

# Letter to Shareholders

Fellow Shareholders:

Culp's performance for fiscal 2009 reflects excellent progress and consistent execution in spite of unprecedented challenges related to the economic downturn. While our annual sales reflect the sharp decline in discretionary consumer spending, especially for furniture, we made measurable progress throughout the year in developing a leaner, more efficient operating platform, reducing our costs and at the same time, significantly strengthening our financial position. We have also continued to make important investments in our businesses during the year with a strategic acquisition and major capital expenditures in our mattress fabrics segment, along with numerous product and marketing initiatives in both segments. As a result, we believe we have enhanced our competitive position as the market leader in mattress fabrics and upholstery fabrics. Most importantly, Culp continues to represent a strong and stable supplier for our customers.

## **MATTRESS FABRICS SEGMENT**

While the sales environment has been very challenging, we are pleased with the strong operating performance of our mattress fabrics business in fiscal 2009. In spite of declining sales, our operations performed well with consistent year over year margin improvement in mattress fabrics throughout the year.

These operating results reflect the implementation of a \$5.0 million capital project completed in early fiscal 2009, as well as the successful integration of the mattress fabrics operation of Bodet & Horst USA, or B&H, acquired in August 2008. Together, these investments have significantly enhanced our operating platform in mattress fabrics, with more efficient, vertically-integrated manufacturing capabilities in all major product categories. At the same time, we have further improved Culp's excellent service capabilities with improved supply logistics from pattern inception to fabric delivery, allowing accelerated responsiveness and greater stability. This new platform provides Culp with a strong competitive advantage as we aggressively pursue new business opportunities, and positions us very well when the industry eventually recovers. More importantly, we have improved our service capabilities with outstanding delivery performance, quality, innovation and value. As always, our top priority is meeting the needs of our customers.

## **UPHOLSTERY FABRICS SEGMENT**

Culp's upholstery fabrics business reflects soft demand industry wide, as well as continued very weak demand for U.S. produced upholstery fabrics, driven by imported furniture and fabrics. While our upholstery fabrics sales have been hit harder than mattress fabric sales during the economic downturn, this segment was still profitable in the second half of the fiscal year as a result of the successful implementation of our profit improvement plan. This plan, initiated during the second quarter of fiscal 2009, has exceeded our expectations as we have realized significant incremental benefits as a result of these actions. The consolidation of our China operations during the second and third quarters and significant reductions in selling, general and administrative expenses have lowered our costs by at least \$6.0 million on an annual basis. Further, the upholstery fabrics division has contributed substantially to our strong cash flow this year through outstanding working capital management, especially with inventories. Inventory levels have been reduced by 56 percent from the previous year-end level, and inventory turnover has also improved significantly in a declining sales environment.

As a result of aggressive restructuring actions both this year and in previous years, we have established a very lean and agile platform with our China operation and one remaining U.S. facility. We have significantly improved our competitive position by pursuing a strategy to dramatically lower the capital invested in the business and transition to a variable cost model. Looking ahead, we are optimistic about our prospects in the upholstery fabrics business for a number of reasons. We have been receiving significantly higher fabric placements, including cut and sew kits, with a broader base of key customers. We have now established a mature, scalable and low cost model in China that is vertically integrated through a network of key manufacturing partners developed over several years. We continue to be very enthusiastic about the opportunities from our China platform, especially when demand improves. We have also made significant progress in the competitive position of our U.S. facility this past year. Finally, and most importantly, we are now keenly focused on sales and marketing initiatives rather than downsizing and restructuring actions. These are all favorable indicators for improving results when the eventual recovery in demand for furniture takes place.

## BALANCE SHEET

A key priority for fiscal 2009 has been a very disciplined focus on strengthening our financial position and generating substantial cash in light of the uncertain business climate. Cash flow from operations was \$22.8 million for fiscal 2009, compared with \$16.4 million in fiscal 2008. Our balance sheet reflected \$11.8 million in cash as of May 3, 2009, compared with \$4.9 million at the end of last year.

We also significantly reduced our debt burden over the past year. Total debt, which includes current maturities of long term debt and long term debt, was \$16.4 million at the end of fiscal 2009, including the \$11.0 million unsecured term loan added in the second quarter for the B&H acquisition, compared with \$28.1 million at the end of the third quarter of fiscal 2009. At year-end, net debt, or total debt less cash, was \$4.6 million, compared with net debt of \$12.3 million at the end of the third quarter and \$23.7 million at the end of the second quarter. Four years ago at the end of fiscal 2005, net debt totaled \$45 million. All of Culp's debt remains unsecured, including lines of credit totaling \$10.5 million in the U.S. and China with no borrowings outstanding. Overall, our financial position has strengthened considerably during this fiscal year and is providing us with an important competitive advantage in light of the challenges facing our industry.

## LOOKING AHEAD

We expect the prevailing economic uncertainties and issues surrounding the housing and credit crises will continue to unfavorably affect consumer demand for furniture and bedding products, although we see some indication of improvement in the economic outlook for early fiscal 2010. While we acknowledge the challenges ahead, we remain confident in our ability to execute and enhance our competitive position as the market leader in both our businesses. Our customers look to Culp as a financially stable and reliable source of innovative fabrics, delivery performance and quality. We are enthusiastic about our business as we begin fiscal 2010 with a focused business strategy in place, a more efficient manufacturing platform, a much stronger balance sheet and a very capable team with a proven ability to execute. The dedication and commitment of everyone associated with Culp - our loyal associates, management team and board of directors - provides us with a solid foundation, and, more importantly, gives us the ability to look confidently to the future. Above all, our primary objectives are to further enhance both our businesses and deliver outstanding value to our customers, continue to improve our financial performance and further strengthen our balance sheet.

Thank you for your continued support of Culp.

Sincerely,



Franklin N. Saxon  
President and Chief Executive Officer  
August 18, 2009



Robert G. Culp, III  
Chairman of the Board