

Taglich Brothers, Inc.

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Research Report - Update

UFP Technologies, Inc.

Rating: Speculative Buy

UFPT \$1.75 — (NASDAQ SC)

John Nobile
May 21, 2001

	FYE (1999)	FYE (2000)	FYE (2001)E	FYE (2002)E
Revenues (millions)	\$58.8	\$74.5	\$71.6	\$77.0
Earnings per share (diluted)	\$0.35	\$0.25	\$0.06	\$0.15

52week range	\$1.25 – \$3.06	Fiscal year ends:	December
Shares outstanding (millions)	4.2	Revenue per share (TTM)	\$16.48
Trading float (millions)	2.4	Price/Sales (TTM)	0.11X
Insider Ownership	70%	Price/Sales (2002)	0.10X
Book value/share	\$3.99	Price/Earnings (TTM)	15.0X
Price/Book	0.45X	Price/Earnings (2002)	11.7X

UFP Technologies is a designer and manufacturer of a broad range of high performance cushion foam and molded fiber products, and specialty foam and plastic products for the industrial and consumer markets. These products are custom designed and fabricated or molded to provide protection for fragile and valuable items, and are sold primarily to original equipment manufacturers in the computer, electronics, telecommunications, industrial, medical and pharmaceutical markets.

www.ufpt.com

Key investment considerations:

- *We are maintaining our speculative buy rating for shares of UFP Technologies (UFPT) with an 18-month price target of \$2.75 per share.*
- *UFP Technologies posted a loss for the first quarter of 2001 primarily due to the current slowdown in the automotive industry and the loss of a major automotive program. For the quarter, net sales decreased 7% to \$17.0 million from \$18.3 million in 2000. Net loss was \$368,000 or \$(0.08) per share versus net income of \$218,000 or \$0.05 per share in 2000.*
- *Industry and economic conditions are expected to improve and we believe UFP Technologies will remain profitable this year and expect revenues to gradually improve from the third quarter on.*
- *For 2001, we estimate sales will decrease 4% to \$71.6 million and net earnings will decrease 77% to \$241,000 or \$0.06 per share. For 2002, we estimate sales will increase 8% to \$77 million and net earnings will increase 174% to \$663,000 or \$0.15 per share over 2001 levels.*

**Please view our disclaimer located at the end of the text portion of this report.*

Recent Financial Results

For the three month period ended March 31, 2001, versus the same period in 2000:

- Net sales decreased 7% to \$17.0 million from \$18.3 million.
- Net loss was \$368,000 or \$(0.08) per share versus net income of \$218,000 or \$0.05 per share.

The decrease in net sales was primarily related to a slowdown in the automotive industry as well as the loss of a large customer that brought a \$5.5 million program in-house. The loss of this customer resulted in specialty product sales to decline 17% in the quarter to \$8.4 million from \$10.1 million during the same period a year earlier. Helping to offset the decline was a 5% increase in packaging sales for the quarter to \$8.7 million from \$8.2 million during the same period a year earlier. Gross margin decreased to 20.0% from 23.5% primarily due to costs associated with consolidating and moving the Company's plants in Detroit and California as well as declining sales in the Company's Detroit location. Despite the net loss for the quarter, EBITDA remained positive at \$389,000.

During the first quarter, UFP Technologies completed the consolidation of two Detroit area facilities into one more efficient facility, and relocated the Gilroy, California, plant to Visalia, California, where labor and real estate costs are much lower. The Company believes these moves will help to position the Company for long-term success and added that they have not cut resources critical to the Company's growth plans. Management believes these steps, combined with new programs scheduled to come on line throughout the year, will return the Company to profitability and reestablish a trend of profitable growth.

Cash and cash equivalents decreased by \$30,000 over the three-month period. Cash used by operations was \$1.5 million primarily from a \$1.1 million decrease in accounts payable, a \$500,000 decrease in accrued expenses and a net loss of \$400,000, partially offset by \$800,000 in depreciation and amortization. Cash used in investing was \$800,000 primarily from additions to property, plant and equipment. Cash provided by financing was \$2.3 million primarily due to a \$2.9 million increase in notes payable offset by a \$500,000 stock repurchase.

The Company has an \$8.0 million revolving bank loan facility, of which \$7.6 million was outstanding on March 31, 2001 and a \$10 million acquisition line of credit of which \$7.8 million was outstanding at March 31, 2001. The current portion of total debt is approximately \$9.3 million. The Company has no significant capital commitments, but plans on investing in capital equipment to support its operations. UFP Technologies believes that its existing resources will be sufficient to meet its cash requirements through at least the next twelve months.

Outlook

Although fiscal 2001 started off with a loss for UFP Technologies, we believe the Company will be profitable for the full year. Weak economic conditions in the automotive industry, as well as the loss of a major automotive program, have put a damper on a significant portion of current and future revenues. Also, computer/electronics packaging customers have reduced their requirements considerably during the quarter. This is no surprise as the high tech sector has been showing negative growth since the beginning of the year. However, as industry and economic conditions are expected to improve, we believe UFP Technologies will remain profitable this year and expect revenues to gradually improve from the third quarter on.

Along with the weak near-term outlook for the automotive division, which makes up approximately 15% of total revenues, the near-term outlook for the packaging side of the business, which makes up the remaining 85% of total revenues, also looks weak. With the current weakness in the U.S. economy, manufacturers are producing and selling less, directly affecting the companies that produce the material needed to package and protect their products. According to First Call, overall industry projections call for a decline in earnings of 31% in 2001. However, for 2002, industry earnings are projected to increase by over 67%. Also, the automotive industry is expected to show signs of improvement starting in the latter half of 2001.

Taking into account the industry projections, the loss of a major automotive program, and that UFP Technologies' sales and earnings for the past five years have grown at a rate approximately 50% higher than the overall industry, we estimate 2001 revenues will decline 4% to \$71.6 million and net income will decline 77% to \$242,000 or \$0.06 per share. For 2002, we estimate sales will increase 8% to \$77 million and net earnings will increase 174% to \$663,000 thousand or \$0.15 per share. The large swing in earnings from year to year can be attributed to the loss in the first half of 2001, with results gradually improving from the third quarter on. Applying the current Price/Earnings multiple of 15X to our projection of \$0.15 earnings per share for 2002, we arrive at an 18-month price target of \$2.25 per share.

In addition, we used a discounted cash flow model using EBITDA as a proxy for cash flow and derived a discount rate of 9.42% using the Capital Asset Pricing Model. This model values shares of UFPT at a price of \$3.25. Averaging these two valuation models puts our anticipated eighteen-month price target for shares of UFPT at \$2.75.

Other Considerations

Competition-

The packaging and specialty foam products industry is highly competitive. The Company's foam and fiber packaging products compete against other alternative products made from materials such as expanded polystyrene foams, die-cut corrugated, plastic peanuts, plastic bubbles and foam-in-place urethane. UFP Technologies also faces competition in the specialty foam products area from smaller companies that typically concentrate on production for specific industries.

Capital resources-

With only \$64,000 in cash as of March 31, 2001 along with the lack of operating income in the first quarter, the ability to raise additional capital is a concern. As mentioned above, the Company has an \$8.0 million revolving bank loan facility, of which \$7.6 million was outstanding on March 31, 2001. Because of the limited funding available on this bank loan, and no assurance of additional financing, shares of UFP Technologies are recommended only for investors who can take on above-average risk.

Liquidity concerns-

With only 4.2 million shares outstanding and 2.4 million in the float, liquidity issues must be considered. Average daily volume is less than 3,000 shares and there are many days when the stock does not trade at all. Any significant trading in shares of UFPT could result in large swings in the price of the stock.

Conclusion

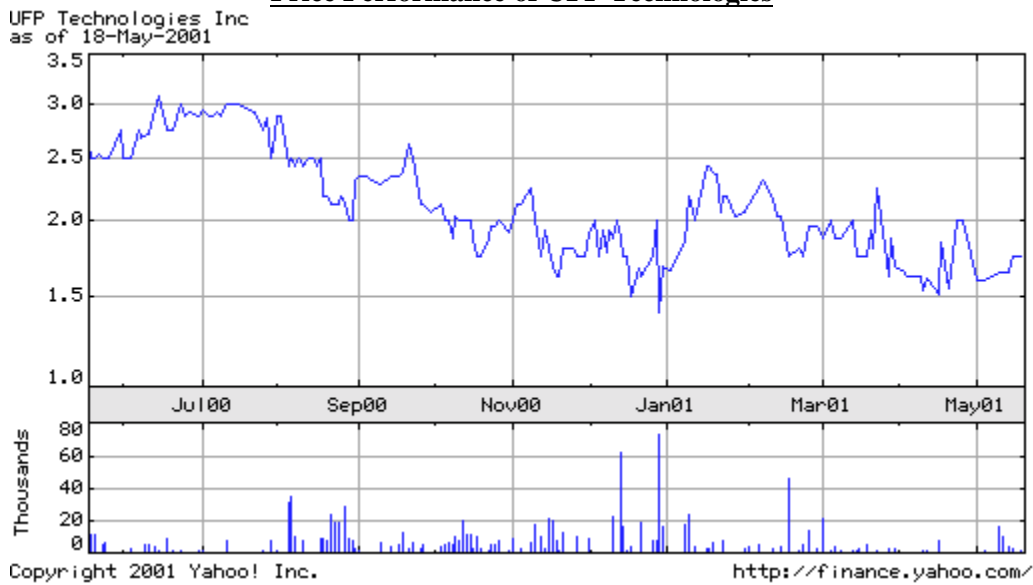
We reiterate our speculative buy rating for shares of UFP Technologies (UFPT) with an 18-month price target of \$2.75 per share.

- We believe that as industry and economic conditions improve, UFP Technologies will return to the strong growth it has seen in the past.
- First Call industry projections call for earnings to increase by 67% in 2002 over 2001 levels.
- We expect the Company will be profitable in the third quarter of 2001 with revenues gradually improving from the third quarter on.

Comparable Company Analysis

Company Name	Symbol	Market				Cash Per Share	Return on	
		Capitalization (\$M)	Price/Earnings	Price/Sales	Price/Book		Equity	Debt/Equity
Peak International	PEAK	88.4	6	1.1	0.8	2.31	15.4%	0
Graphic Packaging	GPK	86.1	N/A	0.1	0.2	0.14	-1.5%	1.22
Polyair Inter Pack	PPK	15.2	5.1	0.2	0.8	0.17	17.8%	1.62
Air Packaging Tech.	AIRP	19.7	N/A	18.7	16.1	0.03	267.6%	0.4
Carmel Container Systems	KML	12.7	54.3	0.1	N/A	N/A	N/A	N/A
RADVA Corporation	RDVA	<u>0.7</u>	<u>N/A</u>	<u>0.1</u>	<u>0.2</u>	<u>0</u>	<u>-23.5%</u>	<u>1.4</u>
Average		37.1	10.9	3.4	3.0	0.4	46.0%	0.8
UFP Technologies	UFPT	7.6	15.0	0.1	0.4	0.0	2.9%	0.8

Price Performance of UFP Technologies



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UFP Technologies, Inc.

Consolidated Balance Sheets
(in thousands)

	31-Mar <u>2001</u>	31-Dec <u>2000</u>
Assets		
<i>Current assets:</i>		
Cash and cash equivalents	\$ 64	\$ 94
Accounts receivable	11,090	10,693
Inventories	6,605	6,780
Prepaid expenses and other current assets	<u>1,334</u>	<u>946</u>
Total Current Assets	19,093	18,513
Property and equipment, net	12,553	12,453
Goodwill, net	6,605	6,725
Other assets	<u>2,614</u>	<u>2,661</u>
Total Assets	<u>\$ 40,865</u>	<u>\$ 40,352</u>
 Liabilities & shareholders' investment		
<i>Current Liabilities:</i>		
Notes payable	\$ 7,604	\$ 4,737
Current portion of long-term debt	1,257	1,057
Current portion of capital lease obligations	422	290
Accounts payable	3,365	4,440
Accrued taxes and other expenses	<u>3,348</u>	<u>3,850</u>
Total current liabilities	15,996	14,374
Long-term debt	6,965	7,174
Capital lease obligations	195	415
Other liabilities	<u>897</u>	<u>862</u>
Total liabilities	24,053	22,825
Total stockholder's equity	<u>16,813</u>	<u>17,527</u>
Total liabilities & stockholder's equity	<u>\$ 40,866</u>	<u>\$ 40,352</u>

UFP Technologies, Inc.

Annual Income Statements for the Years Ended
(in thousands)

	<u>FYE(12/98)</u>	<u>FYE(12/99)</u>	<u>FYE(12/00)</u>	<u>FYE(12/01)E</u>	<u>FYE(12/02)E</u>
Net sales	\$ 47,220	\$ 58,801	\$ 74,491	\$ 71,566	\$ 77,000
Cost of sales	<u>34,140</u>	<u>43,939</u>	<u>56,870</u>	<u>54,595</u>	<u>58,772</u>
Gross profit	13,080	14,862	17,621	16,971	18,228
<i>Gross Margin</i>	27.70%	25.28%	23.66%	23.71%	23.67%
SG&A	<u>9,906</u>	<u>11,582</u>	<u>14,236</u>	<u>15,424</u>	<u>15,900</u>
Operating income	3,174	3,280	3,385	1,547	2,328
<i>Operating Margin</i>	6.72%	5.58%	4.54%	2.16%	3.02%
Interest expense	(447)	(641)	(1,221)	(1,100)	(1,100)
Other income (expense)	<u>61</u>	<u>191</u>	<u>(162)</u>	<u>-</u>	<u>-</u>
Income before taxes	2,788	2,830	2,002	447	1,228
Income tax	<u>1,141</u>	<u>1,136</u>	<u>921</u>	<u>206</u>	<u>565</u>
<i>Tax rate</i>	40.93%	40.14%	46.00%	46.09%	46.01%
Net Income / (Loss)	<u>\$ 1,647</u>	<u>\$ 1,694</u>	<u>\$ 1,081</u>	<u>\$ 241</u>	<u>\$ 663</u>
Basic EPS	<u>\$ 0.35</u>	<u>\$ 0.35</u>	<u>\$ 0.25</u>	<u>\$ 0.06</u>	<u>\$ 0.15</u>
Diluted EPS	<u>\$ 0.34</u>	<u>\$ 0.35</u>	<u>\$ 0.25</u>	<u>\$ 0.06</u>	<u>\$ 0.15</u>
Basic Shares Outstanding	4,682	4,809	4,374	4,375	4,375
Diluted Shares Outstanding	4,830	4,896	4,386	4,375	4,375
<u>Percent of Revenue</u>					
Cost of goods sold	72.30%	74.72%	76.34%	76.29%	76.33%
SG&A	20.98%	19.70%	19.11%	21.55%	20.65%
<u>Year / Year Growth</u>					
Total Revenues	3.89%	24.53%	26.68%	-3.93%	7.59%
Net Income	25.82%	2.85%	-36.19%	-77.71%	175.10%
EPS	25.93%	1.47%	-28.77%	-77.65%	175.10%

UFP Technologies, Inc.

Quarterly Income Statement for the Year Ending 2001
(in thousands)

	<u>Q1(3/01)</u>	<u>Q2(6/01)E</u>	<u>Q3(9/01)E</u>	<u>Q4(12/01)E</u>	<u>FYE(12/01)E</u>
Net sales	\$ 16,966	\$ 17,800	\$ 18,000	\$ 18,800	\$ 71,566
Cost of sales	<u>13,568</u>	<u>13,797</u>	<u>13,568</u>	<u>13,662</u>	<u>54,595</u>
Gross profit	3,398	4,003	4,432	5,139	16,972
<i>Gross Margin</i>	20.03%	23.25%	23.35%	23.50%	23.71%
SG&A	<u>3,805</u>	<u>3,840</u>	<u>3,879</u>	<u>3,900</u>	<u>15,424</u>
Operating income	(407)	163	553	1,239	1,548
<i>Operating Margin</i>	-2.40%	0.92%	3.07%	6.59%	2.16%
Interest expense	(275)	(275)	(275)	(275)	(1,100)
Other income (expense)	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Income before taxes	(682)	(112)	278	964	448
Income tax	<u>(314)</u>	<u>(52)</u>	<u>128</u>	<u>443</u>	<u>206</u>
<i>Tax rate</i>	46.04%	46.00%	46.00%	46.00%	45.94%
Net Income / (Loss)	<u>\$ (368)</u>	<u>\$ (60)</u>	<u>\$ 150</u>	<u>\$ 520</u>	<u>\$ 242</u>
Basic EPS	<u>\$ (0.08)</u>	<u>\$ (0.01)</u>	<u>\$ 0.03</u>	<u>\$ 0.12</u>	<u>\$ 0.06</u>
Diluted EPS	<u>\$ (0.08)</u>	<u>\$ (0.01)</u>	<u>\$ 0.03</u>	<u>\$ 0.12</u>	<u>\$ 0.06</u>
Basic Shares Outstanding	4,375	4,375	4,375	4,375	4,375
Diluted Shares Outstanding	4,375	4,375	4,375	4,375	4,375
<u>Percent of Revenue</u>					
Cost of sales	79.97%	77.51%	75.38%	72.67%	76.29%
SG&A	22.43%	21.57%	21.55%	20.74%	21.55%
<u>Year / Year Growth</u>					
Total Revenues	-7.20%	-8.32%	-4.75%	5.06%	-3.93%
Net Income	NMF	NMF	-31.82%	46.48%	-77.61%
EPS	NMF	NMF	-40.00%	50.00%	-76.00%

UFP Technologies, Inc.

Quarterly Income Statement for the Year Ending 2002
(in thousands)

	<u>Q1(3/02)E</u>	<u>Q2(6/02)E</u>	<u>Q3(9/02)E</u>	<u>Q4(12/02)E</u>	<u>FYE(12/02)E</u>
Net sales	\$ 18,000	\$ 19,400	\$ 19,200	\$ 20,400	\$ 77,000
Cost of sales	<u>13,797</u>	<u>14,802</u>	<u>14,669</u>	<u>15,504</u>	<u>58,772</u>
Gross profit	4,203	4,598	4,531	4,896	18,228
<i>Gross Margin</i>	23.35%	23.70%	23.60%	24.00%	23.67%
SG&A	<u>3,930</u>	<u>3,960</u>	<u>3,990</u>	<u>4,020</u>	<u>15,900</u>
Operating income	273	638	541	876	2,328
<i>Operating Margin</i>	1.52%	3.29%	2.82%	4.29%	3.02%
Interest expense	(275)	(275)	(275)	(275)	(1,100)
Other income (expense)	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>-</u>
Income before taxes	(2)	363	266	601	1,228
Income tax	<u>(1)</u>	<u>167</u>	<u>122</u>	<u>276</u>	<u>565</u>
<i>Tax rate</i>	46.00%	46.00%	46.00%	46.00%	46.00%
Net Income / (Loss)	<u>\$ (1)</u>	<u>\$ 196</u>	<u>\$ 144</u>	<u>\$ 325</u>	<u>\$ 663</u>
Basic EPS	<u>\$ (0.00)</u>	<u>\$ 0.04</u>	<u>\$ 0.03</u>	<u>\$ 0.07</u>	<u>\$ 0.15</u>
Diluted EPS	<u>\$ (0.00)</u>	<u>\$ 0.04</u>	<u>\$ 0.03</u>	<u>\$ 0.07</u>	<u>\$ 0.15</u>
Basic Shares Outstanding	4,375	4,375	4,375	4,375	4,375
Diluted Shares Outstanding	4,375	4,375	4,375	4,375	4,375
<u>Percent of Revenue</u>					
Cost of goods sold	76.65%	76.30%	76.40%	76.00%	76.33%
SG&A	21.83%	20.41%	20.78%	19.71%	20.65%
<u>Year / Year Growth</u>					
Total Revenues	6.09%	8.99%	6.67%	8.51%	7.59%
Net Income	99.73%	NMF	-4.00%	-37.50%	173.97%
EPS	100.00%	NMF	0.00%	-41.67%	150.00%

Statement of Cash Flows for the Three Months Ended
(in thousands)

	31-Mar <u>2001</u>	31-Mar <u>2000</u>
<i>Cash Flows from Operating Activities</i>		
Net Income	\$ (368)	\$ 218
Depreciation & amortization	796	726
Stock issued in lieu of compensation	141	171
<i>Changes in assets and liabilities</i>		
Receivables	(397)	557
Inventories	175	(174)
Prepaid expenses	(388)	(17)
Accounts payable	(1,075)	(2,146)
Accrued taxes and other expenses	(502)	(808)
Retirement and other liabilities	35	(32)
Decrease in other assets	<u>37</u>	<u>126</u>
Net Cash Provided by Operations	(1,546)	(1,379)
<i>Cash Flows from Investing Activities</i>		
Additions to property, plant and equipment	(771)	(453)
Payments received on advances to affiliate	5	23
Acquisition of Simco	<u>-</u>	<u>(6,252)</u>
Net Cash Used in Investing	(766)	(6,682)
<i>Cash Flows from Financing Activities</i>		
Net borrowings under notes payable	2,867	2,298
Principal repayments of long-term debt	(9)	(15)
Principle repayments of capital lease obligations	(89)	(475)
Proceeds from long-term borrowings	-	6,120
Capital stock repurchase	(525)	-
Net proceeds from sale of common stock	<u>37</u>	<u>38</u>
Net cash Provided Financing	2,281	7,966
Net change in Cash	(31)	(95)
Cash - Beginning of Period	<u>94</u>	<u>349</u>
Cash - End of Period	<u>\$ 63</u>	<u>\$ 254</u>