (USTF), Parkdale America, LLC (PAL), and U.N.F. Industries Ltd (UNF) are as follows (amounts in thousands):

	For the Quarter Ended December 28, 2008			
	YUFI	PAL	UNF	Total
Net sales	$30,950	$97,194	$ 6,543	$134,687
Gross profit (loss)	(1,528)	5,825	(877)	3,420
Depreciation and amortization	1,325	5,447	474	7,246
Income (loss) from operations	(2,783)	2,546	(1,374)	(1,611)
Net income (loss)	(2,949)	1,794	(1,268)	(2,423)

	For the Six-Months Ended December 28, 2008			
	YUFI	PAL	UNF	Total
Net sales	$70,830	$219,278	$12,435	$302,543
Gross profit (loss)	(3,575)	12,072	(1,667)	6,830
Depreciation and amortization	2,720	9,904	948	13,572
Income (loss) from operations	(6,939)	6,024	(2,625)	(3,540)
Net income (loss)	(7,566)	11,940	(2,411)	1,963

	For the Quarter Ended December 23, 2007			
	YUFI	PAL	UNF	Total

Net sales	$36,051	$104,944	$4,467	$145,462
Gross profit (loss)	(227)	5,827	(163)	5,437
Depreciation and amortization	1,294	4,760	316	6,370
Income (loss) from operations	(1,856)	2,532	(277)	399
Net income (loss)	(2,431)	3,213	(231)	551

	For the Six-Months Ended December 23, 2007				
	USTF	YUFI	PAL	UNF	Total
Net sales	$6,455	$73,120	$215,539	$11,830	$306,944
Gross profit (loss)	571	(534)	10,449	155	10,641
Depreciation and amortization	578	2,618	9,670	790	13,656
Income (loss) from operations	188	(3,628)	3,590	(142)	8
Net income (loss)	148	(4,845)	4,566	(88)	(219)

9. Income Taxes

The Company s income tax provision for the quarter ended December 28, 2008 resulted in tax expense at an effective rate of 7.1% as compared to the quarter ended December 23, 2007, which resulted in tax benefit at an effective rate of 42.3%. The Company s income tax provision for the year-to-date period ended December 28, 2008 resulted in tax expense at an effective rate of 33.5% compared to the year-to-date period ended December 23, 2007 which resulted in a tax benefit at an effective rate of 42.7%. The primary differences between the Company s effective tax rate and the U.S. statutory rate for the quarter and year-to-date period ended December 28, 2008 were attributable to state income tax benefits, foreign income taxed at rates less than the U.S. statutory rate and an increase in the valuation allowance. The primary differences between the Company s effective tax rate and the U.S. statutory rate for the quarter ended December 23, 2007 were losses from certain foreign operations taxed at a lower effective rate, state income tax benefits, and a decrease in the valuation allowance.

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Deferred income taxes have been provided for the temporary differences between financial statement carrying amounts and the tax basis of existing assets and liabilities. The Company has continued to record a valuation allowance against its net domestic deferred tax assets, and certain foreign deferred tax assets related to net operating losses, as those net deferred tax assets are more likely than not to be unrealizable for income tax purposes. The valuation allowance increased to $3.5 million and $4.1 million in the quarter and year-to-date period ended December 28, 2008, respectively, compared to a $1.7 million and $6.8 million decrease in the quarter and year-to-date period ended December 23, 2007. The net increase in the valuation allowance for the quarter ended December 28, 2008 primarily consisted of a $2.8 million increase for net operating losses generated this quarter (federal and state), and an increase of $0.7 million related to other temporary differences this quarter. The net increase in the valuation allowance for the year-to-date period ended December 28, 2008 primarily consisted of a $3.7 million increase for net operating losses generated year-to-date (federal and state), and an increase of $0.4 million related to other temporary differences.

There was no change in the amount of interest and penalties during the quarter and year-to-date period ended December 28, 2008 due to the company s federal and state net operating loss carryforwards.

The Company is subject to income tax examinations for U.S. federal income taxes for fiscal years 2007 and 2008. The Internal Revenue Service (IRS) recently concluded its exam for fiscal years 2003 through 2006. The Company is also subject to income tax examinations for non-U.S. income taxes for tax years 2000 through 2008, and for state and local income taxes for fiscal years 2001 through 2008.

10. Stock-Based Compensation

During the second quarter of fiscal year 2008, the Compensation Committee (Committee) of the Board of Directors (Board) authorized the issuance of 1,570,000 stock options from the 1999 Long-Term Incentive Plan of which 120,000 were issued to certain Board members and the remaining options were issued to certain key employees. The stock options issued to key employees are subject to a market condition which vests the options on the date that the closing price of the Company s common stock shall have been at least $6.00 per share for thirty consecutive trading days. The stock options issued to certain Board members are subject to a similar market condition in that one half of each member s options vest on the date that the closing price of the Company s common stock shall have been at least $8.00 per share for thirty consecutive trading days and the remaining one half vest on the date that the closing price of the Company s common stock shall have been at least $10.00 per share for thirty consecutive trading days. The Company used a Monte Carlo stock option model to estimate fair value and the derived vesting periods which range from 2.4 to 3.9 years.

On October 29, 2008, the shareholders of the Company approved the 2008 Unifi, Inc. Long-Term Incentive Plan (2008 Long-Term Incentive Plan). The plan authorized the issuance of up to 6,000,000 shares of Common Stock pursuant to the grant or exercise of stock options, including Incentive Stock Options (ISO), Non-Qualified Stock Options (NQSO) and restricted stock, but not more than 3,000,000 shares may be issued as restricted stock. Option awards are granted with an exercise price not less than the market price of the Company s stock at the date of grant.

During the second quarter of fiscal year 2009, the Committee of the Board authorized the issuance of 280,000 stock options from the 2008 Long-Term Incentive Plan to certain key employees. The stock options are subject to a market condition which vests the options on the date that the closing price of the Company s common stock shall have been at least $6.00 per share for thirty consecutive trading days. The exercise price is $4.16 per share. The Company used a Monte Carlo stock option model to estimate the fair value of $2.49 per share and the derived vesting period of 1.2 years.

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The Company incurred $0.3 million in the second quarter of both fiscal years 2009 and 2008, and $0.6 million and $0.4 million for the year-to-date periods, respectively, in stock-based compensation charges which were recorded as selling, general and administrative (SG&A) expenses with the offset to capital in excess of par value.

The Company issued 100,000 shares of common stock and 1,368,300 shares of common stock during the second quarter of fiscal year 2009 and the 2009 fiscal year-to-date period, respectively, as a result of the exercise of an equivalent number of stock options.

11. Assets Held for Sale

As of June 29, 2008, the Company had assets held for sale related to the consolidation of its polyester manufacturing capacity, which included the remaining assets and structures at the Kinston site which have a carrying value of $1.7 million and certain real property and related assets located in Yadkinville, North Carolina which have a carrying value of $2.4 million.

During the first quarter of fiscal year 2009, the Company reclassified as held and used $0.4 million of machines located in Yadkinville, North Carolina. During the second quarter of fiscal year 2009, the Company sold $0.6 million of the assets in Yadkinville, North Carolina to its Brazilian subsidiary.

On September 29, 2008, the Company entered into an agreement to sell the assets located in Yadkinville, North Carolina for $7.0 million. On December 19, 2008, the Company completed the sale which resulted in net proceeds of $6.6 million and a net pre-tax gain of $5.2 million in the second quarter of fiscal year 2009.

The following table summarizes by category assets held for sale (amounts in thousands):

	December 28, 2008	June 29, 2008
Land	$	$ 30
Building		1,348
Machinery and equipment	1,700	2,746
	$ 1,700	$ 4,124

12. Impairment Charges

Write down of long-lived assets

During the first quarter of fiscal year 2008, the Company s Brazilian polyester operation continued the modernization plan for its facilities by abandoning four of its older machines and replacing them with newer machines transferred from the Company s domestic polyester division. As a result, the Company recognized $0.5 million in non-cash impairment charges on the older machines.

During the second quarter of fiscal year 2008, the Company evaluated the carrying value of the remaining machinery and equipment at its Dillon, South Carolina facility and determined that a $1.6 million non-cash impairment charge was required.

In addition, the Company negotiated with a third party to sell the manufacturing facility located in Kinston, North Carolina. As a result of these negotiations, management concluded that the carrying value of the real estate exceeded its fair value. Accordingly, the Company recorded $0.7 million in non-cash impairment charges in the second quarter of fiscal year 2008.

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Write down of investment in unconsolidated affiliates

During the first quarter of fiscal year 2008, the Company performed a review of the fair value of USTF as part of the negotiations related to the sale. The Company determined that the carrying value exceeded its fair value and recorded a non-cash impairment charge of $4.5 million. The investment was sold in the second quarter of fiscal year 2008.

During the second quarter of fiscal year 2009, the Company and Sinopec Yizheng Chemical Fiber Co., Ltd, (YCFC) renegotiated the proposed agreement to sell the Company s interest in YUFI to YCFC for $9.0 million, pending final negotiation and execution of definitive agreements and the receipt of Chinese regulatory approvals. As a result, the Company recorded an additional impairment charge of $1.5 million due to the decline in the value of its investment and other related assets.

13. Severance and Restructuring Charges

Severance

In the first quarter of fiscal year 2008, the Company announced the closure of its polyester facility in Kinston, North Carolina. The Kinston facility produced partially oriented yarn (POY) for internal consumption and third party sales. The Company now purchases its commodity POY needs from external suppliers for conversion in its texturing operations. The Company continues to produce POY in its Yadkinville, North Carolina facility for specialty and premier valued-added (PVA) yarns and certain other commodity yarns. During the first quarter of fiscal year 2008, the Company recorded $0.8 million for severance related to its Kinston consolidation which was reflected on the Cost of sales line item in the Consolidated Statements of Operations. Approximately 231 employees, which included 31 salaried positions and 200 wage positions, were affected as a result of the reorganization.

In the second quarter of fiscal year 2008, the Company recorded an additional $0.4 million in severance costs related to Kinston employees who were associated with providing site services.

The Company recorded severance of $2.4 million for its former President and Chief Executive Officer during the first quarter of fiscal year 2008 and $1.7 million for severance related to its former Chief Financial Officer during the second quarter of fiscal year 2008 which were reflected on the Selling, general, & administrative expense line item in the Consolidated Statements of Operations.

On May 14, 2008, the Company announced the closure of its Staunton, Virginia facility and the transfer of all its production to its facility in Yadkinville, North Carolina which was completed in November 2008. During the first quarter of fiscal year 2009, the Company recorded $0.1 million for severance related to its Staunton consolidation. Approximately 6 salaried employees and 35 wage employees were affected by this reorganization. The expenses were reflected on the Cost of sales line item in the Consolidated Statements of Operations.

Restructuring

In the first quarter of fiscal year 2008, the Company recorded $1.5 million for restructuring charges related to unfavorable Kinston contracts for continued services after the closing of the facility.

In fiscal year 2007, the Company recorded a $2.9 million unfavorable contract reserve related to a portion of the sales and service contract which it entered into with Dillon for continued support of the Dillon business through December 2008. A portion of the sales and service contract was deemed to be unfavorable, after the Company announced its plan to consolidate the Dillon capacity into its other facilities.

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The table below summarizes changes to the accrued severance and accrued restructuring accounts for the period ended December 28, 2008 (amounts in thousands):

	Balance at June 29, 2008	Charges	Adjustments	Amounts Used	Balance at December 28, 2008
Accrued severance	$ 3,668	146	5	(1,280)	$ 2,539(1)
Accrued restructuring	$ 1,414		245	(1,040)	$ 619

(1) As of December 28, 2008, the Company classified $1.0 million of accrued executive severance as long term.

14. Discontinued Operations

The manufacturing facilities in Ireland ceased operations on October 31, 2004. The Company is in the process of closing the business which should be completed by the end of the third quarter of fiscal year 2009. The Company does not anticipate significant future cash flow activity from its discontinued operations. The Company recorded income of $0.2 million and $0.1 million for the second quarter of fiscal years 2009 and 2008, respectively, and income of $0.1 million and $0.1 million for the year-to-date periods, respectively.

15. 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. If the derivative is a hedge, depending on the nature of the 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 or are recorded in other comprehensive income until the hedged item is recognized in earnings. The ineffective portion of a derivative s change in fair value is immediately recognized in 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 and the dates they are consummated. The Company utilizes some natural hedging to mitigate these transaction exposures. The Company primarily enters into foreign currency forward contracts for the purchase and sale of European, North American and Brazilian 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. Counter-parties for these instruments are major financial institutions.

Currency forward contracts are used 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% to 75% of the sales value of these orders is covered by forward contracts. Maturity dates of the forward contracts are intended 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 for all outstanding purchase and sales foreign currency forward contracts are February 2009 and March 2009, respectively.

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

	December 28, 2008	June 29, 2008
Foreign currency purchase contracts:		
Notional amount	$ 638	$ 492
Fair value	664	499
Net (gain) loss	$ (26)	$ (7)
Foreign currency sales contracts:		
Notional amount	$ 656	$ 620
Fair value	638	642
Net gain (loss)	$ 18	$ (22)

For the quarters ended December 28, 2008 and December 23, 2007, the total impact of foreign currency related items on the Condensed Consolidated Statements of Operations, including transactions that were hedged and those that were not hedged, resulted in a pre-tax loss of $0.4 million and $0.1 million, respectively. For the year-to-date periods ended December 28, 2008 and December 23, 2007, the total impact of foreign currency related items resulted in a pre-tax loss of $0.1 million and $0.5 million, respectively.

16. Contingencies

On September 30, 2004, the Company completed its acquisition of the polyester filament manufacturing assets located at Kinston from INVISTA S.a.r.l. (INVISTA). The land for the Kinston site was leased pursuant to a 99 year ground lease (Ground Lease) with E.I. DuPont de Nemours (DuPont). Since 1993, DuPont has been investigating and cleaning up the Kinston site under the supervision of the United States Environmental Protection Agency (EPA) and the North Carolina Department of Environment and Natural Resources (DENR) pursuant to the Resource Conservation and Recovery Act Corrective Action program. The Corrective Action program requires DuPont to identify all potential areas of environmental concern (AOCs), assess the extent of containment at the identified AOCs and clean it up to comply with applicable regulatory standards. Under the terms of the Ground Lease, upon completion by DuPont of required remedial action, ownership of the Kinston site was to pass to the Company and after seven years of sliding scale shared responsibility with DuPont, the Company would have had sole responsibility for future remediation requirements, if any. Effective March 20, 2008, the Company entered into a Lease Termination Agreement associated with conveyance of certain assets at Kinston to DuPont. This agreement terminated the Ground Lease and relieved the Company of any future responsibility for environmental remediation, other than participation with DuPont, if so called upon, with regard to the Company s period of operation of the Kinston site. However, the Company continues to own a satellite service facility acquired in the INVISTA transaction that has contamination from DuPont s operations and is monitored by DENR. This site has been remediated by DuPont and DuPont has received authority from DENR to discontinue remediation, other than natural attenuation. DuPont s duty to monitor and report to DENR will be transferred to the Company in the future, at which time DuPont must pay the Company for seven years of monitoring and reporting costs and the Company will assume responsibility for any future remediation and monitoring of the site. At this time, the Company has no basis to determine if and when it will have any responsibility or obligation with respect to the AOCs or the extent of any potential liability for the same.

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17. Related Party Transaction

In fiscal year 2007, the Company purchased the polyester and nylon texturing operations of Dillon (the Transaction). In connection with the Transaction, the Company and Dillon entered into a Sales and Services Agreement for a term of two years from January 1, 2007, pursuant to which the Company agreed to pay Dillon an aggregate amount of $6.0 million in exchange for certain sales and transitional services to be provided by Dillon s sales staff and executive management, of which $0.8 million was paid during the first and second quarters of both fiscal year 2009 and fiscal year 2008. On December 1, 2008, the Company entered into an agreement to extend the Sales and Service agreement for a term of one year effective January 1, 2009 pursuant to which the Company will pay Dillon an aggregate amount of $1.7 million. Mr. Stephen Wener is the President and Chief Executive Officer of Dillon and is a director of the Company.

18. Segment Disclosures

The following is the Company s selected segment information for the quarters and six-month periods ended December 28, 2008 and December 23, 2007 (amounts in thousands):

	Polyester	Nylon	Total
Quarter ended December 28, 2008:			
Net sales to external customers	$ 93,984	$31,743	$125,727
Depreciation and amortization	5,419	1,795	7,214
Segment operating profit (loss)	(6,735)	(257)	(6,992)
Total assets	332,774	84,505	417,279
Quarter ended December 23, 2007:			
Net sales to external customers	$135,119	$48,250	$183,369
Intersegment net sales	1,422	752	2,174
Depreciation and amortization	6,273	3,291	9,564
Segment operating profit (loss)	(10,845)	705	(10,140)
Total assets	381,758	98,900	480,658

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

	For the Quarters Ended	
	December 28, 2008	December 23, 2007
Depreciation and amortization:		
Depreciation and amortization of specific reportable segment assets	$ 7,214	$ 9,564
Depreciation of allocated assets	418	559
Amortization of allocated assets	289	291
Consolidated depreciation and amortization	$ 7,921	$ 10,414
Reconciliation of segment operating loss to loss from continuing operations before income taxes:		
Reportable segments operating loss	$ (6,992)	$ (10,140)
Provision (recovery) for bad debts	501	(189)

Interest expense, net	5,068	5,832
Other (income) expense, net	(5,212)	(2,192)
Equity in (earnings) losses of unconsolidated affiliates	(162)	21
Write down of investment in unconsolidated affiliate	1,483	
Loss from continuing operations before income taxes	$ (8,670)	$ (13,612)

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	Polyester	Nylon	Total
Six-Months ended December 28, 2008:			
Net sales to external customers	$216,963	$77,773	$294,736
Intersegment net sales		71	71
Depreciation and amortization	12,401	4,103	16,504
Segment operating profit (loss)	(6,925)	2,813	(4,112)
Six-Months ended December 23, 2007:			
Net sales to external customers	$264,498	$89,407	$353,905
Intersegment net sales	3,219	1,521	4,740
Depreciation and amortization	12,883	6,583	19,466
Segment operating profit (loss)	(18,237)	1,471	(16,766)

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

	For the Six-Months Ended	
	December 28, 2008	December 23, 2007
Depreciation and amortization:		
Depreciation and amortization of specific reportable segment assets	$ 16,504	$ 19,466
Depreciation of allocated assets	886	1,127
Amortization of allocated assets	579	581
Consolidated depreciation and amortization	$ 17,969	$ 21,174
Reconciliation of segment operating loss to loss from continuing operations before income taxes:		
Reportable segments operating loss	$ (4,112)	$ (16,766)
Provision for bad debts	1,059	65
Interest expense, net	10,120	11,710
Other (income) expense, net	(5,773)	(3,190)
Equity in earnings of unconsolidated affiliates	(3,644)	(157)
Write down of investment in unconsolidated affiliate	1,483	4,505
Loss from continuing operations before income taxes	$ (7,357)	$ (29,699)

For purposes of internal management reporting, segment operating loss represents segment net sales less cost of sales, allocated selling, general and administrative expenses, segment restructuring charges, and segment impairments of long-lived assets. Certain non-segment manufacturing and unallocated selling, general and administrative costs are allocated to the operating segments based on activity drivers relevant to the respective costs. In the prior year, consolidated intersegment sales were recorded at market. Beginning in fiscal year 2009, the Company changed its domestic intersegment transfer pricing of inventory from a market value approach to a cost approach. Using the new methodology, no intersegment sales are recorded for domestic transfers of inventory. The amounts of domestic intersegment sales that were included in the prior second quarter and year-to-date numbers totaled $1.4 million and $3.2 million, respectively, for domestic polyester and $0.8 million and $1.5 million, respectively, for domestic nylon. The remaining intersegment sales relate to sales to the Company s foreign subsidiaries which are still recorded at market.

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The primary differences between the segmented financial information of the operating segments, 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, interest expense, net, and corporate equity investment and long-lived asset impairments.

Segment operating loss excluded the provision (recovery) for bad debts of $0.5 million and $(0.2) million for the current and prior year second quarter periods, respectively, and $1.1 million and $0.1 million for the year-to-date periods, respectively.

The total assets for the polyester segment decreased from $387.0 million at June 29, 2008 to $332.8 million at December 28, 2008 primarily due to decreases in accounts receivable, property, plant, and equipment, cash, long-term restricted cash, short-term restricted cash, other non-current assets, other current assets, and deferred taxes of $23.7 million, $11.5 million, $5.1 million, $5.1 million, $3.3 million, $2.4 million, $2.2 million, and $0.9 million, respectively. The total assets for the nylon segment decreased from $92.5 million at June 29, 2008 to $84.5 million at December 28, 2008 due primarily to decreases in accounts receivable and property, plant, and equipment of $8.9 million and $3.8 million, respectively. These decreases were offset by increases in inventory and cash of $4.2 million and $0.5 million, respectively.

19. Condensed Consolidated Guarantor and Non-Guarantor Financial Statements

The guarantor subsidiaries presented below represent the Company s subsidiaries that are subject to the terms and conditions outlined in the indenture governing the Company s issuance of the notes due in 2014 (the 2014 notes) and the guarantees, jointly and severally, on a senior secured basis. The non-guarantor subsidiaries presented below represent the foreign subsidiaries which do not guarantee the notes. Each subsidiary guarantor is 100% owned, directly or indirectly, by Unifi, Inc. and all guarantees are full and unconditional.

Supplemental financial information for the Company and its guarantor subsidiaries and non-guarantor subsidiaries of the 2014 notes is presented below.

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UNIFI, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Balance Sheet Information as of December 28, 2008 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current assets:					
Cash and cash equivalents	$ 1,312	$ (159)	$ 11,466	$	$ 12,619
Receivables, net	7	56,484	12,120		68,611
Inventories		98,918	28,189		127,107
Deferred income taxes			1,417		1,417
Assets held for sale		1,700			1,700
Restricted cash			5,970		5,970
Other current assets	223	2,201	2,906		5,330
Total current assets	1,542	159,144	62,068		222,754
Property, plant and equipment	11,336	712,893	57,998		782,227
Less accumulated depreciation	(1,758)	(576,635)	(41,539)		(619,932)
	9,578	136,258	16,459		162,295
Investments in unconsolidated affiliates		58,065	13,029		71,094
Restricted cash		11,106	2,711		13,817
Investments in consolidated subsidiaries	393,553			(393,553)	
Goodwill and intangible assets, net		37,907			37,907
Other noncurrent assets	58,261	(42,697)	(4,723)		10,841
	$ 462,934	$ 359,783	$ 89,544	$ (393,553)	$ 518,708
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					
Accounts payable and other	$ 139	$ 25,211	$ 3,155	$	$ 28,505
Accrued expenses	3,204	12,129	2,142		17,475
Income taxes payable	(804)	764	81		41
Current maturities of long-term debt and other current liabilities		343	5,970		6,313
Total current liabilities	2,539	38,447	11,348		52,334
Long-term debt and other liabilities	190,000	2,791	2,711		195,502

Deferred income taxes			477		477
Shareholders / invested equity	270,395	318,545	75,008	(393,553)	270,395
	$ 462,934	$ 359,783	$ 89,544	$ (393,553)	$ 518,708

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UNIFI, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Balance Sheet Information as of June 29, 2008 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
ASSETS					
Current assets:					
Cash and cash equivalents	$ 689	$ 3,377	$ 16,182	$	$ 20,248
Receivables, net	66	82,040	21,166		103,272
Inventories		92,581	30,309		122,890
Deferred income taxes			2,357		2,357
Assets held for sale		4,124			4,124
Restricted cash			9,314		9,314
Other current assets	26	733	2,934		3,693
Total current assets	781	182,855	82,262		265,898
Property, plant and equipment	11,273	765,710	78,341		855,324
Less accumulated depreciation	(1,616)	(623,262)	(53,147)		(678,025)
	9,657	142,448	25,194		177,299
Investments in unconsolidated affiliates		60,853	9,709		70,562
Restricted cash		18,246	7,802		26,048
Investments in consolidated subsidiaries	417,503			(417,503)	
Goodwill and intangible assets, net		38,965			38,965
Other noncurrent assets	74,271	(60,879)	(633)		12,759
	$ 502,212	$ 382,488	$ 124,334	$ (417,503)	$ 591,531
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					
Accounts payable and other	$ 172	$ 39,328	$ 5,053	$	$ 44,553
Accrued expenses	3,371	18,011	4,149		25,531
Income taxes payable			681		681
Current maturities of long-term debt and other current liabilities		491	9,314		9,805
Total current liabilities	3,543	57,830	19,197		80,570
Long-term debt and other liabilities	193,000	3,563	7,803		204,366

Deferred income taxes			926		926
Shareholders / invested equity	305,669	321,095	96,408	(417,503)	305,669
	$ 502,212	$ 382,488	$ 124,334	$ (417,503)	$ 591,531

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UNIFI, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Statement of Operations Information for the Fiscal Quarter Ended December 28, 2008 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Summary of Operations:					
Net sales	$	$ 103,324	$ 22,586	$ (183)	$ 125,727
Cost of sales		103,756	19,750	(91)	123,415
Selling, general and administrative expenses	190	7,669	1,537	(92)	9,304
Provision (recovery) for bad debts		620	(119)		501
Interest expense	5,717	31			5,748
Interest income	(27)	(2)	(651)		(680)
Other (income) expense, net	(13)	(5,242)	(1)	44	(5,212)
Equity in (earnings) losses of unconsolidated affiliates		(610)	634	(186)	(162)
Equity in subsidiaries	2,640			(2,640)	
Write down of investment in unconsolidated affiliate		483	1,000		1,483
Income (loss) from continuing operations before income taxes	(8,507)	(3,381)	436	2,782	(8,670)
Provision (benefit) for income taxes	561	(573)	626		614
Income (loss) from continuing operations	(9,068)	(2,808)	(190)	2,782	(9,284)
Income from discontinued operations, net of tax			216		216
Net income (loss)	$ (9,068)	$ (2,808)	$ 26	$ 2,782	$ (9,068)

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UNIFI, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Statement of Operations Information for the Fiscal Quarter Ended December 23, 2007 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Summary of Operations:					
Net sales	$	$ 149,387	$ 34,402	$ (420)	$ 183,369
Cost of sales		144,756	30,506	(213)	175,049
Selling, general and administrative expenses		10,076	2,000	(68)	12,008
Provision (recovery) for bad debts		(367)	178		(189)
Interest expense	6,316	161	101		6,578
Interest income	(184)	(136)	(426)		(746)
Other (income) expense, net	(6,239)	3,602	201	244	(2,192)
Equity in (earnings) losses of unconsolidated affiliates		(1,342)	1,331	32	21
Equity in subsidiaries	(5,159)			5,159	
Write down of long-lived assets		2,247			2,247
Restructuring charges		4,205			4,205
Income (loss) from continuing operations before income taxes	5,266	(13,815)	511	(5,574)	(13,612)
Provision (benefit) for income taxes	13,012	(19,372)	603		(5,757)
Income (loss) from continuing operations	(7,746)	5,557	(92)	(5,574)	(7,855)
Income from discontinued operations, net of tax			109		109
Net income (loss)	$ (7,746)	$ 5,557	$ 17	$ (5,574)	$ (7,746)

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UNIFI, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Statement of Operations Information for the Six-Months Ended December 28, 2008 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Summary of Operations:					
Net sales	$	$ 233,015	$ 62,253	$ (532)	$ 294,736
Cost of sales		226,235	53,185	(421)	278,999
Selling, general and administrative expenses	190	16,239	3,573	(153)	19,849
Provision (recovery) for bad debts		1,074	(15)		1,059
Interest expense	11,646	62	5		11,713
Interest income	(46)	(48)	(1,499)		(1,593)
Other (income) expense, net	(15)	(5,222)	(361)	(175)	(5,773)
Equity in (earnings) losses of unconsolidated affiliates		(4,060)	1,205	(789)	(3,644)
Equity in subsidiaries	(1,251)			1,251	
Write down of investment in unconsolidated affiliate		483	1,000		1,483
Income (loss) from continuing operations before income taxes	(10,524)	(1,748)	5,160	(245)	(7,357)
Provision (benefit) for income taxes	(780)	802	2,477		2,499
Income (loss) from continuing operations	(9,744)	(2,550)	2,683	(245)	(9,856)
Income from discontinued operations, net of tax			112		112
Net income (loss)	$ (9,744)	$ (2,550)	$ 2,795	$ (245)	$ (9,744)

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UNIFI, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Statement of Operations Information for the Six-Months Ended December 23, 2007 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Summary of Operations:					
Net sales	$	$ 290,230	$ 64,576	$ (901)	$ 353,905
Cost of sales		277,871	57,419	(698)	334,592
Selling, general and administrative expenses		22,876	3,747	(161)	26,462
Provision for bad debts		47	18		65
Interest expense	12,878	315	97		13,290
Interest income	(336)	(136)	(1,108)		(1,580)
Other (income) expense, net	(12,753)	8,903	416	244	(3,190)
Equity in (earnings) losses of unconsolidated affiliates		(2,251)	2,466	(372)	(157)
Equity in subsidiaries	4,049			(4,049)	
Write down of long-lived assets		2,247	533		2,780
Write down of investment in unconsolidated affiliate		4,505			4,505
Restructuring charges		6,837			6,837
Income (loss) from continuing operations before income taxes	(3,838)	(30,984)	988	4,135	(29,699)
Provision (benefit) for income taxes	13,096	(26,905)	1,121		(12,688)
Income (loss) from continuing operations	(16,934)	(4,079)	(133)	4,135	(17,011)
Income from discontinued operations, net of tax			77		77
Net income (loss)	$ (16,934)	$ (4,079)	$ (56)	$ 4,135	$ (16,934)

UNIFI, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Statements of Cash Flows Information for the Six-Months Ended December 28, 2008 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Operating activities:					
Net cash provided by (used in) continuing operating activities	$ 4,642	$ (11,129)	$ (1,316)	$ (149)	$ (7,952)
Investing activities:					
Capital expenditures	(68)	(6,742)	(1,769)	750	(7,829)
Acquisition		(500)			(500)
Change in restricted cash		7,140	2,978		10,118
Proceeds from sale of capital assets		7,658	42	(750)	6,950
Reclassification of investment to foreign guarantor	(4,781)		4,781		
Net cash provided by (used in) investing activities	(4,849)	7,556	6,032		8,739
Financing activities:					
Borrowings of long term debt	14,600				14,600
Payments of long term debt	(17,600)		(2,978)		(20,578)
Proceeds from stock exercises	3,830				3,830
Other		37			37
Net cash provided by (used in) financing activities	830	37	(2,978)		(2,111)
Cash flows of discontinued operations:					
Operating cash flow			(162)		(162)
Net cash used in discontinued operations			(162)		(162)
Effect of exchange rate changes on cash and cash equivalents			(6,292)	149	(6,143)
Net increase (decrease) in cash and cash equivalents	623	(3,536)	(4,716)		(7,629)
Cash and cash equivalents at beginning of period	689	3,377	16,182		20,248

Cash and cash equivalents at end of period	$	1,312	$	(159)	$	11,466	$		$	12,619

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UNIFI, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Statements of Cash Flows Information for the Six-Months Ended December 23, 2007 (amounts in thousands):

	Parent	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Operating activities:					
Net cash provided by (used in) continuing operating	$ (1,743)	$ (4,820)	$ 1,412	$ (435)	$ (5,586)
Investing activities:					
Capital expenditures		(2,464)	(2,203)	840	(3,827)
Return of capital in equity affiliates		234			234
Change in restricted cash		(14,810)			(14,810)
Proceeds from sale of equity affiliate		8,750			8,750
Proceeds from sale of capital assets		11,288	112	(840)	10,560
Other	7	260			267
Net cash provided by (used in) investing activities	7	3,258	(2,091)		1,174
Financing activities:					
Payments of long term debt	(11,000)				(11,000)
Dividend payment	9,494		(9,494)		
Other	(3)	34	(739)		(708)
Net cash provided by (used in) financing activities	(1,509)	34	(10,233)		(11,708)
Cash flows of discontinued operations:					
Operating cash flow			(201)		(201)
Net cash used in discontinued operations			(201)		(201)
Effect of exchange rate changes on cash and cash equivalents			1,630	435	2,065
Net increase (decrease) in cash and cash equivalents	(3,245)	(1,528)	(9,483)		(14,256)

Cash and cash equivalents at beginning of period	17,808	1,645	20,578		40,031
Cash and cash equivalents at end of period	$ 14,563	$ 117	$ 11,095	$	$ 25,775

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

The following is Management s discussion and analysis of certain significant factors that have affected Unifi, Inc. s (the Company s) operations and material changes in financial condition during the periods included in the accompanying Condensed Consolidated Financial Statements.

Business Overview

The Company is a diversified producer and processor of multi-filament polyester and nylon yarns, including specialty yarns with enhanced performance characteristics. The Company adds value to the supply chain and enhances consumer demand for its products through the development and introduction of branded yarns that provide unique performance, comfort and aesthetic advantages. The Company manufactures partially oriented, textured, dyed, twisted and beamed polyester yarns as well as textured nylon and nylon covered spandex products. The Company sells its products to other yarn manufacturers, knitters and weavers that produce fabric for the apparel, hosiery, furnishings, automotive, industrial and other end-use markets. The Company maintains one of the industry s most comprehensive product offerings and emphasizes quality, style and performance in all of its products.

Polyester Segment. The polyester segment manufactures partially oriented, textured, dyed, twisted and beamed yarns with sales to other yarn manufacturers, knitters and weavers that produce fabrics for the apparel, automotive, hosiery, furnishings, industrial and other end-use markets. The polyester segment primarily manufactures its products in Brazil and the United States (U.S.) which has the largest operations.

Nylon Segment. The nylon segment manufactures textured nylon and covered spandex products with sales to other yarn manufacturers, knitters and weavers that produce fabrics for the apparel, hosiery, sock and other end-use markets. The nylon segment consists of operations in Colombia and the U.S. which has the largest operations.

Recent Developments and Outlook

Although the global textile and apparel industry continues to grow, the U.S. textile and apparel industry has contracted substantially since 1999. This contraction was caused primarily by intense foreign competition in finished products which has resulted in over capacity domestically and the closure of many domestic textile and apparel plants or the movement of their operations offshore. According to industry experts, the North American polyester textile filament market is estimated to have declined by approximately 5% in calendar year 2007 compared to an estimated decline of approximately 16% in calendar year 2006. Regional manufacturers continue to demand North American manufactured yarn and fabrics due to the duty-free advantage, quick response times, readily available production capacity, and specialized products. In addition, North American retailers have expressed the need to have a balanced procurement strategy with both global and regional producers. Industry experts originally projected a decline for calendar year 2008 at a rate of 4% to 5%, similar to calendar year 2007; however, experts now believe the rate of polyester industry contraction in North America during calendar year 2008 is projected to have declined by approximately 18% to 20% as a result of the current economic crisis. Unlike prior contractions in North American production, which were primarily due to import competition of finished goods, the contraction in calendar year 2008 was primarily driven by decreased demand from all sectors of the Company s downstream market such as apparel, automotive, and furnishings which have been significantly impacted by the economic and retail downturn which began in the second half of calendar year 2008. The U.S. economic slowdown is expected to impact consumer spending and retail sales within the Company s key market segments during calendar year 2009.

During the last fiscal year, the Company faced an extremely difficult operating environment, driven by a faltering economy, and unprecedented increases in the cost of raw materials, energy and freight. However, the Company has reacted decisively in dealing with these conditions. A combination of sales price increases, cost containment, operational efficiencies and customer service, coupled with an aggressive raw material sourcing strategy, has partially offset the negative impact of the economic downturn on the Company.

The Company believes that its success going forward is primarily based on its ability to improve the mix of its product offerings by shifting to more premier value-added (PVA) products, aggressively negotiating favorable raw material supply agreements, implementing cost saving strategies which will improve its operating efficiencies, and leveraging the free-trade agreements to which the U.S. is a party. The continued viability of the U.S. domestic textile and apparel industry is dependent, to a large extent, on the international trade regulatory environment.

In addition to the difficult economic conditions in the U.S. markets, the Company was negatively impacted by the continued rising cost of raw materials and other petrochemical driven costs during the first quarter of fiscal year 2009. The impact of the surge in crude oil prices since the beginning of fiscal year 2008 created a spike in polyester and nylon raw material prices. As raw material prices peaked in July 2008, the Company was not able to pass all of these raw material increases along to its customers in the first quarter of fiscal year 2009 which resulted in lower conversion margins. Operating results for the second quarter of fiscal year 2009 were also adversely impacted as these higher priced products continued to work through the Company s inventory systems. However, crude oil prices declined substantially during the second quarter and therefore the cost of polyester ingredients declined as well.

Polyester raw yarn imports have declined by approximately 17% in calendar year 2008 while global imports of synthetic apparel were down approximately 3% during the first eleven months of calendar year 2008. However, imports from the U.S. Dominican Republic Central American Free Trade Agreement (CAFTA) region were up approximately 13% during the same period as U.S. brands and retailers continue to take advantage of the shorter lead times and the competitiveness of the region. The trend toward regional production is expected to continue and is significant because over half of the U.S. production goes into programs that require regional fiber in order for the garment to qualify for duty free treatment.

The recent global economic downturn negatively impacted the Company s sales volume beginning in mid-September 2008 in the apparel, home furnishings, and automotive segments. The Company s sales volume declined 32% during the second quarter of fiscal year 2009 compared to the same quarter in the prior year as a result of sharp declines in retail apparel sales of 7%, home furnishing sales of 15%, and automotive sales of 18%. Industry experts expect the decline in apparel retail sales to further deteriorate to a run rate of negative 10% to 12% over the next six months. Based on these volumes and the extraordinarily high inventory levels across the supply chain, the Company expects its sales volumes to remain significantly lower than retail sales over the next two quarters. Other economic recessionary trends such as low consumer confidence and job losses could further adversely impact the Company s sales during the second half of fiscal year 2009.

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Key Performance Indicators

The Company continuously reviews performance indicators to measure its success. The following are the indicators management uses to assess performance of the Company s business:

- sales volume, which is an indicator of demand;
- margins, which are indicators of product mix and profitability;
- net income or loss before interest, taxes, depreciation and amortization, and income or loss from discontinued operations (EBITDA), which are indicators of the Company s ability to pay debt; and
- working capital of each business unit as a percentage of sales, which is an indicator of the Company s production efficiency and ability to manage its inventory and receivables.

Corporate Restructuring

Severance

In the first quarter of fiscal year 2008, the Company announced the closure of its polyester facility in Kinston, North Carolina. The Kinston facility produced partially oriented yarn (POY) for internal consumption and third party sales. The Company now purchases its commodity POY needs from external suppliers for conversion in its texturing operations. The Company continues to produce POY in its Yadkinville, North Carolina facility for specialty and premier valued-added (PVA) yarns and certain other commodity yarns. During the first quarter of fiscal year 2008, the Company recorded $0.8 million for severance related to its Kinston consolidation which was reflected on the Cost of sales line item in the Consolidated Statements of Operations. Approximately 231 employees, which included 31 salaried positions and 200 wage positions, were affected as a result of the reorganization.

In the second quarter of fiscal year 2008, the Company recorded an additional $0.4 million in severance costs related to Kinston employees who were associated with providing site services.

The Company recorded severance of $2.4 million for its former President and Chief Executive Officer during the first quarter of fiscal year 2008 and $1.7 million for severance related to its former Chief Financial Officer during the second quarter of fiscal year 2008 which were reflected on the Selling, general, & administrative expense line item in the Consolidated Statements of Operations.

On May 14, 2008, the Company announced the closing of its Staunton, Virginia facility and the transfer of all its production to its facility in Yadkinville, North Carolina which was completed in November 2008. During the first quarter of fiscal year 2009, the Company recorded $0.1 million for severance related to its Staunton consolidation. Approximately 6 salaried employees and 35 wage employees were affected by this reorganization. The expenses were reflected on the Cost of sales line item in the Consolidated Statements of Operations.

Restructuring

In the first quarter of fiscal year 2008, the Company recorded $1.5 million for restructuring charges related to unfavorable Kinston contracts for continued services after the closing of the facility.

In fiscal year 2007, the Company recorded a $2.9 million unfavorable contract reserve related to a portion of the sales and service contract which it entered into with Dillon for continued support of the Dillon business through December 2008. A portion of the sales and service contract was deemed to be unfavorable, after the Company announced its plan to consolidate the Dillon capacity into its other facilities.

The table below summarizes changes to the accrued severance and accrued restructuring accounts for the period ended December 28, 2008 (amounts in thousands):

	Balance at June 29, 2008	Charges	Adjustments	Amounts Used	Balance at December 28, 2008
Accrued severance	$ 3,668	146	5	(1,280)	$ 2,539(1)
Accrued restructuring	$ 1,414		245	(1,040)	$ 619

(1) As of December 28, 2008, the Company classified $1.0 million of accrued executive severance as long term.

Joint Ventures and Other Equity Investments

Condensed income statement information for the quarters ended and year-to-date periods December 28, 2008 and December 23, 2007, of the combined unconsolidated equity affiliates, Yihua Unifi Fibre Company Limited (YUFI), UNIFI-SANS Technical Fibers, LLC (USTF), Parkdale America, LLC (PAL), and U.N.F. Industries Ltd (UNF) are a follows (amounts in thousands):

	For the Quarter Ended December 28, 2008			
	YUFI	PAL	UNF	Total
Net sales	$30,950	$ 97,194	$ 6,543	$134,687
Gross profit (loss)	(1,528)	5,825	(877)	3,420
Depreciation and amortization	1,325	5,447	474	7,246
Income (loss) from operations	(2,783)	2,546	(1,374)	(1,611)
Net income (loss)	(2,949)	1,794	(1,268)	(2,423)

	For the Six-Months Ended December 28, 2008			
	YUFI	PAL	UNF	Total
Net sales	$70,830	$219,278	$12,435	$302,543
Gross profit (loss)	(3,575)	12,072	(1,667)	6,830
Depreciation and amortization	2,720	9,904	948	13,572
Income (loss) from operations	(6,939)	6,024	(2,625)	(3,540)
Net income (loss)	(7,566)	11,940	(2,411)	1,963

	For the Quarter Ended December 23, 2007			
	YUFI	PAL	UNF	Total
Net sales	$36,051	$104,944	$ 4,467	$145,462
Gross profit (loss)	(227)	5,827	(163)	5,437
Depreciation and amortization	1,294	4,760	316	6,370
Income (loss) from operations	(1,856)	2,532	(277)	399
Net income (loss)	(2,431)	3,213	(231)	551

	For the Six-Months Ended December 23, 2007				
	USTF (1)	YUFI	PAL	UNF	Total
Net sales	$6,455	$73,120	$215,539	$11,830	$306,944
Gross profit (loss)	571	(534)	10,449	155	10,641
Depreciation and amortization	578	2,618	9,670	790	13,656
Income (loss) from operations	188	(3,628)	3,590	(142)	8
Net income (loss)	148	(4,845)	4,566	(88)	(219)

(1) Sold in the second quarter of fiscal year 2008

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In August 2005, the Company formed YUFI, a 50/50 joint venture with Sinopec Yizheng Chemical Fiber Co., Ltd, (YCFC), a publicly traded (listed in Shanghai and Hong Kong) enterprise, to manufacture, process, and market commodity and specialty polyester filament yarn in YCFC s facilities in China. The Company granted YUFI an exclusive, non-transferable license to certain of its branded product technology (including Mynx®, Sorbtek®, Reflexx®, and dye springs) in China for a license fee of $6.0 million over a four year period.

In July 2008, the Company announced a proposed agreement to sell its 50% ownership interest in YUFI to its partner, YCFC, for $10.0 million. In connection with a review of the fair value of YUFI during negotiations related to the sale, the Company initiated a review of the carrying value of its investment in YUFI in accordance with Accounting Principles Board Opinion 18, The Equity Method of Accounting for Investments in Common Stock (APB 18). As a result of this review, the Company determined that the carrying value of its investment in YUFI exceeded its fair value. Accordingly, the Company recorded a non-cash impairment charge of $6.4 million in the fourth quarter of fiscal year 2008. During the second quarter of fiscal year 2009, the Company and YCFC renegotiated the proposed agreement to sell the Company s interest in YUFI to YCFC for $9.0 million, pending final negotiation and execution of definitive agreements and the receipt of Chinese regulatory approvals. As a result, the Company recorded an additional impairment charge of $1.5 million due to the decline in the value of its investment and other related assets. However, there can be no assurances that this transaction will occur upon these terms.

For the quarter and year-to-date periods ended December 23, 2007, the Company recognized equity losses net of technology and license fee income of $1.0 million and $1.7 million, respectively. In addition, the Company recognized $0.5 million and $1.3 million in operating expenses for the quarter and year-to-date periods ended December 23, 2007, respectively, which was primarily reflected on the Cost of sales line item in the Consolidated Statements of Operations, directly related to providing technological support in accordance with the Company s joint venture contract. The Company did not record its share of equity losses in YUFI for the year-to-date period ended December 28, 2008, since the carrying value of its investment reflects the lower fair value of $9.0 million as a result of the impairment charge described above.

In June 1997, the Company and Parkdale Mills, Inc. entered into a contribution agreement whereby both companies contributed all of the assets of their spun cotton yarn operations utilizing open-end and air jet spinning technologies to create PAL. In exchange for its contributions, the Company received a 34% ownership interest in the joint venture. PAL is a producer of cotton and synthetic yarns for sale to the textile and apparel industries primarily within North America. PAL has 12 manufacturing facilities primarily located in central and western North Carolina and in South Carolina. For the quarter and year-to-date periods ended December 28, 2008, the Company recognized net equity earnings of $0.6 million and $4.1 million, respectively, compared to equity earnings of $1.1 million and $1.6 million for the respective corresponding periods in the prior year. The Company received accumulated distributions from PAL of $2.1 million and $0.7 million for the year-to-date periods of fiscal years 2009 and 2008, respectively.

In September 2000, the Company and SANS Fibres of South Africa (SANS Fibres) formed USTF, a 50/50 joint venture created to produce low-shrinkage high tenacity nylon 6.6 light denier industrial yarns in North Carolina. The business was operated in a plant in Stoneville, North Carolina. In the second quarter of fiscal year 2008, the Company completed the sale of its interest in USTF.

In September 2000, the Company and Nilit Ltd (Nilit) formed UNF; a 50/50 joint venture to produce nylon POY at Nilit s manufacturing facility in Migdal Ha-Emek, Israel which is the Company s primary source of nylon POY for its texturing operations. For the quarter and year-to-date periods ended December 28, 2008, the Company recognized net equity losses of $0.4 million and $0.4 million, respectively, compared to net equity losses of $0.1 million and net equity earnings of $0.3 million for the respective corresponding periods in the prior year.

The Company accounts for its goodwill and other intangibles under the provisions of Statements of Financial Accounting Standard (SFAS) No. 142, Goodwill and Other Intangible Assets (SFAS 142). SFAS 142 requires tha these assets be reviewed for impairment annually, unless specific circumstances indicate that a more timely review is warranted. This impairment test involves estimates and judgments that are critical in determining whether any impairment charge should be recorded and the amount of such charge if an impairment loss is deemed to be necessary.
As a result of the significant decline in the Company s market capitalization during the second quarter, the Company determined that it was appropriate to perform an interim impairment analysis. Accordingly, the Company conducted an impairment test of its goodwill during the second quarter of fiscal year 2009 and concluded that no impairment was necessary. However, given the current market conditions and fluctuations in the Company s market capitalization the results of the test could change going forward. Therefore, the Company will continue to evaluate the need to perform interim impairment tests on a quarter-by-quarter basis until market conditions stabilize. Future events impacting cash flows for existing assets could render a write-down necessary that previously required no such write-down.
In fiscal year 2007, the Company purchased the polyester and nylon texturing operations of Dillon (the Transaction). In connection with the Transaction, the Company and Dillon entered into a Sales and Services Agreement for a term of two years from January 1, 2007, pursuant to which the Company agreed to pay Dillon an aggregate amount of $6.0 million in exchange for certain sales and transitional services to be provided by Dillon s sales staff and executive management, of which $0.8 million was paid during the first and second quarters of both fiscal year 2009 and fiscal year 2008. On December 1, 2008, the Company entered into an agreement to extend the Sales and Service agreement for a term of one year effective January 1, 2009 pursuant to which the Company will pay Dillon an aggregate amount of $1.7 million. Mr. Stephen Wener is the President and Chief Executive Officer of Dillon and is a director of the Company.

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Review of Second Quarter Fiscal Year 2009 compared to Second Quarter Fiscal Year 2008

The following table sets forth the loss from continuing operations components for each of the Company s business segments for the fiscal quarters ended December 28, 2008 and December 23, 2007, respectively. The table also sets forth each of the segments net sales as a percent to total net sales, the net income (loss) components as a percent to total net sales and the percentage increase or decrease of such components over the comparable prior year period (amounts in thousands, except percentages):

	For the Quarters Ended				
	December 28, 2008		December 23, 2007		
		% to Total		% to Total	% Change
Net sales					
Polyester	$ 93,984	74.8	$ 135,119	73.7	(30.4)
Nylon	31,743	25.2	48,250	26.3	(34.2)
Total	$ 125,727	100.0	$ 183,369	100.0	(31.4)

		% to Sales		% to Sales	
Gross profit					
Polyester	$ 559	0.4	$ 5,850	3.2	(90.4)
Nylon	1,753	1.4	2,470	1.3	(29.0)
Total	2,312	1.8	8,320	4.5	(72.2)
Selling, general and administrative expenses					
Polyester	7,294	5.8	10,243	5.6	(28.8)
Nylon	2,010	1.6	1,765	0.9	13.9
Total	9,304	7.4	12,008	6.5	(22.5)
Write down of long-lived assets and investment in unconsolidated affiliate					
Polyester			2,247	1.2	
Nylon					
Corporate	1,483	1.1			
Total	1,483	1.1	2,247	1.2	(34.0)
Restructuring charges					
Polyester			4,205	2.3	
Nylon					
Total			4,205	2.3	
Other (income) expense, net	195	0.2	3,472	1.9	(94.4)

Loss from continuing operations before income taxes	(8,670)	(6.9)	(13,612)	(7.4)	(36.3)
Provision (benefit) for income taxes	614	0.5	(5,757)	(3.1)	(110.7)
Loss from continuing operations	(9,284)	(7.4)	(7,855)	(4.3)	18.2
Income from discontinued operations, net of tax	216	(0.2)	109	0.1	98.2
Net loss	$ (9,068)	(7.2)	$ (7,746)	(4.2)	17.1

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As reflected in the tables above, consolidated net sales from continuing operations decreased from $183.4 million to $125.7 million which was primarily attributable to decreased sales in the apparel, automotive and furnishing market segments. Consolidated unit volumes decreased by 32.4% for the second quarter of fiscal year 2009, while average net selling prices increased 1.0% for the same period.

Refer to the discussion of segment operations under the captions Polyester Operations and Nylon Operations for a further discussion of each segment s operating results.

Consolidated gross profit from continuing operations decreased by $6.0 million to $2.3 million for the quarter ended December 28, 2008 as compared to the prior year second quarter. This decrease was primarily attributable to lower conversion margins and increases in fixed converting costs due to lower utilization rates.

Consolidated selling, general and administrative (SG&A) expenses decreased by $2.7 million or 22.5% during the second quarter of fiscal year 2009 as compared to the prior year second quarter. The decrease in SG&A for the second quarter was primarily a result of decreases of $1.7 million in executive severance costs, $0.5 million in the Company s Brazilian operation, $0.3 million in salaries and fringe expenses which includes a $0.5 million savings related to management bonuses, $0.2 million in depreciation expenses, $0.1 million in insurance expenses, and $0.1 million in amortization of intangibles offset by an increase of $0.2 million in start up costs related to the Company s Unifi Textiles (Suzhou) Company, Ltd. (UTSC) operation. SG&A expenses related to the Company s Brazilian operation decreased $0.5 million compared to the prior year period due to a decrease of $0.4 million related to the strengthening of the U.S. dollar against the Brazilian real and a decrease of $0.1 million in overall expenses.

During the second quarter of fiscal year 2008, the Company evaluated the carrying value of the remaining machinery and equipment at its Dillon, South Carolina facility. The Company sold several machines to a foreign subsidiary and also transferred several other machines to its Yadkinville, North Carolina facility. Five machines were scrapped for spare parts inventory. Six of the remaining machines were leased under an operating lease to a manufacturer in Mexico at a fair market value substantially less than their carrying value. These remaining machines were written down to the fair market value determined by the lease; and as a result, the Company recorded a non-cash impairment charge of $1.6 million in the second quarter of fiscal year 2008. The adjusted net book value will be depreciated over a two year period which is consistent with the life of the lease.

In addition, during the second quarter of fiscal year 2008, the Company began negotiations with a third party to sell the manufacturing facility located in Kinston, North Carolina. As a result of these negotiations, management concluded that the carrying value of the real estate exceeded its fair value. Accordingly, a $0.7 million non-cash impairment charge was recorded in the quarter ended December 23, 2007.

During the second quarter of fiscal year 2008, the Company evaluated the contract termination costs associated with the closure of its Kinston, North Carolina facility for the remainder of its current fiscal year. The Company accrued for unfavorable contract costs of $4.6 million related to site services that the Company was obligated to provide through June 2008.

In fiscal year 2004, the Company recorded restructuring charges of $5.7 million in lease related costs associated with the closure of its facility in Altamahaw, North Carolina. In the second quarter of fiscal year 2008, the Company evaluated its remaining obligation on the lease and as a result recorded a $0.4 million favorable adjustment.

During the second quarter of fiscal year 2009, the Company and YCFC renegotiated the proposed agreement to sell the Company s interest in YUFI to YCFC for $9.0 million, pending final negotiation and execution of definitive agreements and the receipt of Chinese regulatory approvals. As a result, the Company recorded an additional impairment charge of $1.5 million due to the decline in the value of its investment and other related assets. However, there can be no assurances that this transaction will occur upon these terms.

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Other (income) expense, net increased from $2.2 million in the second quarter of fiscal year 2008 to $5.2 million in the second quarter of fiscal year 2009. The following table shows the components of other (income) expense, net (amounts in thousands):

	For the Quarters Ended	
	December 28, 2008	December 23, 2007
Gain on sale of fixed assets	$ (5,594)	$ (1,271)
Gain from sale of nitrogen credits		(807)
Technology fee from China joint venture		(250)
Currency (gains) losses	380	131
Other, net	2	5
Other (income) expense, net	$ (5,212)	$ (2,192)

As a result of the discussions above, loss from continuing operations before income taxes was $8.7 million in the second quarter of fiscal year 2009 as compared to a loss of $13.6 million recorded in the same period of the prior year. The Company s income tax provision for the quarter ended December 28, 2008 resulted in tax expense at an effective rate of 7.1% as compared to the quarter ended December 23, 2007 which resulted in tax benefit at an effective rate of 42.3%. The primary differences between the Company s effective tax rate and the U.S. statutory rate for the quarter ended December 28, 2008 were attributable to state income tax benefits, foreign income being taxed at rates less than the U.S. statutory rate and an increase in the valuation allowance.

Deferred income taxes have been provided for the temporary differences between financial statement carrying amounts and the tax basis of existing assets and liabilities. The Company has continued to record a valuation allowance against its net domestic deferred tax assets, and certain foreign deferred tax assets related to net operating losses, as those net deferred tax assets are more likely than not to be unrealizable for income tax purposes. The valuation allowance increased $3.5 million in the quarter ended December 28, 2008 compared to a $1.7 million decrease in the quarter ended December 23, 2007. The net increase in the valuation allowance for the quarter ended December 28, 2008 primarily consisted of a $2.8 million increase for net operating losses generated this quarter (federal and state) and an increase of $0.7 million related to other temporary differences.

The income from discontinued operations for the second quarter of fiscal years 2009 and 2008 was primarily due to wind up activities and currency translation adjustments associated with the Ireland facility.

Polyester Operations

Polyester unit volumes decreased 32.7% for the quarter ended December 28, 2008, while average net selling prices increased 2.3% compared to the quarter ended December 23, 2007. Net sales for the polyester segment for the second quarter of fiscal year 2009 decreased by $41.1 million or 30.4% as compared to the same quarter in the prior year. Net sales of domestic polyester decreased by 29.2% primarily due to a decline in volume attributed to a reduction in merchant market sales of commodity POY stemming from shutting down the Kinston facility in October 2007 and to a reduction in polyester sales related to the slowdown in the retail apparel, automotive and home upholstery markets. The polyester price increases are attributable to an enriched mix due to a higher percentage of PVA sales, a lower percentage of POY sales, and increases in raw material pricing.

Sales in local currency for the Brazilian operation decreased by 15.8% for the quarter ended December 28, 2008 compared to the same quarter in the prior year primarily due to a decrease in unit volumes of 17.5% offset by an increase in average selling prices of 2.1%. The decrease in U.S. dollar net sales for the second quarter as compared to the prior year period includes a reduction of $7.0 million due to an increase in the Brazilian currency exchange rate.

In the second quarter of fiscal year 2009, the Company experienced a decline in its polyester business beginning in November 2008 which was attributable to market conditions previously discussed. Fiber costs for the polyester segment, excluding the Brazilian currency impact, decreased approximately 4.8% compared to the prior year second quarter primarily due to lower volumes which were offset by an increase in costs on a per-unit basis. Converting costs, excluding the Brazilian currency impact, decreased 49.0% primarily from lower sales volumes, the closure of the Kinston facility and management s efforts in controlling manufacturing costs. Gross profit for the polyester segment decreased $5.3 million in the second quarter of fiscal year 2009 which reflects these reductions in conversion margins and lower volumes.

SG&A expenses for the second quarter of fiscal year 2009 were $7.3 million compared to $10.2 million in the same quarter in the prior year. Refer to the discussion of SG&A in the quarter overview discussed above.

Nylon Operations

Nylon unit volumes decreased by 30.0% in the second quarter of fiscal year 2009 compared to the prior year quarter while average selling prices decreased by 4.2%. Net sales for the nylon segment for the second quarter of fiscal year 2009 decreased by $16.5 million or 34.2% as compared to the same quarter in the prior year. This decrease in net sales was primarily due to the slowdown in the retail apparel markets.

Total raw material costs decreased by 34.7% in the second quarter of fiscal year 2009 as compared to the prior year quarter as a result of the decreased volumes discussed above. Total converting costs for the nylon segment decreased by 34.1% in the same period as compared to the same quarter in the prior year reflecting lower depreciation expense in excess of higher other converting costs resulting in overall lower cost per unit. As a result, gross profit for the nylon segment decreased by $0.7 million for the second quarter of fiscal year 2009 over the prior year quarter.

SG&A expenses for the second quarter of fiscal year 2009 were $2.0 million compared to $1.8 million in the same quarter in the prior year. Refer to the discussion of SG&A in the quarter overview discussed above.

Corporate

During the first quarter of fiscal year 2007, the Company established the Unifi, Inc. Supplemental Key Employee Retirement Plan (the Plan). This Plan, which replaced a similar retirement plan, was established for the purpose of providing supplemental retirement benefits for a select group of management employees. In the second quarter of fiscal year 2009, the Company recognized $12 thousand of net expense related to the Plan s deferred compensation charges offset by its change in market value.

On July 26, 2006, the Compensation Committee (Committee) of the Board of Directors (Board) authorized the issuance of an additional 1,065,000 stock options to certain key employees from the 1999 Long-Term Incentive Plan. In addition, on October 24, 2007, the Committee authorized the issuance of approximately 1,570,000 stock options from the 1999 Long-Term Incentive Plan, of which 120,000 were issued to certain Board members and the remaining options were issued to certain key employees. On October 29, 2008, the shareholders of the Company approved the 2008 Unifi, Inc. Long-Term Incentive Plan (2008 Long-Term Incentive Plan). The plan authorized the issuance of up to 6,000,000 shares of Common Stock pursuant to the grant or exercise of stock options, including Incentive Stock Options (ISO), Non-Qualified Stock Options (NQSO) and restricted stock, but not more than 3,000,000 shares may be issued as restricted stock. Option

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awards are granted with an exercise price not less than the market price of the Company s stock at the date of grant. During the second quarter of fiscal year 2009, the Committee of the Board authorized the issuance of 280,000 stock options from the 2008 Long-Term Incentive Plan to certain key employees. As a result of these grants, the Company incurred $0.3 million of stock-based compensation charges in both the second quarters for fiscal years 2009 and 2008, which were recorded as SG&A expenses with the offset to additional paid-in-capital.

Review of Year-To-Date Fiscal Year 2009 compared to Year-To-Date Fiscal Year 2008

The following table sets forth the loss from continuing operations components for each of the Company s business segments for the year-to-date periods ended December 28, 2008 and December 23, 2007, respectively. The table also sets forth each of the segments net sales as a percent to total net sales, the net income (loss) components as a percent to total net sales and the percentage increase or decrease of such components over the comparable prior year period (amounts in thousands, except percentages):

	For the Six-Months Ended				
	December 28, 2008		December 23, 2007		
		% to Total		% to Total	% Change
Net sales					
Polyester	$ 216,963	73.6	$ 264,498	74.7	(18.0)
Nylon	77,773	26.4	89,407	25.3	(13.0)
Total	$ 294,736	100.0	$ 353,905	100.0	(16.7)
		% to Sales		% to Sales	
Gross profit					
Polyester	$ 8,729	2.9	$ 13,738	3.9	(36.5)
Nylon	7,008	2.4	5,575	1.5	25.7
Total	15,737	5.3	19,313	5.4	(18.5)
Selling, general and administrative expenses					
Polyester	15,654	5.3	22,576	6.4	(30.7)
Nylon	4,195	1.4	3,886	1.1	8.0
Total	19,849	6.7	26,462	7.5	(25.0)
Write down of long-lived assets and investment in unconsolidated affiliate					
Polyester			2,780	0.8	
Nylon					
Corporate	1,483	0.5	4,505	1.3	(67.1)
Total	1,483	0.5	7,285	2.1	(79.6)
Restructuring charges					
Polyester			6,619	1.8	
Nylon			218		
Total			6,837	1.8	
Other (income) expense, net	1,762	0.6	8,428	2.4	(79.1)

Loss from continuing operations before income taxes	(7,357)	(2.5)	(29,699)	(8.4)	(75.2)
Provision (benefit) for income taxes	2,499	0.8	(12,688)	(3.6)	(119.7)
Loss from continuing operations	(9,856)	(3.3)	(17,011)	(4.8)	(42.1)
Income from discontinued operations, net of tax	112		77		45.5
Net loss					