

## Mr. Goodale should visit this trust: Spinrite yarnmaker hardly a drain on Canadian economy

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Illustration: Colour Photo: Spinrite / An employee tends to a spinning frame at the Spinrite factory in Listowel, Ont. Although the yarnmaker must deal with a strong dollar and demanding customers, its biggest challenge comes from Ottawa.

It is 7:30 a.m. in downtown Toronto and the turnout for a day-long field trip to Spinrite Income Fund is looking a little light. The company has rented a bus to ferry analysts, brokers and investors to its headquarters in Listowel, Ont. and not more than a dozen people have showed up.

It is early. It is a two-hour drive. It is a small income trust. It makes yarn. But Ottawa has also made this tour a tough sell.

"Maybe Ralph Goodale scared everybody away," offers one analyst waiting in the dark to board.

A couple of analysts cancelled at the last minute. They were swamped with calls after the Finance Minister announced his review of the trust sector and then banned advance tax rulings for corporations wanting to convert.

For those with the gumption to attend, it is a scenic outing to heart of Mennonite country. The traffic and ugly sprawl of Toronto give way to tidy farmhouses and fields and signs you wouldn't see next to congested roadways in the city: "Tractor seats re-upholstered," "Foundation Sires, Bulls you can build on" and "Prepare to meet your God." The bus is quiet as we all prepare for four hours at a yarn factory.

But Listowel and Spinrite aren't so dull, after all. Along with Spinrite's operations that employ about 600 workers, there is a Honda parts plant here and a Campbell's Soup Co. factory. Locals say big business likes the town of 5,300, given its traditional aversion to unions. None of the plants here are organized.

We are ushered from the bus into Spinrite's cafeteria, now a makeshift conference room with displays of knitted shawls, scarves, sweaters and hats and balls of yarn at every table. "The appearance of the yarn on the shelf is everything," says Frank Verwey, head of manufacturing.

Looking a tad nervous, company executives are eager to start their sales pitch. Before Goodale announced the tax-ruling ban on Sept. 19, Spinrite units traded at \$13, down from their all-time high of \$14.25 in August. By the investor day on Sept. 29, they had slipped to \$12.60. (They closed yesterday at \$11.61.)

Spinrite, bought by a private-equity firm in 2004, went public in February with a \$200-million IPO, tapping into the heavy demand for trusts and the apparent resurgence in knitting. Spurred by fashion trends -- including Martha Stewart's famous "prison poncho" that she wore leaving jail -- and the curious trend towards "cocooning" at home, knitting is no longer confined to grannies.

The number of knitters under the age of 45 has doubled in the last six years, according to chief executive Dario Margve. Last year, a New York City knitting festival attracted 35,000. There are knitting cafes and knitting television shows.

Two Spinrite executives missed the investor day because they were down at Wal-Mart headquarters in Arkansas, meeting with executives and offering eight knitting classes. All were full.

This is not a fad, but a "cultural shift," said Margve. "A lot of younger users now see relevance in the craft."

Spinrite figures craft yarn is a \$41-billion market. It has 62% market share in Canada and has increased its U.S. share 55% over the past three years to 18%.

Spinrite's strategy is to focus on fancier yarns with higher margins, while improving its distribution through major retailers like Wal-Mart and new channels such as grocery stores.

With the surging Canadian dollar and the fluctuating cost of acrylic, a key ingredient in yarn, Spinrite is under constant pressure to keep expenses down. It is also under constant pressure to satisfy Wal-Mart. While Spinrite takes 48 hours to fill most orders, it aims to complete Wal-Mart shipments in less than 24.

In 2002, it built a new distribution centre. The company used to keep track of inventory manually, writing it in a book they called "The Bible" that had to be updated every morning. Spinrite is now installing a computerized system.

Making yarn has not changed much over the years, though. On a wall at Spinrite headquarters, there is a

photograph of the plant some 20 years ago. It looks nearly the same today. The company still uses the same machines, since there has been little technological innovation aside from new methods for dyeing yarn.

Overall, Spinrite has a decent story to tell. There will be challenges. Will the growth in knitting persist? Will Spinrite get continually squeezed by Wal-Mart? Will raw materials costs rise?

But like other income trusts, the most unpredictable factor is the Ottawa's eventual stance on trusts. Will they tax trusts? Will they instead lower dividend taxes on corporations? These are questions executives at Spinrite can't answer.

As we wrap up the tour with lunch at Spinrite's warehouse, chief financial officer Ryan Newell sounds a little frustrated. How can a structure considered legitimate just months ago, when Spinrite went public, be considered bogus today? he asks.

While Goodale makes noises about trusts sapping our tax base and the economy, Spinrite is clearly eager to grow.

The company's payout ratio is a conservative 62%. By holding back a larger share of its cash, Spinrite has room to increase distributions and cushion any shocks to the business. It also has room to grow through acquisitions. After spending a few hours at Spinrite, it doesn't look like an unambitious company or a drain on our economy, as Ottawa seems to fear.

From the piles of sandwiches and desserts and the bags of free yarn, it looks like Spinrite expected a few more guests for its first-ever investor day. But there is one person that probably would have benefited the most from visiting a real, live income trust: Ralph Goodale. Maybe next year.