



July 30, 2015

CURRENT PRICE: \$16.28
RATING: HOLD
PRICE TARGET: N/A
CURRENT YIELD: 0.7%

EPS Estimates - Non-GAAP

	SEP 14A	SEP 15E
1Q	\$0.15	\$0.22A
2Q	\$0.19	\$0.14A
3Q	\$0.31	\$0.29A
4Q	\$0.24	\$0.43
	\$0.89	\$1.09

Trading Data

52-WEEK PRICE RANGE: **\$24.85 - \$16.04**
 SHARES OUTSTANDING: **18.83(M)**
 MARKET CAP: **\$306.7(M)**
 AVG. DAILY TRADING VOLUME: **0.05(M)**
 S&P 500: **2,108**

Valuation Data

BOOK VALUE: **\$10.37**
 PRICE TO BOOK: **1.57x**
 DIVIDEND: **\$0.12**

INSTEEL INDUSTRIES, INC (NSDQ: IIIN)

3Q15 earnings results

Highlights

- 3Q15 earnings of \$0.29/share vs. \$0.31/share during 3Q14
- Earnings results impacted by heavy rain in customer areas
- IIIN anticipates increase of customer orders next 2 quarters
- Lowering annual operating costs
- Maintain HOLD rating

Investment Thesis

IIIN could be an interesting speculative play for aggressive investors. Since most of IIIN's business is related to the US construction market, its stock has been volatile during the past four years as investor's have moved in and out of the shares based on expectations of a recovery in the construction industry. While an increase in meaningful customer orders may start to materialize, improvement in construction spending may lead to earnings growth for IIIN. Aggressive and speculative investors should look for attractive entry points into IIIN for potential price appreciation when the US construction market improves and increases demand for the company's products.

Company Summary

Insteel Industries (IIIN-\$16.28), headquartered in Mt. Airy NC, is one of the largest manufacturers of steel wire reinforcing products for concrete construction applications. It is the parent holding company of two wholly-owned subsidiaries, Insteel Wire Products Company and Intercontinental Metals Corporation. IIIN manufactures/markets PC strand and welded wire reinforcement (WWR) products. Products are sold through its sales force and a sales agent, primarily to concrete product manufacturers for use in nonresidential construction. Approximately 97% of sales were to US customers and the remaining 3% from Canada and Central/Latin America. Started in 1958, the company has approximately 847 employees (as of 9/27/14), and generated total revenues of \$409 million during FY14. An estimated 90% of IIIN's sales went towards nonresidential construction (approximately 35% infrastructure & 55% non-infrastructure) and 10% to residential construction. The company has very little debt on its balance sheet.

For Important Disclosure information regarding the Firm's rating system, valuation methods and potential conflicts of interest, please refer to the last two pages of this report.

100 Concourse Boulevard, Suite 101
 Glen Allen, Virginia 23059

804.612.9700 ■ 800.612.1484
 804.527.1104

www.CapitolSecurities.com

Member
 FINRA
 SIPC

Offices: Glen Allen, VA ■ Reston, VA ■ Charlottesville, VA ■ Silver Spring, MD ■ Baltimore, MD ■ Tampa, FL ■ Boston, MA ■ Florham Park, NJ



EQUITY RESEARCH

Recent Earnings

IIIN reported 3Q15 earnings of \$0.29/share vs. \$0.31/share during 3Q14. 3Q15's results includes \$300,000 of restructuring charges, connected to the recent closing of the Newnan GA pre-stressed concrete strand facility, \$700,000 for settlement of a customer dispute, and \$100,000 net gain from insurance proceeds related to a fire at IIIN's Gallatin TN facility. These items reduced 3Q15's earnings by \$0.03/share. 3Q14's earnings were positively impacted by \$0.03/share from insurance a net gain on insurance proceeds related to the Gallatin fire.

Net sales improved 3.3% to \$117.0 million from \$113.2 million due to the added revenue generated from the August 2014 acquisition of the PC Strand business of American Spring Wire Corp (ASW). This offset the negative effects of record rainfall/flooding in the central US, which management believes suppressed potential revenue streams during this past quarter. The rains/flooding brought construction activity and customer operations to a stop for extended periods of time in Texas (IIIN's largest market).

When comparing 3Q15 with 3Q14, shipments increased 5.1% while average selling prices fell 1.7%. Adjusting the two quarters' results, to include pre-acquisition shipment volumes of ASW, shipments during 3Q15 decreased 8.8% due mainly to bad weather. Sequential quarterly shipments improved 19.1%, during 3Q15, compared to a 25.2% sequential quarterly increase during 3Q14, reflecting the impact of adverse weather.

Gross profit margin improved to \$15.7 million from \$14.3 million, when comparing 3Q15 vs. 3Q14. Results were positively impacted by higher spreads between selling prices/raw material costs and an increase in shipments. These were partly offset by increased conversion costs when compared to 3Q14. Capacity utilization was 54% versus 58% when comparing 3Q15 with 3Q14.

EARNINGS CONFERENCE CALL

Management noted 3Q15's earnings results were impacted by the heavy rains which hit the central region of the US, particularly Texas, during the end of May and beginning of June. Many customers suffered from adverse weather and flooding, causing a delay in orders/shipments, especially in Texas representing 20% of IIIN's revenues. The company believes the deferral of these shipments will favorably impact sales during the next two quarters, 4Q15 and 1Q16.

On the cost cutting side of its business, management noted it had the closed its Newnan GA PC strand plant (acquired in the 2014 ASW transaction). This move and the relocation of its equipment to other IIIN facilities, while ramping up the Houston TX PC strand facility should generate annual savings of \$3 million/year.

Additionally, the new high volume standard welded wire reinforcing production line at its PA facility to replace obsolete technology will generate increased capacity producing certain SKUs and lower conversion costs. The company anticipates increasing production from this line which could increase IIIN's operating capacity and margins. IIIN also plans to commission a new wire production line at its FL Welded Wire reinforcing facility, with



expectations of being fully operational during 4Q15, and believes it will round out capacity and should lower operating costs.

In terms of forward operating guidance, IIN feels 4Q results should improve based on stable selling prices and lower material costs. Expectations are for continued improvement in the non-residential construction market in 2015 and increased spreads/margins based on expected revenues and lower cost inventory expected to be used in the coming months' production cycle.

Our Thoughts

Overall, a respectable earnings report for IIN during 3Q15 vs. 3Q14, as the company reported earnings per share of \$0.29/share vs. \$0.31/share. The negative result as severe weather in its customers' areas affected business orders. 3Q15's results contained various charges which penalized earnings by \$0.03/share. Shipments rose 5.1%, average selling prices fell 1.7%, and the gross profit margin rose to \$15.7 million from \$14.3 million. IIN's management the delay in orders, due to bad weather, could show up during the next two quarters. However, despite the relative good earnings report/prospects, IIN's stock has fallen during the past few weeks as Wall Street is concerned whether the recent slide in commodity prices is a prelude to an economic slowdown. On a valuation basis, IIN is beginning to look inexpensive trading at 1.57x book. Investors may want to wait to see if these shares become cheaper during the next 3 months. We maintain our HOLD rating on this stock.



Risks

There are no guarantees IIIN will be able to grow future earnings. Declining customer orders, rising commodity prices, and rising operating costs could negatively affect the company's profits. Management has a labor union operating at one of its plants. An influx of foreign imports and increase in competition could cause a decrease in overall revenues. Negative equity markets, rising interest rates, terrorist attacks, and failure to comply with the Sarbanes Oxley Act could cause a decline in IIIN's share price. Given the relatively small amount of daily trading activity in IIIN's stock, any increase in trading volume could significantly accelerate the volatility of its share price movement.

Steven F. Marascia
Director of Research
Capitol Securities Management
804-612-9715

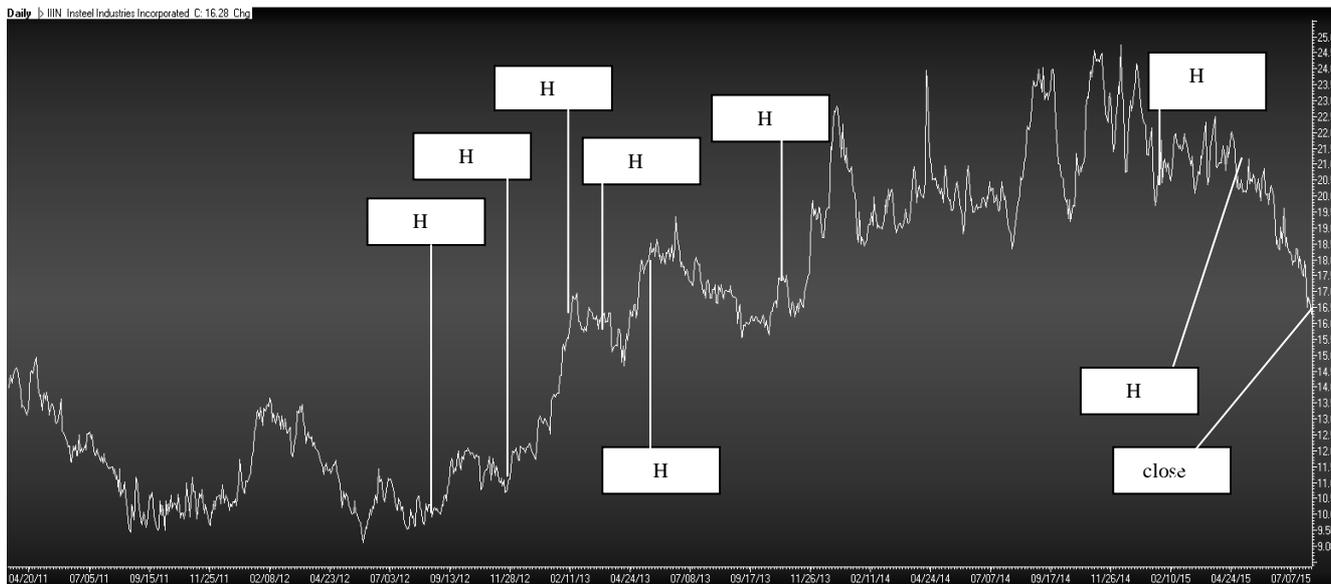


EQUITY RESEARCH

INSTEEL INDUSTRIES, INC.
 FY ends 9/30
 (in thousands except per share amounts)

	1Q14	2Q14	3Q14	4Q14	2014	1Q15	2Q15	3Q15	4Q15e	2015e
Revenues	\$87,218	\$91,436	\$113,227	\$117,097	\$408,978	\$110,628	\$101,767	\$117,016	\$134,921	\$464,332
Cost of sales	78,163	79,830	98,964	103,248	360,205	98,585	93,065	101,322	116,950	409,922
Inventory write-downs										
Gross profit	9,055	11,606	14,263	13,649	48,773	12,043	8,702	15,694	17,971	54,410
SG&A	4,705	5,984	6,219	6,463	23,371	5,652	5,975	6,427	6,387	24,441
Acquisition costs				612	612					
Bargain Purchase gain										
Gain on debt extinguishment										
Restructuring charges				1,247	1,247		333	345	200	878
Other expenses/income	32	228	849	1,254	1,907	40	1,599	601	723	2,963
Income	4,382	5,394	8,893	6,781	24,450	6,431	3,993	8,321	10,661	29,406
Interest expense	-56	-57	-56	-83	-252	-94	-114	-65	-72	-345
Interest income	5	1	4		10		4	1	4	9
Income from cont. operations	4,331	5,338	8,841	6,698	25,208	6,337	3,883	8,257	10,593	29,070
Income taxes	1,584	1,816	3,044	2,123	8,567	2,187	1,339	2,865	3,676	10,067
Earnings from continuing Ops.	2,747	3,552	5,797	4,575	16,641	4,150	2,544	5,392	6,917	19,003
Earnings from discont. Ops										
Net Earnings	2,747	3,552	5,797	4,575	16,641	4,150	2,544	5,392	6,917	19,003
Net earnings/share	\$0.15	\$0.19	\$0.31	\$0.24	\$0.89	\$0.22	\$0.14	\$0.29	\$0.37	\$1.02
Cash dividends/share	\$0.03	\$0.03	\$0.03	\$0.03	\$0.12	\$0.03	\$0.03	\$0.03	\$0.03	\$0.12
Fully diluted shares outstanding	18,587	18,637	18,683	18,755	18,755	18,820	18,822	18,828	18,828	18,828

Important Disclosures



3/07/11 \$11.74 Initiate HOLD

Ratings:

Buy: B

Hold: H

Sell: S

Steven Marascia certifies, with respect to the companies or securities that he analyzes, that (1) the views expressed in this report accurately reflect his personal views about all of the subject companies and securities and (2) no part of his compensation was, is or will be directly or indirectly related to the specific recommendations or views expressed in this report.

Stock ratings used in this report are defined as follows:

- (1) Buy – The stock's total return including dividends is expected to exceed the industry or market average by at least 10% over the next twelve months.
- (2) Hold – The stock's total return including dividends is expected to be in line with the industry or market average of +/- 10% over the next twelve months.
- (3) Sell – The Stock's total return including dividends is expected to be below the industry or market average by 10% or more over the next twelve months.

The distribution of investment ratings for all companies in our coverage universe are as follows: (1) 43%, (2) 57%, (3) 0%

The distribution of investment ratings used for companies whom we have performed banking services in the last 12 months are (1) 0%, (2) 0%, (3) 0%

Capitol Securities Management's Investment Banking/Public Finance unit has not received compensation for investment banking services from the subject company in the past 12 months. Nor does it expect to receive, or intend to seek compensation for, investment banking services from the subject company in the next 3 months.

No affiliate of Capitol Securities Management, or Capitol Securities Management, received compensation from the subject company for products or services during the past 12 months.

The subject company is not, or during the past 12 months, was not, a client of Capitol Securities Management's Investment Banking/Public Finance unit



Other Disclosures

This report is not directed to, or intended for distribution to or use by any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction where such distribution, publication, availability or use would be contrary to law or regulation or which would subject Capitol Securities or its affiliates to any registration or licensing requirement within such jurisdiction. The information presented in this report is provided to you for information purposes only and is not to be used or considered as an offer or the solicitation of an offer to sell or buy or subscribe for securities or other financial instruments. Capitol Securities may not have taken any steps to ensure that the securities referred to in this report are suitable for any particular investor. Capitol Securities will not treat recipients of this report as its customers by virtue of their receiving this report. The investments and services contained or referred to in this report may not be suitable for you and it is recommended that you consult an independent investment advisor if you are in doubt about such investments or investment services. Nothing in this report constitutes investment, legal, accounting or tax advice, or a representation that any investment or strategy is suitable or appropriate to your individual circumstances, or otherwise constitutes a personal recommendation to you. Capitol Securities does not advise on the tax consequences of investments and you are advised to contact an independent tax advisor. Information and opinions presented in this report have been obtained or derived from sources believed by Capitol Securities to be reliable, but Capitol Securities

makes no representation as to their accuracy or completeness. This report is not to be relied upon in substitution for the exercise of independent judgment. Capitol Securities may have issued, and may in the future issue, other reports that are inconsistent with, and reach different conclusions from, the information presented in this report. Past performance should not be taken as an indication or guarantee of future performance, and no representation or warranty, express or implied, is made regarding future performance. Information, opinions and estimates contained in this report reflect a judgment at its original date of publication by Capitol Securities and are subject to change without notice. The price, value of and income from any of the securities mentioned in this report can fall as well as rise.

For more information on this report, please contact us at 800.612.1484 or write to Capitol Securities, 100 Concourse Boulevard, Suite 101, Glen Allen, Virginia 23059