

## FELLOW SHAREHOLDERS

We are pleased to report that Culp delivered another solid performance in fiscal 2014 with higher annual sales in both of our businesses. Notably, this is the fifth consecutive year of overall sales growth and a record year of annual sales for mattress fabrics. We reported \$19.0 million in pre-tax income, the second highest level in 15 years. We also achieved a 26 percent return on capital employed. Throughout the year, we continued to make outstanding progress with our strategic focus on design creativity and product innovation. These efforts have been the key driver to our sales and profit performance, with an increasing percentage of our sales coming from our latest product introductions. Demand trends have been favorable, and our ability to sustain excellence in creating innovative fabrics season after season has been an important advantage for Culp in our fashion-driven business. Importantly, we also maintained the financial strength to support our growth initiatives and make strategic investments in both of our businesses.

### CASH RETURNED TO SHAREHOLDERS

We had a solid financial performance and achieved excellent free cash flow of \$13.8 million in fiscal 2014, compared with \$13.1 million in fiscal 2013. Commensurate with our capital allocation strategy, we were pleased to return \$2.2 million to our shareholders in regular quarterly dividends. We raised the quarterly cash dividend by 33 percent from \$0.03 to \$0.04 per share beginning in the first quarter of fiscal 2014, and our Board of Directors approved an additional 25 percent increase to \$0.05 per share, commencing the third quarter of fiscal 2014. Following the end of the fiscal year, the Board of Directors also approved a special cash dividend of \$0.40 per share, which was paid in July 2014. The special dividend payment reflects our solid and consistent financial performance and strong free cash flow, along with the leadership position we have achieved in each of our businesses. These actions reinforce our confidence in Culp's future and our commitment to generating value for our shareholders.

### MATTRESS FABRICS SEGMENT

For the year, mattress fabric sales were \$160.7 million, surpassing the previous year's sales by 4 percent and establishing a new annual record for this business. This growth reflects our ability to capitalize on the growing consumer demand for "better" designed bedding products. As the mattress industry has evolved into a much more decorative business, our customers are more selective in their fabric choices to achieve today's fashionable look. In response to this demand trend, we increased our design staff, as well as expanded our design capabilities and technical expertise, to enhance our ability to develop an array of innovative fabric choices across all price points. We have a scalable manufacturing platform and reactive capacity that supports our ability to deliver a diverse and favorable product mix in line with customer demand. As a result, we have enhanced our competitive position as a leading supplier of mattress fabrics and covers to the major players across all categories in the mattress industry.

Our operating profit and margins for the year were affected by several factors, primarily during the second half of the year. During the third quarter, our operating results were affected by higher than expected transition costs in Culp-Lava, our mattress cover operation, as well as additional sampling and development costs

in support of new customer roll-outs. The severe winter weather conditions experienced in many parts of the country affected our mattress fabrics locations with at least a week of lost production during the fourth quarter. The interruption placed additional pressure on our operations to meet the ongoing sales demand.

We also experienced higher than expected demand for premium decorative knitted mattress fabrics, which affected our production throughput and operating efficiencies. In order to meet this growing demand and to improve our efficiency, we are increasing knitted fabric production at all of our facilities. We are expanding our Stokesdale, North Carolina, building in order to increase and enhance our internal knit finishing capabilities and improve our production flow. This first phase of the capacity expansion is anticipated to be completed by the end of December 2014. The second phase, which will involve purchasing additional knit machines, is expected to be completed during the second half of fiscal 2015. Our projected \$9.5 million in capital expenditures for fiscal 2015 demonstrates Culp's continued commitment to the future growth of our mattress fabrics business.

We made significant progress with respect to Culp-Lava in fiscal 2014, and we are pleased with the increased sales contribution for the year. The demand for new mattress covers has been better than expected and we are pleased by the market response for this category. While we experienced some short-term production challenges and inefficiencies related to absorbing new products, we are very focused on improving our operating efficiencies as we continue to add capacity and enhance reactivity.

Overall, the fundamentals of our mattress fabrics business are strong, and Culp has a solid competitive position as we continue to outpace the overall industry growth. We are especially pleased with the favorable customer response to our exciting designs and new product introductions that meet today's style trends. We are excited about the opportunities ahead in fiscal 2015 to grow our business and to enhance Culp's leadership position in the bedding industry.

### UPHOLSTERY FABRICS SEGMENT

Our upholstery fabrics business experienced continued growth throughout fiscal 2014, highlighted by a 10 percent increase in sales, marking the fifth consecutive year for annual sales growth in this segment. Importantly, along with the higher sales, we achieved a 16 percent increase in profitability over the prior year. These results are product-driven, with favorable customer response to our outstanding designs and innovative fabrics. We are especially pleased with the increased demand for our newest product introductions.

Our 100 percent owned China platform provides significant manufacturing flexibility to produce a variety of product categories, and we have continued to leverage this capability to meet changing customer demand in line with the latest furniture style trends. Sales of China produced fabrics accounted for approximately 92 percent of upholstery fabric sales in fiscal 2014. This platform has also supported our ability to expand our global market presence and reach new customers. We had great showings at the 2014 furniture markets with very positive feedback from customers and strong placements.

With respect to Culp Europe, we are continuing our efforts to develop sales in Europe through our Culp Europe operation. We remain optimistic about the future opportunities in Europe to support our global sales efforts, and we are currently assessing the best strategy for taking advantage of this market's opportunities.

We have continued to enhance our leadership position in upholstery fabrics with significant manufacturing flexibility, creative design capabilities, and a strong commitment to customer service - all important advantages to effectively meet the demands of a global marketplace. We believe Culp is well positioned for continued growth in upholstery fabrics, especially as the furniture industry continues to consolidate and business conditions improve with a more stable housing market and higher consumer spending for home furnishings.

### **BALANCE SHEET AND FREE CASH FLOW**

We are very pleased to end fiscal 2014 with a strong financial position. The company generated \$13.8 million in free cash flow in fiscal 2014, after investing \$7.2 million primarily in working capital and capital expenditures. During fiscal 2014, we used the free cash flow to build our net cash position by approximately \$9.0 million, to pay dividends of \$2.2 million, and to make a small acquisition that totaled \$2.6 million. Looking ahead to fiscal 2015, we expect a good year of free cash flow, with capital expenditures projected to be significantly higher than normal and modest growth in working capital.

As of the end of fiscal 2014, we reported \$35.6 million in cash and cash equivalents and short-term investments. Total debt at the end of fiscal 2014 was \$5.0 million, which includes long-term debt plus current maturities of long-term debt and our line of credit. Notably, our net cash position, or cash minus total debt, was \$30.6 million at the end of the year compared with \$21.7 million a year ago. The \$30.6 million is the highest net cash position in the company's history. We have since made a scheduled \$2.2 million principal debt payment in August 2014, with one remaining annual \$2.2 million payment due August 2015.

### **CAPITAL ALLOCATION STRATEGY**

A very important focus of Culp's overall strategy is to prioritize our use of capital. In last year's annual report, we outlined the details of our capital allocation strategy, and we are pleased with our ability to follow this directive in fiscal 2014. As we noted, our first priority will always be to invest in our existing businesses. In fiscal 2014, we had a modest increase in working capital of about \$2.0 million, which supported the growth of both businesses. Additionally, capital expenditures for the year were \$5.3 million, most of which related to our mattress fabrics business.

Secondly, with the free cash flow we continued to generate in fiscal 2014, we met our goal to raise the regular quarterly cash dividend on a moderate basis with the two increases noted earlier.

Third, we continued to identify potential strategic acquisition opportunities to enhance our mattress fabrics business. Early in the year, we entered into an asset purchase agreement totaling \$2.6 million, which gave us the ability to sell our mattress fabrics to a leading bedding manufacturer.

Fourth, our goal has been to build our net cash position, or total cash minus total debt, to a target level of approximately \$25.0 million at

the end of our fiscal year. We were very pleased to reach a net cash position of \$30.6 million at the end of fiscal 2014, well above our stated goal. Our intention was to use those excess funds for special dividends and share repurchases, dependent on the prevailing economic and business outlook and other conditions. As such, following the end of fiscal 2014, we announced a special dividend of \$0.40 per share. In addition, thus far for fiscal 2015, the company has purchased approximately 32,000 shares of Culp common stock for approximately \$550,000, pursuant to the \$5.0 million share repurchase program authorized by the Board of Directors in February 2014. These actions reinforce our confidence in Culp's future and our commitment to generating value for our shareholders.

For fiscal 2015, we expect to invest approximately \$10.0 million in capital expenditures, primarily in the mattress fabrics business for expansion projects. However, even with the higher than normal level of capital expenditures and modest working capital growth, we expect fiscal 2015 to be another year of meaningful free cash flow generation.

### **LOOKING AHEAD**

We are pleased with Culp's performance in fiscal 2014 and our ability to drive sales and enhance our leadership position in a global marketplace. Our consistent growth reflects our ability to meet changing customer demands and style trends with our creative designs and innovative fabrics. Looking ahead, we will continue to strive to strengthen our economic moat in both businesses with our flexible and scalable global manufacturing platform, supported by design expertise, product innovation and outstanding customer service. At the same time, we have the financial strength to make the strategic investments to enhance and expand our production capabilities in line with market demand.

As we move forward in fiscal 2015, we are proud of the solid leadership position we have established in each of our businesses. Culp's success is built on the collective strength of a talented and dedicated team of long-term associates located throughout the world, with the support of an outstanding management team and board of directors. Above all, we are committed to outstanding performance for our customers as a financially stable and trusted source for innovative fabrics. We are equally committed to building shareholder value, and we look forward to the opportunities before us in fiscal 2015 and beyond.

We thank you for your support.

Sincerely,



Franklin N. Saxon  
President and Chief Executive Officer



Robert G. Culp, III  
Chairman of the Board

August 13, 2014