TAGLICH BROTHERS

MEMBER: FINRA, SIPC | WWW.TAGLICHBROTHERS.COM

# *Research Report – Update*

***Investors should consider this report as only a single factor in making their investment decision.***

# UFP Technologies, Inc.

**Rating: Speculative Buy**

John Nobile
December 22, 2011

## UFPT $15.06 — (NASDAQ CM)

| | 2009A | 2010A | 2011E | 2012E |
|---|---|---|---|---|
| Revenues (millions) | $99.2 | $120.8 | $129.1 | $138.4 |
| Earnings per share (diluted) | $0.94 | $1.37 | $1.44 | $1.65 |

| | | | |
|---|---|---|---|
| 52-Week range | $21.59 – $11.92 | Fiscal year ends: | December |
| Shares outstanding as of 11/1/11 | 6.5 million | Revenue per share (TTM) | $18.32 |
| Approximate float | 4.4 million | Price/Sales (TTM) | 0.8X |
| Market capitalization | $98 million | Price/Sales (2012)E | 0.8X |
| Tangible book value/share | $7.96 | Price/Earnings (TTM) | 10.1X |
| Price/tangible book | 1.9X | Price/Earnings (2012)E | 9.1X |

*UFP Technologies designs and manufactures high performance cushion packaging and molded fiber products and specialty foam and plastic products. These products are used as protection for fragile and valuable items, and are sold primarily to original equipment manufacturers in the computer, electronics, automotive, medical/pharmaceutical and industrial markets. (www.ufpt.com)*

***Key investment considerations:***

***Reiterate Speculative Buy rating on UFP Technologies (UFPT). Maintaining twelve-month price target of $18.00.***

***Growth is projected for UFPT's principal end markets (medical equipment, automotive, consumer electronics) driven by an aging population, increasing automotive demand, and innovative new electronics products.***

***Sales in the first nine months of 2011 increased 7%, down from 10% sales growth in 2010. The slowdown in growth was due to the loss of a significant portion of a long-term automotive program. However, the projected growth of the automotive industry should help to offset in part the lost sales from this program.***

***By our estimates, sales will grow at a slower rate in 2012 primarily due to slow economic growth.***

***Our profit forecasts for 2011 and 2012 are largely unchanged.***

***For 2011, we project revenue of $129.1 million and EPS of $1.44.***

***For 2012, we project revenue of $138.4 million and EPS of $1.65 per share.***

***UFPT reported Q3/11 sales increased 1% to $30.8 million while EPS was flat at $0.35. We estimated Q3/11 sales of $30.8 million and EPS of $0.31.***

***Please view our disclosures on pages 13 - 15.***

790 New York Avenue, Huntington, N.Y. 11743
(800) 383-8464 • Fax (631) 757-1333

### *Recommendation and Valuation*

We are reiterating our **Speculative Buy** rating on UFP Technologies and maintaining our **twelve-month price target of $18.00 per share.**

From 2004 to 2010, UFPT traded at an average earnings multiple of 12X. During that period, the stock's P/E ranged between 6X and 28X. We believe that with the growth we are projecting, the market will accord the stock a multiple of 11X. Applying a multiple of 11X to our 2012 earnings of $1.65 per share gives us a price target of approximately $18.00.

### *Recent Development*

In December 2011, UFP Technologies announced a new unified brand name. All of the company's product lines, including United Foam, Molded Fiber, Simco Automotive, United Case, and others, will now be marketed under the UFP Technologies brand name. The aim of establishing a single master brand name is providing a common identity across all markets, clarifying the relationships among diverse brands and business units, and making it easier for customers to do business with UFP Technologies.

### *Business*

UFP Technologies designs and manufactures engineered packaging solutions utilizing molded fiber, vacuum-formed plastics, and molded and fabricated foam plastic products. The company also designs and manufactures engineered component products using laminating, molding, and fabricating technologies. UFP sells mainly to the automotive, computer and electronics, medical, aerospace and defense, industrial, and consumer markets in the United States.

Sales of the company's components products were responsible for 67% of total sales in 2010 while packaging products comprised 33%. Since 2005, sales of component products have averaged annual growth of approximately 11% while packaging products have averaged annual growth of approximately 4% during that time frame. Judging by the magnitude of revenue changes generated by UFPT's principal end markets, we believe that approximately 35% of total sales are to the medical device industry for applications such as compression-molded foam finger splints, orthopedic foam components, and dental fluoride trays. We believe that UFPT's other end markets (automotive, defense, electronics, and industrial) each account for roughly 10% – 20% of the company's revenue.

The company's high-performance cushion packaging products are made primarily from polyethylene and polyurethane foams, and a wide range of sheet plastics. These products provide protection for fragile and valuable items, and are sold primarily to original equipment and component manufacturers. Molded fiber products are made primarily from 100% recycled paper principally derived from waste newspaper. These products are used for packaging high volume consumer goods, including computer components, medical devices, other light electronics, scented candles, and health and beauty products.

The cushion packaging market is characterized by three primary sectors: (1) custom fabricated or molded products for low volume, high fragility products; (2) molded or die-cut products for high volume, industrial and consumer goods; and (3) loose fill and commodity packaging materials for products that do not require custom-designed packaging. The company serves the low volume, high fragility market and the high volume industrial and consumer market with a range of materials and manufacturing capabilities.

In addition to packaging products, UFPT fabricates and molds component products made from cross-linked polyethylene foam (closed-cell foam characterized by a compact feel and resistance to water) and other materials. The company also laminates fabrics and other materials to cross-linked polyethylene foams, polyurethane foams and other substrates. UFPT's component products include automotive interior trim, athletic padding, industrial safety belts, components for medical equipment and devices, abrasive nail files and other beauty aids, anti-fatigue mats, and shock absorbing inserts used in athletic and leisure footwear.

Cross-linked foams have many advantages over traditional foams, including the ability to be thermoformed (molded), availability in vibrant colors, a fine cell structure providing improved esthetics and lower abrasiveness, and enhanced resistance to chemicals and ultraviolet light.  Certain grades of cross-linked foams can be radiation-sterilized and have been approved by the U.S. Food and Drug Administration for open wound skin contact.

The company differentiates itself is through the design and production of customized foam case inserts for the automotive, computers and electronics, medical, aerospace and defense, consumer, and industrial markets (see picture). Through a combination of materials, technology, and engineering, the company is able to produce unique case inserts for surgical instruments, customized repair kits, electronic parts, emergency response equipment, and many other applications.

***Industry Outlook***

IBISWorld forecasts the urethane and foam products industry growth of 4.2% in 2012.  The industries that UFP sells to are projected to show growth going forward.

Medical device sales are primarily dependent on demographics.  IBISWorld has observed that an aging population and technological advancements are among the top factors that should influence the medical device industry over the next five years.  Although the The Conference Board's Global Economic Outlook (November 2011) is suggesting global economic growth of approximately 3.2% in 2012, this is down from the 3.9% rate projected for 2011.  We believe this slower rate of growth could reduce the number of hi-value elective procedures involving medical devices, resulting in a slower growth rate for this industry.  In September 2011, IBISWorld forecasted the medical device industry to grow sales by an average annual rate of 6.4% to $82.1 billion during the five years to 2016.  This rate is slower than average annual rate of 16.4% over the five years to 2011.

The US automobile industry appears set for growth.  An article in Automotive News[1] reported that automotive demand is recovering faster than anticipated, with automakers headed toward their best annual performance in three years.  Consumers entered December 2011 demanding models ranging from big pickups to luxury sedans to fuel-sipping hybrids after pushing November's sales to the fastest monthly pace since the government's "cash for clunkers" trade-in program in August 2009.  The article said that US buyers were replacing their cars after delaying new-vehicle purchases as long as possible.  Further, the article cited data from The Conference Board showing consumer confidence surging in November by the most in more than eight years, and the portion of consumers planning to buy a new vehicle within six months climbing the highest since April 2011.  During the five years to 2016, IBISWorld expects industry revenue to rise 4.2% annually to $102.3 billion.

The consumer electronics industry has grown at an average annual rate of 5% from 2003 to 2006 but came to an abrupt halt in 2007 with the onset of the recession.  The economic downturn and subsequent declines in consumer spending have adversely affected consumer electronics demand and according to IBISWorld, is projected to decline at an average annual rate of 3.0% from 2007 to 2011.  However, the introduction of innovative new technologies (like tablet computers and 3D displays) should drive growth going forward.  In August 2011, IBISWorld projected this industry to show modest growth (1.3%) in 2011 after several years of declines. IBISWorld forecasted sales from US consumer electronics stores to grow at an average annual rate of approximately 3% to $93.3 billion during the six years to 2016.

[1] Automakers gain speed at year end as US shoppers return; December 5, 2011

Consumer Electronics Stores Revenue Outlook

| Year | Revenue $ million | Growth % |
|---|---|---|
| 2011 | 79,348.4 | 1.3 |
| 2012 | 81,252.8 | 2.4 |
| 2013 | 85,000.2 | 4.6 |
| 2014 | 87,935.2 | 3.5 |
| 2015 | 90,024.6 | 2.4 |
| 2016 | 91,750.3 | 1.9 |
| 2017 | 93,289.0 | 1.7 |

Source: IBISWorld

Growth is projected for the aerospace and defense industry. The latest forecast (January 2011) from the industry research firm Datamonitor projects the global aerospace and defense market to have a value of $1,190.5 billion in 2014, for a compound annual growth rate of approximately 5%.

### *Economic Outlook*

Most of UFPT's sales are to economically sensitive industries.

The November 2011 Global Economic Outlook from The Conference Board projected global economic growth to slow to 3.2% in 2012 from 3.9% in 2011. However, growth in the five years from 2012 to 2016 is projected to be roughly the same as the growth rate for 2006 to 2011 (3.5%).

Although global growth is projected to be down to 3.2% in 2012 from 3.9% in 2011, the forecast for the US economy shows an increasing growth rate. In December 2011, The Conference Board projected the US economy's growth rate to increase to 2.1% in 2012 from a 1.7% growth rate in 2011.

The Conference Board's latest US Leading Economic Index (LEI) and Consumer Confidence Index support its growth projections for the US economy. The Leading Economic Index increased in November 2011 following increases in October and September. The Conference Board said that the November increase in the LEI for the US suggests that the risk of an economic downturn has receded. However, this somewhat positive outlook for the domestic economy is at odds with a global economy that appears to be losing steam. The Conference Board said that a deeper-than-expected recession in Europe could derail the outlook for the US economy.

Although The Conference Board is projecting economic growth, there is still recent economic data being published that suggest the economy may still be struggling. The Federal Reserve said that US industrial production fell in November 2011 for the first time in seven months. International Monetary Fund (IMF) chief Christine Lagarde warned in December 2011 that the world economy is in a dangerous phase. Lagarde said that although the last forecast (September 2011) from the IMF saw global growth at four percent, today the growth outlook is much dimmer. Further, the advanced countries, especially in the Euro Area, are at the center of the crisis. Lagarde said that although Eurozone leaders have started to outline a solution, what is needed now is implementation.

As the company primarily sells its products in the US, a growing (albeit weak) US economy should increase (moderately) sales of the company's products in 2012.

### *Competition*

The packaging industry is highly competitive. Competition is based primarily on price, product performance, product reliability, and customer service. We believe the company's ability to custom design proprietary manufacturing equipment in conjunction with its machinery suppliers enables the company to effectively differentiate its products. For example, UFPT has custom-designed its own lamination machines allowing the company to achieve adhesive bonds between cross-linked foam and fabric and other materials that do not easily combine. These specialty laminates typically command higher prices than traditional foam products.

Some of UFPT's public competitors include Graphic Packaging, Packaging Corp. of America, Greif, Bemis Company, Smurfit-Stone Container, and Sealed Air Corp. As a group, UFPT's competitors grew revenues at an average rate of approximately 15% in 2010 versus 22% for UFPT.

## ***Projections***

*2011 Forecast*

Over the past five years, UFPT's sales have grown twice as fast as the packaging and containers industry. Sales for the first nine months of 2011 increased 7%, a growth rate we project for 2012 due to slow economic growth and the loss of a significant portion of a long-term automotive program that was responsible for 9% of 2010 sales. Revenue for 2012 will fall below the organic rate of 10% achieved in 2010.

For 2011, we project revenue of $129.1 million and net income of $10.1 million or $1.44 per share. We previously estimated revenue of $129.2 million and net income of $9.9 million or $1.41 per share. We increased our net income projection primarily due to a decrease in the effective tax rate stemming from the reversal of approximately $385,000 in reserves in Q3/11 that were previously established for uncertain tax benefits. We lowered gross margins to 28.8% from 29.2% due to the costs ($250,000 in Q3/11 and $100,000 estimated for Q4/11) associated with the closure and relocation of the company's Alabama operations. Our projections for 2011 include a $0.8 million gain from the sale of real estate in Alabama by an affiliated partnership. Of this gain, approximately $428,000 relates to non-controlling interests that have been deducted to determine net income attributable to UFPT.

SG&A expenses should increase to $22.0 million and SG&A margins should increase to 17.1% from 16.8% due to the development of enhanced internal operating and information systems which are responsible for approximately $0.5 million of the increase in SG&A expenses. We have lowered our tax rate projection to 33.6% (lower than the typical 37% rate) due to income from the company's noncontrolling interest in UDT that was not subject to corporate income tax and the reversal of tax reserves.

In 2011, we project $13.8 million cash from operations, cash earnings of $13.1 million and reductions in working capital of $0.7 million. We project $3.3 million of capital expenditures will be partially offset by $1.2 million proceeds from the sale of property, plant and equipment will result in $2.1 million cash used in investing. Financing activities consist primarily of $1.3 million principal repayments of long-term debt. We project an increase in cash of $10.0 million for a year-end cash balance of $34.4 million.

*2012 Forecast*

For 2012, we project revenue of $138.4 million and net income of $11.9 million or $1.65 per share.

We are increasing gross margins to 30.2% as higher sales volumes should increase overhead coverage and a greater percentage of total revenue (97% versus 94% in 2011) should come from higher margin non-automotive product sales. SG&A margin should decrease to 16.4% from 17.1% due to leverage of expenses. We are maintaining a tax rate projection of 37%.

In 2012, we project $15.3 million cash from operations, cash earnings of $16.1 million and increases in working capital of $0.8 million. We project 44 days sales outstanding in 2012 and inventory turnover of 11; both figures are in line with 2010 actual numbers and our 2011 estimates. We project $3.3 million of capital expenditures. Financing activities consist primarily of $0.8 million principal repayments of long-term debt. We project an increase in cash of $10.8 million for a year end cash balance of $45.2 million.

### *Q3 and Nine Months Financial Results*

For the third quarter sales increased 1% to $30.8 million. Net income was flat at $2.4 million or $0.35 per share.

We projected Q3/11 sales of $30.8 million and net income of $2.2 million or $0.31 per share.

The increase in sales was primarily due to a $0.7 million increase in sales to the medical industry as well as a $0.8 million increase in sales of molded fiber packaging. The increase in sales was partially offset by a $1.0 million decrease in sales to the automotive industry. Gross margins decreased to 27.6% from 29.2% due to increased overhead costs incurred from the closure and relocation of the company's Alabama operations of approximately $250,000 as well as $150,000 of compensation and benefits associated with increased engineering resources. The company did not give details as to why these specific costs were allocated to cost of sales. We believe the reason stems from employee severance and shutdown costs associated with the closure and relocation of the Alabama facility. Our research has found that some components of engineering and development costs can be allocated to cost of sales. Excluding these one-time items, Q3/11 gross margins would be 28.9% and operating margins would be 11.9%. SG&A expenses increased to $5.2 million from $5.1 million primarily due to IT spending and compensation increases.

The company showed a Q3/11 effective income tax rate of approximately 25% compared to an effective tax rate of 37% in Q3/10 due to the reversal of approximately $385,000 in reserves in Q3/11 that were previously established for uncertain tax benefits.

For the first nine months in 2011, revenue increased 7% to $95.8 million. Net income was $7.3 million or $1.05 per share versus net income of $6.2 million or $0.92 per share in the first nine months of 2010. The results for the first nine months of 2011 included a $0.8 million gain from the sale of real estate in Alabama by an affiliated partnership. Of this $0.8 million gain, approximately $428,000 relates to non-controlling interests that have been deducted to determine net income attributable to UFPT.

| | 9mos2010 | 9mos2011 |
|---|---|---|
| **Net sales** | **$ 89,126** | **$ 95,766** |
| Cost of sales | 63,716 | 68,477 |
| Gross profit | 25,410 | 27,289 |
| SG&A | 15,502 | 16,628 |
| Extraordinary items | (12) | (834) |
| Operating income | 9,920 | 11,495 |
| Interest expense, other income and expenses | (104) | (19) |
| Income before taxes | 9,816 | 11,476 |
| Income tax | 3,617 | 3,701 |
| Income attributable to noncontrol. interests | (41) | (433) |
| **Net Income / (Loss)** | **$ 6,158** | **$ 7,342** |
| **Diluted EPS** | **$ 0.92** | **$ 1.05** |
| Diluted Shares Outstanding | 6,728 | 6,985 |
| Margin Analysis | | |
| Gross margin | 28.5% | 28.5% |
| SG&A | 17.4% | 17.4% |
| Operating margin | 11.1% | 12.0% |

The increase in sales for the nine month period was primarily due to a $4.0 million increase to the automotive industry as well as a $1.6 million increase in sales to the defense and aerospace industry. The increase in sales was partially offset by a $0.6 million decrease in sales to the medical industry due to the loss of a portion of a large medical account in the second half of 2010. Gross margins remained flat at 28.5%. SG&A expenses increased to $16.6 million from $15.5 million primarily due to a $0.5 million increase in professional fees and a $0.3 million increase in salaries.

The company showed an effective income tax rate of approximately 32% in the nine months of 2011 versus 37% in the nine months of 2010 due to the reversal of approximately $385,000 in reserves in 2011 that were previously established for uncertain tax benefits.

*Liquidity*

The company has a strong balance sheet. Long-term debt is $5.8 million (for a debt/equity ratio of 0.1 versus 1.0 for the industry) and cash (approximately $4.70 per share) exceeds all indebtedness and liabilities.

Cash of $9.2 million from operations for the nine month period consisted mainly of cash earnings of $9.4 million offset by increases in working capital of $0.2 million due primarily to increased receivables and inventory offset in part by increased accounts payable and lower taxes receivable. Capital expenditures of $2.6 million and proceeds of $1.2 million from the sale of fixed assets resulted in $1.4 million cash used in investing activities. Long-term debt principal payments of $1.1 million and $0.8 million payment of statutory withholdings for stock options accounted for most of the cash used in financing activities. The net result was a $6.2 million net increase in cash for a balance of $30.7 million as of September 30, 2011.

UFPT's available bank credit facilities are as follows: a $17 million revolving line of credit, a $2.1 million term loan with seven-year straight-line amortization, a $1.8 million term loan with 20-year straight-line amortization, and a $4.0 million term loan with 20-year straight-line amortization.

As of September 30, 2011, the company had approximately $16.7 million available on its revolving line of credit based upon available collateral. The credit facility bears interest at LIBOR plus 1.0% to 1.5% or, the bank's prime rate less a margin that ranges from 0.25% to zero. In both cases the applicable margin is dependent upon company performance. The company's $17 million revolving credit facility is due November 30, 2013; the term loans are all due on January 29, 2016. Under the credit facility, the company is subject to a minimum fixed-charge coverage financial covenant which the company was in compliance with at September 30, 2011. The interest rate on these facilities was 1.2% at September 30, 2011.

## ***Risks***

In our view, these are the principal risks underlying the stock:

<u>Dependence on a small number of customers</u>
The company's top ten customers represented approximately 31% of total revenues in 2010. A single automotive program accounted for approximately 9% of total sales in 2010. Approximately 2/3 of this program is scheduled to phase out beginning in Q3/11.

<u>Environmental Considerations</u>
Future government action may impose restrictions affecting the industry in which the company operates. There can be no assurance that any such action will not adversely impact UFP Technologies.

<u>Economic conditions</u>
Poor economic conditions could negatively impact sales of the company's packaging customers.

<u>Competition</u>
The packaging and component products industries are highly competitive. The company's primary competition for its packaging products has been from smaller independent regional manufacturers. UFPT's component products face competition from smaller companies that typically concentrate on production of component products for specific industries.

<u>Liquidity</u>
With only 6.5 million shares outstanding and 4.4 million in the float, liquidity issues must be considered. Average daily volume has been approximately 12,000 shares. Any significant trading in shares of UFPT could result in large swings in the price of the stock.

Miscellaneous

The company's financial results and equity values are subject to other risks and uncertainties including competition, operations, financial markets, regulatory risk, and/or other events. These risks may cause actual results to differ from expected results.

## Balance Sheet for the Periods Ended
(in thousands $)

| | 2008A | 2009A | 2010A | 9/11A | 2011E | 2012E |
|---|---|---|---|---|---|---|
| Cash and cash equivalents | 6,729 | 14,999 | 24,434 | 30,659 | 34,422 | 45,175 |
| Receivables | 12,755 | 14,218 | 14,634 | 15,115 | 15,651 | 16,765 |
| Inventories | 8,153 | 7,647 | 8,044 | 9,006 | 8,536 | 9,007 |
| Prepaid expenses | 516 | 476 | 1,035 | 773 | 1,128 | 1,200 |
| Refundable income taxes | - | - | 1,414 | 855 | - | - |
| Deferred income taxes | 1,489 | 1,411 | 1,209 | 1,187 | 1,000 | 1,200 |
| Total current assets | 29,642 | 38,751 | 50,770 | 57,595 | 60,737 | 73,347 |
| Net property, plant and equipment | 11,754 | 12,218 | 12,575 | 13,012 | 13,075 | 13,575 |
| Deferred income taxes | - | - | - | - | - | - |
| Goodwill | 6,481 | 6,481 | 6,481 | 6,481 | 6,481 | 6,481 |
| Other assets | 846 | 2,002 | 1,983 | 1,758 | 2,000 | 2,000 |
| **Total assets** | **48,723** | **59,452** | **71,809** | **78,846** | **82,293** | **95,403** |
| | | | | | | |
| Current portion of long-term debt | 717 | 623 | 654 | 581 | 600 | 600 |
| Current portion of capital lease obligations | 703 | - | - | - | - | - |
| Accounts payable | 3,304 | 4,274 | 5,169 | 5,657 | 5,485 | 5,788 |
| Accrued taxes and other expenses | 6,230 | 6,153 | 6,679 | 6,226 | 7,143 | 7,651 |
| Total current liabilities | 10,954 | 11,050 | 12,502 | 12,464 | 13,228 | 14,039 |
| Long-term debt | 3,942 | 7,502 | 6,847 | 5,784 | 5,620 | 4,820 |
| Capital lease obligations | 910 | - | - | - | - | - |
| Minority interest | 523 | - | - | - | - | - |
| Deferred income taxes | 113 | 777 | 881 | 852 | 1,100 | 1,350 |
| Other liabilities | 914 | 1,118 | 1,353 | 1,295 | 1,474 | 1,500 |
| **Total liabilities** | **17,356** | **20,447** | **21,583** | **20,395** | **21,422** | **21,709** |
| **Total stockholders' equity** | **31,367** | **39,005** | **50,226** | **58,451** | **60,871** | **73,693** |
| **Total liabilities & stockholders' equity** | **48,723** | **59,452** | **71,809** | **78,846** | **82,293** | **95,403** |

Source: Company filings and Taglich Brothers' estimates

Annual Income Statements for the Years Ended
(in thousands $)

| | 2008A | 2009A | 2010A | 2011E | 2012E |
|---|---|---|---|---|---|
| Net sales | 110,032 | 99,231 | 120,766 | 129,117 | 138,350 |
| Cost of sales | 81,469 | 72,512 | 86,150 | 91,990 | 96,562 |
| Gross profit | 28,563 | 26,719 | 34,616 | 37,127 | 41,788 |
| | | | | | |
| Extraordinary items | 1,315 | - | - | (834) | - |
| SG&A | 18,823 | 18,539 | 20,236 | 22,032 | 22,750 |
| Operating income | 8,425 | 8,180 | 14,380 | 15,929 | 19,038 |
| | | | | | |
| Interest exp, other inc and exp | (314) | 618 | 46 | (1) | 60 |
| Income before taxes | 8,111 | 8,798 | 14,426 | 15,928 | 19,098 |
| Income tax | 2,995 | 2,817 | 5,019 | 5,349 | 7,066 |
| | | | | | |
| Income attrib. to noncontrol. interests | - | (52) | (160) | (472) | (160) |
| Net Income / (Loss) | 5,116 | 5,929 | 9,247 | 10,108 | 11,872 |
| EPS | 0.82 | 0.94 | 1.37 | 1.44 | 1.65 |
| Shares Outstanding | 6,263 | 6,294 | 6,757 | 7,000 | 7,175 |
| | | | | | |
| Margin Analysis | | | | | |
| Gross margin | 26.0% | 26.9% | 28.7% | 28.8% | 30.2% |
| SG&A | 17.1% | 18.7% | 16.8% | 17.1% | 16.4% |
| Operating margin | 7.7% | 8.2% | 11.9% | 12.3% | 13.8% |
| Tax rate | 36.9% | 32.0% | 34.8% | 33.6% | 37.0% |
| | | | | | |
| Year / Year Growth | | | | | |
| Total Revenues | 17.6% | (9.8%) | 21.7% | 6.9% | 7.2% |
| Net Income | 23.0% | 15.9% | 56.0% | 9.3% | 17.5% |
| EPS | 15.1% | 15.3% | 45.3% | 5.5% | 14.6% |

Source: Company filings and Taglich Brothers' estimates

## Quarterly Income Statement for the Fiscal Years Ending December 31, 2010, 2011, and 2012
(in thousands $)

| | 3/10A | 6/10A | 9/10A | 12/10A | 2010A | 3/11A | 6/11A | 9/11A | 12/11E | 2011E | 3/12E | 6/12E | 9/12E | 12/12E | 2012E |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Net sales | 28,700 | 29,957 | 30,468 | 31,640 | 120,766 | 31,504 | 33,501 | 30,762 | 33,350 | 129,117 | 32,500 | 35,300 | 33,900 | 36,650 | 138,350 |
| Cost of sales | 21,243 | 20,911 | 21,562 | 22,434 | 86,150 | 22,702 | 23,498 | 22,278 | 23,512 | 91,990 | 23,010 | 24,534 | 23,730 | 25,289 | 96,562 |
| Gross profit | 7,457 | 9,046 | 8,906 | 9,206 | 34,616 | 8,802 | 10,003 | 8,484 | 9,838 | 37,127 | 9,490 | 10,767 | 10,170 | 11,362 | 41,788 |
| | | | | | | | | | | | | | | | |
| Extraordinary items | - | - | - | - | - | (834) | - | - | - | (834) | - | - | - | - | - |
| SG&A | 5,012 | 5,387 | 5,103 | 4,734 | 20,236 | 5,726 | 5,686 | 5,220 | 5,400 | 22,032 | 5,650 | 5,675 | 5,700 | 5,725 | 22,750 |
| Operating income | 2,445 | 3,659 | 3,803 | 4,472 | 14,380 | 3,910 | 4,317 | 3,264 | 4,438 | 15,929 | 3,840 | 5,092 | 4,470 | 5,637 | 19,038 |
| | | | | | | | | | | | | | | | |
| Interest exp, other inc and exp | (35) | (22) | (35) | 139 | 46 | 2 | (12) | (6) | 15 | (1) | 15 | 15 | 15 | 15 | 60 |
| Income before taxes | 2,410 | 3,637 | 3,768 | 4,611 | 14,426 | 3,912 | 4,305 | 3,258 | 4,453 | 15,928 | 3,855 | 5,107 | 4,485 | 5,652 | 19,098 |
| Income tax | 888 | 1,339 | 1,389 | 1,403 | 5,019 | 1,279 | 1,603 | 819 | 1,648 | 5,349 | 1,426 | 1,889 | 1,659 | 2,091 | 7,066 |
| | | | | | | | | | | | | | | | |
| Income attrib. to noncontrol. interests | (11) | (16) | (14) | (119) | (160) | (428) | - | (4) | (40) | (472) | (40) | (40) | (40) | (40) | (160) |
| Net Income / (Loss) | 1,511 | 2,282 | 2,365 | 3,089 | 9,247 | 2,205 | 2,702 | 2,435 | 2,766 | 10,108 | 2,389 | 3,177 | 2,786 | 3,520 | 11,872 |
| EPS | 0.23 | 0.34 | 0.35 | 0.45 | 1.37 | 0.32 | 0.39 | 0.35 | 0.39 | 1.44 | 0.34 | 0.44 | 0.39 | 0.49 | 1.65 |
| Shares Outstanding | 6,642 | 6,725 | 6,785 | 6,875 | 6,757 | 6,969 | 6,982 | 6,999 | 7,050 | 7,000 | 7,100 | 7,150 | 7,200 | 7,250 | 7,175 |
| | | | | | | | | | | | | | | | |
| Margin Analysis | | | | | | | | | | | | | | | |
| Gross margin | 26.0% | 30.2% | 29.2% | 29.1% | 28.7% | 27.9% | 29.9% | 27.6% | 29.5% | 28.8% | 29.2% | 30.5% | 30.0% | 31.0% | 30.2% |
| SG&A | 17.5% | 18.0% | 16.7% | 15.0% | 16.8% | 18.2% | 17.0% | 17.0% | 16.2% | 17.1% | 17.4% | 16.1% | 16.8% | 15.6% | 16.4% |
| Operating margin | 8.5% | 12.2% | 12.5% | 14.1% | 11.9% | 12.4% | 12.9% | 10.6% | 13.3% | 12.3% | 11.8% | 14.4% | 13.2% | 15.4% | 13.8% |
| Tax rate | 36.8% | 36.8% | 36.9% | 30.4% | 34.8% | 32.7% | 37.2% | 25.1% | 37.0% | 33.6% | 37.0% | 37.0% | 37.0% | 37.0% | 37.0% |
| | | | | | | | | | | | | | | | |
| Year / Year Growth | | | | | | | | | | | | | | | |
| Total Revenues | 32.8% | 42.9% | 10.3% | 8.9% | 21.7% | 9.8% | 11.8% | 1.0% | 5.4% | 6.9% | 3.2% | 5.4% | 10.2% | 9.9% | 7.2% |
| Net Income | 338.0% | 303.2% | 12.0% | 6.3% | 56.0% | 45.9% | 18.4% | 3.0% | (10.5%) | 9.3% | 8.3% | 17.6% | 14.4% | 27.3% | 17.5% |
| EPS | 305.7% | 271.2% | 4.0% | 0.5% | 45.3% | 39.1% | 14.0% | (0.2%) | (12.7%) | 5.5% | 6.3% | 14.8% | 11.2% | 23.8% | 14.6% |

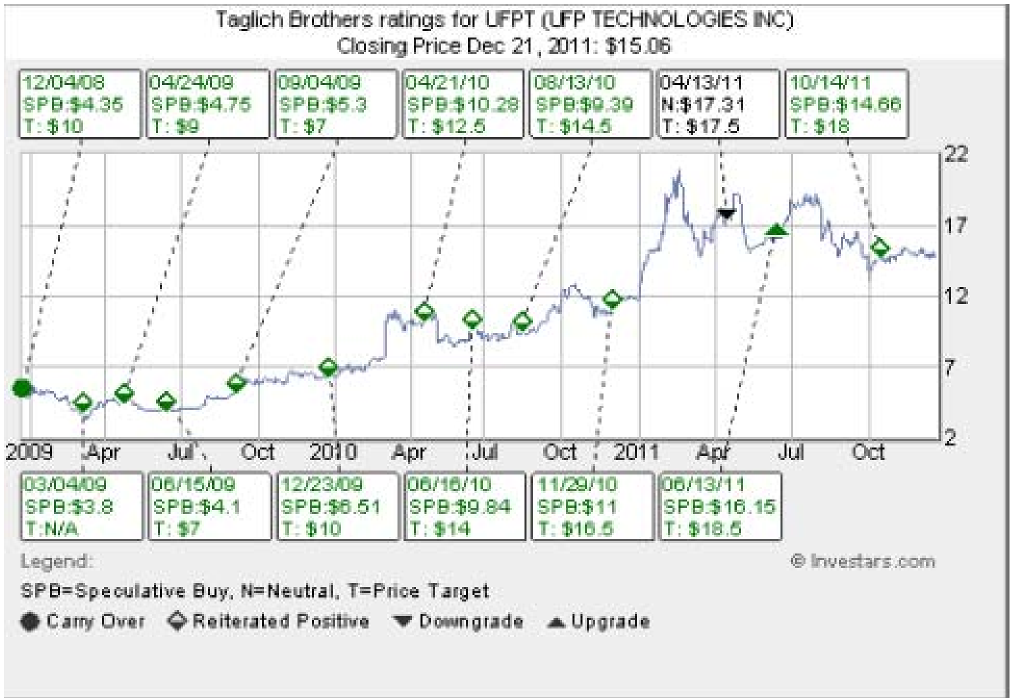
Source: Company filings and Taglich Brothers' estimates

## Statement of Cash Flows for the Periods Ended
(in thousands $)

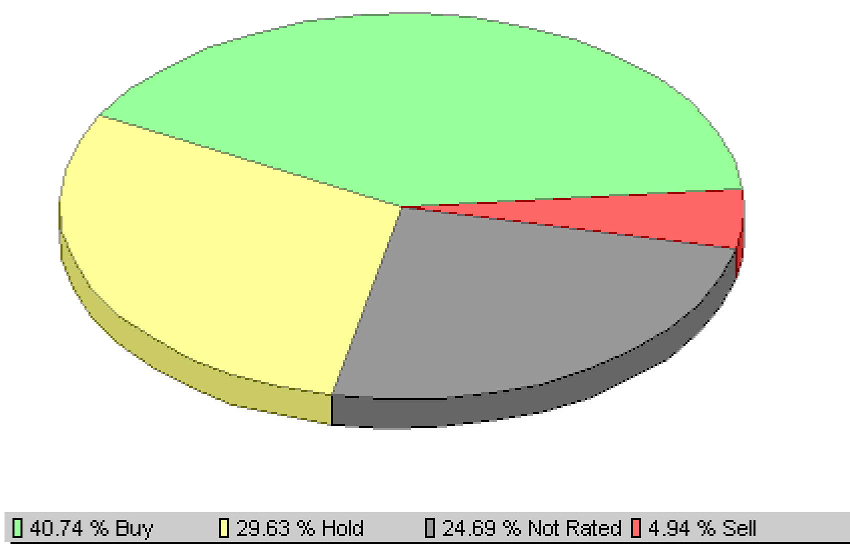
| | 2008A | 2009A | 2010A | 9mos11A | 2011E | 2012E |
|---|---|---|---|---|---|---|
| Net income | 5,116 | 5,982 | 9,407 | 7,775 | 10,108 | 11,872 |
| Depreciation & amortization | 2,977 | 2,895 | 3,152 | 1,982 | 2,800 | 2,800 |
| Restructuring leasehold improvement write-off | 170 | - | - | - | - | - |
| Equity in net income of unconsolidated affiliate | (7) | - | - | - | - | - |
| Minority interest | 44 | - | - | - | - | - |
| Gain on acquisition | - | (840) | - | - | - | - |
| (Gain) loss on disposal of property, plant and equipment | (57) | (11) | (12) | (834) | (834) | - |
| Share-based compensation | 1,306 | 901 | 964 | 860 | 1,200 | 1,200 |
| Stock issued in lieu of compensation | 344 | 184 | 79 | 55 | 100 | 100 |
| Excess tax benefit on share-based compensation | | | | (419) | (419) | |
| Deferred income taxes | 16 | 227 | 306 | (7) | 100 | 100 |
| *Changes in assets and liabilities* | | | | | | |
| Receivables | 777 | (342) | (415) | (482) | (1,017) | (1,114) |
| Inventories | (435) | 1,863 | (397) | (962) | (492) | (471) |
| Prepaid expenses | 350 | 73 | (559) | 262 | (93) | (72) |
| Refundable income taxes | - | - | (1,414) | 560 | 1,414 | - |
| Accounts payable | (2,777) | 393 | 895 | 488 | 316 | 303 |
| Accrued expenses and other | (937) | (331) | 527 | (33) | 464 | 509 |
| Retirement and other liabilites | (119) | 204 | 234 | (58) | 121 | 26 |
| Other assets | (83) | (509) | (205) | 61 | (17) | - |
| **Net Cash Provided by Operations** | **6,685** | **10,689** | **12,562** | **9,248** | **13,751** | **15,252** |
| | | | | | | |
| Additions to property, plant and equipment | (2,763) | (1,857) | (3,286) | (2,638) | (3,300) | (3,300) |
| Cash surrender value of officers' life insurane | (15) | - | - | - | - | - |
| Payments from affiliated company | 7 | - | - | - | - | - |
| Proceeds from sale of property, plant and equipment | 101 | 13 | 12 | 1,217 | 1,217 | - |
| Acquisitions | (5,181) | (2,435) | - | - | - | - |
| **Net Cash Used in Investing** | **(7,851)** | **(4,279)** | **(3,274)** | **(1,421)** | **(2,083)** | **(3,300)** |
| | | | | | | |
| Borrowings (payments) of notes payable | - | - | - | - | - | - |
| Proceeds from long-term borrowings | - | 4,000 | - | - | - | - |
| Distribution to United Development Company partners | (105) | (105) | (105) | (289) | (289) | (289) |
| Tax benefit from exercise of non-qualified stock options | 211 | 23 | 854 | 420 | 420 | 420 |
| Net proceeds from sale of common stock | 20 | - | - | - | - | - |
| Proceeds from exercise of stock options | 333 | 130 | 507 | 234 | 300 | 300 |
| Payment of statutory witholdings for stock options exercised | - | - | (485) | (830) | (830) | (830) |
| Principal repayments of long-term debt | (714) | (577) | (624) | (1,137) | (1,281) | (800) |
| Principle repayments of capital lease obligations | (704) | (1,612) | - | - | - | - |
| Proceeds from refinancing capital leases | - | - | - | - | - | - |
| Cash settlement of restricted stock units | (206) | - | - | - | - | - |
| **Net Cash Provided by (Used in) Financing** | **(1,165)** | **1,859** | **147** | **(1,602)** | **(1,680)** | **(1,199)** |
| **Net Change in Cash** | **(2,331)** | **8,269** | **9,435** | **6,225** | **9,988** | **10,753** |
| **Cash - Beginning of Period** | **9,060** | **6,729** | **14,999** | **24,434** | **24,434** | **34,422** |
| **Cash - End of Period** | **6,729** | **14,999** | **24,434** | **30,659** | **34,422** | **45,175** |
| | | | | | | |
| Cash Flow from Operations | 6,685 | 10,689 | 12,562 | 9,248 | 13,751 | 15,252 |
| Capital Expenditures | (2,763) | (1,857) | (3,286) | (2,638) | (3,300) | (3,300) |
| Free Cash Flow | 3,922 | 8,832 | 9,276 | 6,610 | 10,451 | 11,952 |

Source: Company filings and Taglich Brothers' estimates

## Price Chart




## Taglich Brothers' Current Ratings Distribution




**Investment Banking Services for Companies Covered in the Past 12 Months**

| Rating | # | % |
|---|---|---|
| Buy | | |
| Hold | None | |
| Sell | | |
| Not Rated | | |

## Important Disclosures

As of the date of this report, we, our affiliates, any officer, director or stockholder, or any member of their families do not have a position in the stock of the company mentioned in this report. Taglich Brothers, Inc. does not currently have an Investment Banking relationship with the company mentioned in this report and was not a manager or co-manager of any offering for the company within the last three years.

All research issued by Taglich Brothers, Inc. is based on public information. Since February 2000, the company has paid a monthly monetary fee of $1,000 (USD) to Taglich Brothers, Inc. for the creation and dissemination of research reports.

## General Disclosures

The information and statistical data contained herein have been obtained from sources, which we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to changes in figures or our views. This is not a solicitation of any order to buy or sell. Taglich Brothers, Inc. is fully disclosed with its clearing firm, Pershing, LLC, is not a market maker and does not sell to or buy from customers on a principal basis. The above statement is the opinion of Taglich Brothers, Inc. and is not a guarantee that the target price for the stock will be met or that predicted business results for the company will occur. There may be instances when fundamental, technical and quantitative opinions contained in this report are not in concert. We, our affiliates, any officer, director or stockholder or any member of their families may from time to time purchase or sell any of the above-mentioned or related securities. Analysts and members of the Research Department are prohibited from buying or selling securities issued by the companies that Taglich Brothers, Inc. has a research relationship with, except if ownership of such securities was prior to the start of such relationship, then an Analyst or member of the Research Department may sell such securities after obtaining expressed written permission from Compliance.

## Analyst Certification

**I, John Nobile, the research analyst of this report, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities and issuers; and that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this report.**

## Public Companies Mentioned in this Report

Graphic Packaging (NYSE: GPK)
Packaging Corp. of America (NYSE: PKG)
Greif (NYSE: GEF)
Bemis Company (NYSE: BMS)
Smurfit-Stone Container (NYSE: SSCC)
Sealed Air Corp. (NYSE: SEE)

## Meaning of Ratings

*Buy*

We believe the company is undervalued relative to its market and peers. We believe its risk reward ratio strongly advocates purchase of the stock relative to other stocks in the marketplace. Remember, with all equities there is always downside risk.

*Speculative Buy*

We believe that the long run prospects of the company are positive. We believe its risk reward ratio advocates purchase of the stock. We feel the investment risk is higher than our typical “buy” recommendation. In the short run, the stock may be subject to high volatility and continue to trade at a discount to its market.

*Neutral*

We will remain neutral pending certain developments.

*Underperform*

We believe that the company may be fairly valued based on its current status. Upside potential is limited relative to investment risk.

*Sell*

We believe that the company is significantly overvalued based on its current status. The future of the company's operations may be questionable and there is an extreme level of investment risk relative to reward.

*Dropping Coverage*

We have discontinued research coverage of the company due to termination of research services, non-payment for such services or departure of the analyst.

**Some notable Risks within the Microcap Market**

**Stocks in the Microcap segment of the market have many risks that are not as prevalent in Large-cap, Blue Chips or even Small-cap stocks. Often it is these risks that cause Microcap stocks to trade at discounts to their peers. The most common of these risks is liquidity risk, which is typically caused by small trading floats and very low trading volume which can lead to large spreads and high volatility in stock price. In addition, Microcaps tend to have significant company specific risks that contribute to lower valuations. Investors need to be aware of the higher probability of financial default and higher degree of financial distress inherent in the microcap segment of the market.**

---

From time to time our analysts may choose to withhold or suspend a rating on a company. We continue to publish informational reports on such companies; however, they have no ratings or price targets. In general, we will not rate any company that has too much business or financial uncertainty for our analysts to form an investment conclusion, or that is currently in the process of being acquired.