CULP INC
Form 10-Q
March 14, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D)
OF THE SECURITIES EXCHANGE ACT OF 1934

FOR THE QUARTERLY PERIOD ENDED JANUARY 28, 2007

COMMISSION FILE NO. 0-12781

CULP, INC.
(Exact name of registrant as specified in its charter)

NORTH CAROLINA	56-1001967
(State or other jurisdiction of incorporation or other organization)	(I.R.S. Employer Identification No.)

1823 EASTCHESTER DRIVE HIGH POINT, NORTH CAROLINA	27265-1402
(Address of principal executive offices)	(zip code)

(336) 889-5161 (Registrant's telephone number, including area code)

INDICATE BY CHECK MARK WHETHER THE REGISTRANT (1) HAS FILED ALL REPORTS REQUIRED TO BE FILED BY SECTION 13 OF THE SECURITIES EXCHANGE ACT OF 1934 DURING THE PRECEDING 12 MONTHS AND (2) HAS BEEN SUBJECT TO THE FILING REQUIREMENTS FOR AT LEAST THE PAST 90 DAYS. [X] YES NO [_]

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A LARGE ACCELERATED FILER, AN ACCELERATED FILER, OR A NON-ACCELERATED FILER. SEE DEFINITION OF "ACCELERATED FILER AND LARGE ACCELERATED FILER" IN RULE 12B-2 OF THE EXCHANGE ACT. (CHECK ONE);

LARGE ACCELERATED FILER [_] ACCELERATED FILER [_] NON-ACCELERATED FILER [X]

INDICATE BY CHECK MARK WHETHER THE REGISTRANT IS A SHELL COMPANY (AS DEFINED BY RULE 12B-2 OF THE EXCHANGE ACT). [_] YES NO [X]

INDICATE THE NUMBER OF SHARES OUTSTANDING OF EACH ISSUER'S CLASSES OF COMMON STOCK, AS OF THE LATEST PRACTICAL DATE:

COMMON SHARES OUTSTANDING AT JANUARY 28, 2007: 12,554,541
PAR VALUE: $0.05

INDEX TO FORM 10-Q
FOR THE PERIOD ENDED JANUARY 28, 2007

Item 1: FINANCIAL STATEMENTS

CULP, INC.
CONSOLIDATED STATEMENTS OF LOSS
FOR THE THREE MONTHS AND NINE MONTHS ENDED JANUARY 28, 2007 AND JANUARY 29, 2006
(UNAUDITED)

(Amounts in Thousands, Except for Per Share Data)

THREE MONTHS EN

		Amounts		
		January 28, 2007	January 29, 2006	% Over (Under)
Net sales	$	55,712	61,035	(8.7)%
Cost of sales		51,001	56,858	(10.3)%
Gross profit		4,711	4,177	12.8 %
Selling, general and administrative expenses		6,394	6,098	4.9 %
Restructuring expense		1,275	343	271.7 %
Loss from operations		(2,958)	(2,264)	(30.7)%
Interest expense		952	1,063	(10.4)%
Interest income		(50)	(43)	16.3 %
Other (income) expense		(157)	135	216.3 %
Loss before income taxes		(3,703)	(3,419)	(8.3)%
Income taxes*		(1,482)	(1,250)	18.6 %
Net loss	$	(2,221)	(2,169)	(2.4)%
Net loss per share-basic		($0.19)	($0.19)	0.0 %
Net loss per share-diluted		($0.19)	($0.19)	0.0 %
Average shares outstanding-basic		11,773	11,562	1.8 %
Average shares outstanding-diluted		11,773	11,562	1.8 %

NINE MONTHS EN

		Amounts		
		January 28, 2007	January 29, 2006	% Over (Under)
Net sales	$	177,337	190,383	(6.9)%
Cost of sales		156,575	174,098	(10.1)%
Gross profit		20,762	16,285	27.5 %
Selling, general and administrative expenses		19,240	22,480	(14.4)%
Restructuring expense		1,742	6,581	(73.5)%
Loss from operations		(220)	(12,776)	98.3 %
Interest expense		2,841	2,955	(3.9)%
Interest income		(147)	(78)	88.5 %
Other (income) expense		(98)	481	120.4 %
Loss before income taxes		(2,816)	(16,134)	82.5 %
Income taxes*		(1,540)	(5,873)	(73.8)%

Net loss	$	(1,276)	(10,261)	87.6 %
Net loss per share-basic		($0.11)	($0.89)	87.6 %
Net loss per share-diluted		($0.11)	($0.89)	87.6 %
Average shares outstanding-basic		11,710	11,557	1.3 %
Average shares outstanding-diluted		11,710	11,557	1.3 %

* Percent of sales column for income taxes is calculated as a % of loss before income taxes.

See accompanying notes to consolidated financial statements

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CULP, INC.
CONSOLIDATED BALANCE SHEETS
JANUARY 28, 2007, JANUARY 29, 2006 AND APRIL 30, 2006
(UNAUDITED)

(Amounts in Thousands)

		Amounts		Inc (Dec
		January 28, 2007	January 29, 2006	Dollars
Current assets				
Cash and cash equivalents	$	10,675	12,870	(2,195
Accounts receivable		23,755	28,485	(4,730
Inventories		42,717	42,099	618
Deferred income taxes		7,120	7,054	66
Assets held for sale		1,231	-	1,231
Other current assets		2,710	1,649	1,061
Total current assets		88,208	92,157	(3,949
Property, plant & equipment, net		40,784	52,562	(11,778
Goodwill		4,114	4,114	-
Deferred income taxes		23,232	15,731	7,501
Other assets		2,683	1,775	908
Total assets	$	159,021	166,339	(7,318
Current liabilities				
Current maturities of long-term debt	$	4,744	8,049	(3,305
Accounts payable		18,051	20,669	(2,618
Accrued expenses		7,704	9,751	(2,047
Accrued restructuring		3,490	4,299	(809
Income taxes payable		4,136	635	3,501
Total current liabilities		38,125	43,403	(5,278
Long-term debt , less current maturities		41,965	47,229	(5,264

Total liabilities		80,090	90,632	(10,542
Shareholders' equity		78,931	75,707	3,224
Total liabilities and shareholders' equity	$	159,021	166,339	(7,318
Shares outstanding		12,555	11,566	989

* Derived from audited financial statements

See accompanying notes to consolidated financial statements

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CULP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED JANUARY 28, 2007 AND JANUARY 29, 2006
(UNAUDITED)

(Amounts in Thousands)

		NIN
		January 2 2007
Cash flows from operating activities:		
Net loss	$	(1
Adjustments to reconcile net loss to net cash provided by operating activities:		
Depreciation		5
Amortization of other assets		
Stock-based compensation		
Deferred income taxes		(3
Restructuring expenses, net of gain on sale of related assets		
Changes in assets and liabilities:		
Accounts receivable		5
Inventories		(1
Other current assets		
Other assets		
Accounts payable		(2
Accrued expenses		
Accrued restructuring		
Income taxes payable		1
Net cash provided by operating activities		4
Cash flows from investing activities:		
Capital expenditures		(2
Acquisition of assets		(2
Proceeds from the sale of buildings and equipment		3

Net cash used in investing activities		(1
Cash flows from financing activities:		
Payments on vendor-financed capital expenditures		
Payments on long-term debt		(3
Proceeds from issuance of long-term debt		2
Proceeds from common stock issued		
Net cash (used in) provided by financing activities		(1
Increase in cash and cash equivalents		
Cash and cash equivalents at beginning of period		9
Cash and cash equivalents at end of period	$	10

See accompanying notes to consolidated financial statements

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CULP, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(UNAUDITED)

(Dollars in thousands, except share data)

	Common Stock		Capital Contributed in Excess of Par Value	Unearned Compensation	Retained Earnings	C
	Shares	Amount				
Balance, May 1, 2005	11,550,759	$ 579	39,964	(139)	45,367	
Net loss	-	-	-	-	(11,796)	
Gain on cash flow hedge, net of income taxes	-	-	-	-	-	
Stock-based compensation	-	-	-	139	-	
Common stock issued in connection with stock option plans	104,200	5	386	-	-	
Balance, April 30, 2006	11,654,959	$ 584	40,350	-	33,571	
Net loss	-	-	-	-	(1,276)	
Loss on cash flow hedge, net of income taxes	-	-	-	-	-	
Stock-based compensation	-	-	406	-	-	
Common stock issued in connection with acquisition of assets (see Note 2)	798,582	40	5,057	-	-	

Common stock issued in connection with stock option plans	101,000	5	189	-	-	
Balance, January 28, 2007	12,554,541	$ 629	46,002	-	32,295	

See accompanying notes to consolidated financial statements

CULP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements of Culp, Inc. and subsidiaries (the "company") include all adjustments, which are, in the opinion of management, necessary for fair presentation of the results of operations and financial position. All of these adjustments are of a normal recurring nature except as disclosed in notes 2 and 11 to the consolidated financial statements. Results of operations for interim periods may not be indicative of future results. The unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements, which are included in the company's annual report on Form 10-K filed with the Securities and Exchange Commission on July 20, 2006 for the fiscal year ended April 30, 2006.

The company's nine months ended January 28, 2007 and January 29, 2006 represent 39 week periods.

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2. ASSET ACQUISITION

In January 2007, the company closed on an Asset Purchase Agreement (the "Agreement") for the purchase of certain assets from International Textile Group, Inc. ("ITG") related to the mattress fabrics product line of ITG's Burlington House division. The company purchased ITG's mattress fabrics finished goods inventory, a credit on future purchases of inventory manufactured by ITG during the transition period, along with certain proprietary rights (patterns, copyrights, artwork, and the like) and other records that related to ITG's mattress fabrics product line. The company did not purchase any accounts receivable, property, plant, and equipment, and did not assume any liabilities other than certain open purchase orders.

The consideration given for this transaction, after adjustments to the closing date inventory as defined by the Agreement, was $8.1 million. Payment consisted of $2.5 million in cash financed by a term loan (see Note 8), the issuance of 798,582 shares of the company's common stock with a fair value of $5.1 million, and the company also incurred direct acquisition costs relating to legal, accounting, and other professional fees of $515,000. The total transaction cost allocation is not final based on the ultimate settlement of certain direct acquisition costs. The final allocation may impact the ultimate valuation of the assets acquired. This transaction did not constitute a business combination within the criteria of EITF 98-3, DETERMINING WHETHER A NON-MONETARY TRANSACTION INVOLVES RECEIPT OF PRODUCTIVE ASSETS OR OF A BUSINESS. The total transaction cost was allocated as follows:

(DOLLARS IN THOUSANDS)	Fair Value
Inventories	$ 4,754
Other current assets (credit on future purchases of inventory)	2,210
Non-compete agreement	1,148
	$ 8,112

The company recorded the non-compete agreement at its fair value based on various valuation techniques, which is reflected in other assets in the accompanying consolidated balance sheet. The non-compete agreement will be amortized on a straight-line basis over the four year life of the agreement. Amortization expense during the next five fiscal years follows: FY 2007 - $72,000; FY 2008 - $287,000; FY 2009 - $287,000; FY 2010 - $287,000; and FY 2011 - $215,000.

The Agreement requires ITG to provide certain transition services to the company and will manufacture goods for the company for a limited period of time (expected to be approximately 120 days) to support the company's efforts to transition the former ITG mattress fabrics products into the company's operations. The company does not plan to hire any of ITG's employees after the transition period is completed. ITG has also agreed that it will not compete with the company in the mattress fabrics business for a period of four years, except for mattress fabrics production in China for final consumption in China (meaning the mattress fabric and the mattress on which it is used is sold only in China).

In connection with the Agreement, the company issued 798,582 shares of common stock. As a result, the company entered into a Registration Rights and Shareholder Agreement ("the Registration Agreement"), which relates to the shares of the common stock issued by the company to ITG (the "Shares"). Under the terms of the Registration Agreement, ITG may demand that the company register the Shares with the Securities and Exchange Commission, which would allow the Shares to be sold to the public after the registration statement becomes effective. The Registration Agreement also contains provisions pursuant to which ITG will agree not to purchase additional company shares or take certain other actions to influence control of the company, and will agree to vote the shares in accordance with recommendations of the company's board of directors.

3. STOCK-BASED COMPENSATION

Effective May 1, 2006, the company began recording compensation expense associated with its stock option plans in accordance with SFAS No. 123R, "Share-Based Payment" which requires the measurement of the cost of employee services received in exchange for an award of an equity instrument based on the grant date fair value of the award. The company adopted the modified prospective transition method provided for under SFAS No. 123R, and consequently has not retroactively adjusted results from prior periods. Under this transition method, compensation expense associated with stock options recognized in the first quarter of fiscal 2007 now includes amortization related to the remaining unvested portion of all stock option awards granted prior to May 1, 2006, based on their grant date fair value estimated in accordance with the original provisions of SFAS No. 123, "Accounting for Stock-Based Compensation."

Prior to May 1, 2006, the company recognized compensation costs related to employee stock option plans utilizing the intrinsic value-based method prescribed by APB Opinion No. 25, "ACCOUNTING FOR STOCK ISSUED TO EMPLOYEES," and related interpretations. The company had also adopted the disclosure requirements of SFAS No. 123, "ACCOUNTING FOR STOCK-BASED COMPENSATION," as amended by SFAS No. 148, "ACCOUNTING FOR STOCK-BASED COMPENSATION TRANSITION AND DISCLOSURE." SFAS No. 123 required disclosure of pro-forma net income, earnings per share, and other information as if the fair value method of accounting for stock options and other equity instruments described in SFAS No. 123 had been adopted.

As a result of adopting SFAS No. 123R, the company recorded $119,000 and $406,000 of compensation expense for stock options within selling, general, and administrative expense for the three-month and nine-month periods ended January 28, 2007. In the prior year, the company recorded $35,000 and $139,000 of compensation expense for stock options that were required to be accounted for under the provisions of APB Opinion No. 25 for the three-month and nine-month periods ended January 29, 2006.

Prior to the adoption of SFAS No. 123R, the benefit of tax deductions in excess of recognized compensation costs were reported as an operating cash flow. SFAS No. 123R requires such benefits be recorded as financing cash flow rather than as a reduction of taxes paid within operating cash flow. For the nine-month period ended January 28, 2007, no tax benefits in excess of recognized compensation costs were realized from option exercises.

The remaining unrecognized compensation costs related to unvested awards at January 28, 2007, is $1.0 million which is expected to be recognized over a weighted average period of 2.7 years.

The following table illustrates the effect on net loss and net loss per share if the company had applied the fair value recognition provisions of SFAS No. 123 to options granted under the company's stock option plan for three-month and nine-month period ended January 29, 2006:

(DOLLARS IN THOUSANDS, EXCEPT PER SHARE DATA)	Three-Months Ended	Nine-Mont
Net loss, as reported	$ (2,169)	$
Add: Total stock-based employee compensation expense included in net loss, net of taxes	22	
Deduct: Total stock-based employee compensation expense determined under fair value-based method for all awards, net of taxes	(112)	
Pro forma net loss	$ (2,259)	$

Net loss per share:			
Basic - as reported	$	(0.19)	$
Basic - pro forma		(0.20)	
Diluted - as reported		(0.19)	
Diluted - pro forma		(0.20)	

Under the company's stock option plans, employees and directors may be granted options to purchase shares of common stock at the fair market value on the date of grant. Options granted under these plans generally vest over four years and expire five to ten years after the date of grant. The fair value of each option award was estimated on the date of grant using a Black-Scholes option-pricing model. The fair value of stock options granted to directors during the nine-month period ended January 28, 2007 and January 29, 2006 were $3.68 and $3.52 per share using the following assumptions:

	2007	2006
Risk-free interest rate	4.57%	4.39%
Dividend yield	0.00%	0.00%
Expected volatility	68.36%	73.93%
Expected term (in years)	6.8	8.5

CULP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

The fair value of stock options granted to employees during the nine-month period ended January 28, 2007 and January 29, 2006 were $2.43 and $2.47 per share using the following assumptions:

	2007	2006
Risk-free interest rate	5.03%	4.39%
Dividend yield	0.00%	0.00%
Expected volatility	67.03%	73.93%
Expected term (in years)	1.6	3.5

The assumptions utilized in the model are evaluated and revised, as necessary, to reflect market conditions and actual historical experience. The risk-free interest rate for periods within the contractual life of the option was based on the U.S. Treasury yield curve in effect at the time of grant. The dividend yield was calculated based on the company's annual dividend as of the option grant date. The expected volatility was derived using a term structure based on historical volatility and the volatility implied by exchange-traded options on the company's common stock. The expected term of the options is the contractual term of the stock options and expected employee exercise and post-vesting employment termination trends.

The following table summarizes the stock options (vested and unvested) as of January 28, 2007, and option activity during the nine-month period then ended:

	Shares	Weighted-Average Exercise Price	Weighted-Average Contractual Term	Aggregate Intrinsic Value
Outstanding, April 30, 2006	993,875	$ 7.11		
Granted	228,000	4.56		
Expired	(180,125)	6.38		
Exercised	(101,000)	1.92		$ 292,
Outstanding, January 28, 2007	940,750	7.19	3.1 Years	$ 820,

At January 28, 2007, there were 254,750 shares available for future grants under the company's incentive stock option plans and options to purchase 478,375 shares were exercisable which had a weighted average exercise price of $9.39 per share, an aggregate intrinsic value of $166,130 and a weighted average contractual term of 0.18 years. Cash received from stock options were $194,000 and $57,000 for the nine-month periods ended January 28, 2007 and January 29, 2006, respectively.

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CULP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

4. ACCOUNTS RECEIVABLE

A summary of accounts receivable follows:

(DOLLARS IN THOUSANDS)	January 28, 200
Customers	$ 26,
Allowance for doubtful accounts	(1,
Reserve for returns and allowances and discounts	(1,
	$ 23,

A summary of the activity in the allowance for doubtful accounts follows:

(DOLLARS IN THOUSANDS)	Ni January 28, 200
Beginning balance	$ (1,
Provision for uncollectible accounts	(
Net write-offs	
Ending balance	$ (1,

A summary of the activity in the allowance for returns and allowances and discounts accounts follows:

(DOLLARS IN THOUSANDS)	Ni January 28, 200
Beginning balance	$ (
Provision for returns and allowances and discounts	(1,
Discounts taken	1,
Ending balance	$ (1,

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5. INVENTORIES

Inventories are carried at the lower of cost or market. Cost is determined using the FIFO (first-in, first-out) method.

A summary of inventories follows:

(DOLLARS IN THOUSANDS)	January 28, 200
Raw materials	$ 11,
Work-in-process	1,
Finished goods	29,
	$ 42,

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CULP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

6. ACCOUNTS PAYABLE

A summary of accounts payable follows:

(DOLLARS IN THOUSANDS)	January 28, 2007	April
Accounts payable-trade	$ 16,392	$
Accounts payable-capital expenditures	1,659	
	$ 18,051	$

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7. ACCRUED EXPENSES

A summary of accrued expenses follows:

(DOLLARS IN THOUSANDS)	January 28, 2007	April
Compensation, commissions and related benefits	$ 4,312	$
Interest	742	
Accrued rebates	403	
Other	2,247	
	$ 7,704	$

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8. LONG-TERM DEBT

A summary of long-term debt follows:

(DOLLARS IN THOUSANDS)	January 28, 2007	April
Unsecured senior term notes	$ 39,440	$
Real estate loan - I	4,091	
Real estate loan - II	2,500	
Canadian government loans	678	
	46,709	
Less current maturities	(4,744)	
	$ 41,965	$

UNSECURED TERM NOTES

The company's unsecured term notes (the "Notes") are payable over an average remaining term of 2.5 years beginning February 2007 through March 2010. As of January 28, 2007, the principal payments that are required to be paid in periodic installments over the next four years are as follows: Year 1 - $4.5 million; Year 2 - $19.9 million; Year 3 - $7.5 million; and Year 4 - $7.5 million.

On December 6, 2006, the company entered into a Second Amendment to Note Purchase Agreements (the "Amendment"). Upon execution of this amendment, the company prepaid $3.0 million in principal amount and interest on the Notes, without prepayment penalty or "make whole" premium. The Amendment raised the interest rate from 7.76% to 8.80% on the remaining outstanding Notes and allows for an increase in the amount of other debt to be incurred by the company, including a provision that allows for debt of up to $5 million in the company's China subsidiary. The Amendment changed the financial covenants applicable to the company to provide additional flexibility to account for recent changes that the company has made or could make to its business and the accounting consequences of those changes. Beginning in the third quarter of fiscal 2007, these changes exclude from the financial covenants, all restructuring and related charges associated with the U.S. upholstery fabrics operations and any valuation allowance, if needed, against the company's net deferred tax assets from U.S. operations. The Amendment provides for prepayments of the Notes (at the option of the noteholders and without prepayment penalty) to the extent that the company's cash balances exceed $8 million at the end of each fiscal quarter. The company paid the remaining $4.5 million due in March of 2007 on February 20, 2007, as part of this prepayment provision.

REAL ESTATE LOAN - I

The company has a real estate loan that is secured by a lien on the company's corporate headquarters office located in High Point, NC. This term loan bears interest at the one-month London Interbank Offered Rate plus an adjustable margin based on the company's debt/EBITDA ratio, as defined in the agreement and is payable in varying monthly installments through September 2010, with a final payment of $3.3 million in October 2010.

REAL ESTATE LOAN - II

On January 22, 2007, the company entered into an agreement with a bank to provide for a term loan in the amount of $2.5 million in connection with the ITG asset purchase agreement (see Note 2). This term loan is secured by a lien on the company's corporate headquarters office located in High Point, NC and bears interest at the one-month London Interbank Offered Rate plus 3%. This agreement requires the company to pay interest monthly with the entire principal amount of $2.5 million due on June 30, 2010.

CANADIAN GOVERNMENT LOANS

In November 2005, the company entered into an agreement with the Canadian government to provide for a term loan in the amount of $680,000. The proceeds are to partially finance capital expenditures at the company's facility located in Quebec, Canada. This loan is non-interest bearing and is payable in 48 equal monthly installments commencing December 1, 2009. In addition to the term loan entered into in November 2005, the company had an existing non-interest bearing term loan with the Canadian government which was paid in May 2006.

REVOLVING CREDIT AGREEMENT -UNITED STATES

On January 22, 2007, the company entered into a Tenth Amendment to this unsecured credit agreement dated August 23, 2002. This amendment reduced the line of credit available from $8.0 million to $6.5 million, including letters of credit up to $5.5 million and extended the term of the credit agreement from August 31, 2007 to December 31, 2007. The amendment also removed the liquidity provision that required the company to maintain collected deposit balances of at least $2.0 million. It also amended certain other financial covenants as defined in the agreement. Borrowings under the credit facility bear interest at the one-month London Interbank Offered Rate plus an adjustable margin based on the company's debt/EBITDA ratio, as defined in the agreement. As of January 28, 2007, there were $2.4 million in outstanding letters of credit (most of which related to workers compensation) and no borrowings outstanding under the agreement.

REVOLVING CREDIT AGREEMENT - CHINA

On February 1, 2007, the company's China subsidiary entered into an unsecured credit agreement with a bank to provide a line of credit available up to approximately $5.0 million, of which approximately $1.3 million includes letters of credit. The credit agreement expires on February 1, 2008 with an annual renewal option, and requires interest to be paid on a quarterly basis at a fixed annual rate of 5.8%. As of March 9, 2007, approximately $1.3 million was outstanding under the agreement.

OVERALL

The company's loan agreements require that the company maintain compliance with certain financial ratios. At January 28, 2007, the company was in compliance with these financial covenants.

As of January 28, 2007, the principal payment requirements of long-term debt during the next five years are: Year 1 - $4.7 million; Year 2 - $20.1 million; Year 3 - $7.8 million; Year 4 - $13.5 million; Year 5 - $169,000; and thereafter - $480,000.

9. INTEREST RATE HEDGING

In connection with the company's first real estate loan with its bank, the company was required to have an agreement to hedge the interest rate risk exposure on the first real estate loan. The company entered into a $2,170,000 notional principal interest rate swap, which represents 50% of the principal amount of the first real estate loan, that effectively converted the floating rate LIBOR based payments to fixed payments at 4.99% plus the spread calculated under the first real estate loan agreement. This agreement expires October 2010.

The company accounts for the interest rate swap as a cash flow hedge whereby the fair value of this contract is reflected in other assets in the accompanying consolidated balance sheets with the offset recorded as accumulated other comprehensive income. The fair value of the interest rate swap at January 28, 2007 was $9,000 in the company's favor and was determined by quoted market prices.

10. CASH FLOW INFORMATION

Payments for interest and income taxes follow:

	Nine months ended	
(DOLLARS IN THOUSANDS)	January 28, 2007	January 29, 2006
Interest	$ 2,532	$ 2,048
Income taxes (received) paid	(156)	892

The company did not finance any of its capital expenditures for the nine months ended January 28, 2007. The non-cash portion of capital expenditures representing vendor financing totaled $1,699,000 for the nine months ended January 29, 2006.

In connection with the ITG Asset Purchase Agreement (see Note 2), the company issued 798,582 shares of common stock with a fair value of $5.1 million.

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11. RESTRUCTURING AND RELATED CHARGES

A summary of accrued restructuring costs follows:

(DOLLARS IN THOUSANDS)	January 28, 2007	April 30, 2006
December 2006 Upholstery Fabrics	$ 1,284	$ -
September 2005 Upholstery Fabrics	313	439
August 2005 Upholstery Fabrics	59	134
April 2005 Upholstery Fabrics	289	1,000
October 2004 Upholstery Fabrics	6	64
Fiscal 2003 Culp Decorative Fabrics	1,539	2,412
Fiscal 2001 Culp Decorative Fabrics	-	5
	$ 3,490	$ 4,054

DECEMBER 2006 UPHOLSTERY FABRICS

On December 12, 2006, the company's board of directors approved a restructuring plan within the upholstery fabrics segment to consolidate the company's U.S. upholstery fabrics manufacturing facilities and outsource its specialty yarn production. This process will involve closing the company's weaving plant located in Graham, NC, and closing the yarn plant located in Lincolnton, NC. The company will transfer certain production from the Graham, NC plant facility to its Anderson, SC and Shanghai, China, plant facilities as well as a small portion to contract weavers. The company will continue to operate one upholstery fabrics plant in Anderson, SC, which will produce velvets and decorative fabrics. As a result of these two plant closures, the company will reduce the number of associates by approximately 185 people.

During the third quarter and the nine-month period of fiscal 2007, total restructuring and related charges incurred were $4.1 million of which $2.2 million related to inventory markdowns, $1.3 million related to employee termination benefits, and $665,000 related to accelerated depreciation. Of the total charge, $2.8 million was recorded in cost of sales and $1.3 million was recorded in restructuring expense in the 2007 Consolidated Statement of Loss.

The balance of $1.3 million in accrued restructuring costs represents the employee termination benefits incurred. As of January 28, 2007, there were no assets classified as held for sale.

SEPTEMBER 2005 UPHOLSTERY FABRICS

During the third quarter of fiscal 2007, a total restructuring and related net credit of $20,000 was recorded, of which, a charge of $14,000 related to lease termination costs, a charge of $3,000 related to asset movement costs, and a credit of $37,000 related to employee termination benefits. The $20,000 net credit was recorded in restructuring expense in the 2007 Consolidated Statement of Loss.

During the nine-month period of fiscal 2007, total restructuring and related net charges incurred were $512,000, of which, a charge of $450,000 related to operating costs associated with the closing of a plant facility, a charge of $273,000 related to lease termination and other exit costs, a charge of $212,000 related to asset movement costs, a credit of $40,000 related to a write-down of a building, a credit of $148,000 related to employee termination benefits, and a credit of $235,000 for sales proceeds received on equipment with no carrying value. Of the total net charge, a charge of $62,000 was recorded in restructuring expense and a charge of $450,000 was recorded in cost of sales in the 2007 Consolidated Statement of Loss.

The following summarizes the fiscal 2007 activity in the restructuring accrual (dollars in thousands):

		Employee Termination Benefits	Lease Termination and Other Exit Costs	Total
Balance, April 30, 2006	$	439	-	439
Adjustments in fiscal 2007		(148)	2	(146)
Additions in fiscal 2007		-	271	271
Paid in fiscal 2007		(210)	(41)	(251)
Balance, January 28, 2007	$	81	232	313

As of January 28, 2007, there were no assets classified as held for sale. At April 30, 2006, assets classified as held for sale consisted of a building with a carrying value of $641,000.

AUGUST 2005 UPHOLSTERY FABRICS

During the third quarter of fiscal 2007, a total restructuring and related net credit of $245,000 was recorded, of which, a charge of $272,000 related to write-downs of equipment, a charge of $6,000 related to lease termination costs, a credit of $21,000 related to employee termination benefits, a credit of $68,000 related to other operating costs associated with the closing of a plant facility, and a credit of $434,000 for sales proceeds received on equipment with no carrying value. Of the total net credit, a credit of $177,000 was recorded in restructuring expense and a credit of $68,000 was recorded in cost of sales in the 2007 Consolidated Statement of Loss.

During the nine month period of fiscal 2007, a total restructuring and related net credit of $146,000 was recorded, of which, a charge of $307,000 related to write-downs of a building and equipment, a charge of $49,000 related to asset movement costs, a charge of $6,000 related to lease termination costs, a charge of $2,000 related to employee termination benefits, a credit of $19,000 for other operating costs associated with the closing of a plant facility, and a credit of $491,000 for sales proceeds received on equipment with no carrying value. Of the total net credit, a credit of $127,000 was recorded in restructuring expense and a credit of $19,000 was recorded in cost of sales in the 2007 Consolidated Statement of Loss.

The following summarizes the fiscal 2007 activity in the restructuring accrual (dollars in thousands):

	Employee Termination Benefits	Lease Termination and Other Exit Costs	Total
Balance, April 30, 2006	$ 127	7	134
Adjustments in fiscal 2007	2	-	2
Addition in fiscal 2007	-	6	6
Paid in fiscal 2007	(70)	(13)	(83)
Balance, January 28, 2007	$ 59	-	59

As of January 28, 2007 and April 30, 2006, assets classified as held for sale consisted of equipment with a carrying value of $360,000 and $700,000, respectively. As of April 30, 2006, assets classified as held for sale also included a building with a carrying value of $475,000, which was sold in May 2006.

APRIL 2005 UPHOLSTERY FABRICS

During the third quarter of fiscal 2007, total restructuring and related net charges incurred were $223,000, of which, a charge of $171,000 related to asset movement costs, a charge of $47,000 related to lease termination costs, a charge of $35,000 related to operating costs associated with closing a plant facility, a credit of $10,000 related to employee termination benefits, and a credit of $20,000 for sales proceeds received on equipment with no carrying value. Of the total net charge, a charge of $188,000 was recorded in restructuring expense and a charge of $35,000 was recorded in cost of sales in the 2007 Consolidated Statement of Loss.

During the first nine months of fiscal 2007, total restructuring and related net charges incurred were $1.1 million, of which, a charge of $653,000 related to asset movement costs, a charge of $321,000 related to operating costs associated with the closing of a plant facility, a charge of $238,000 related to inventory markdowns, a charge of $138,000 related to lease termination costs, a charge of $67,000 related to write-downs of equipment, a credit of $112,000 related to employee termination benefits, and a credit of $164,000 for sales proceeds received on equipment with no carrying value. Of the total net charge, a charge of $582,000 was recorded in restructuring expense; a charge of $501,000 was recorded in cost of sales; and a charge of $58,000 was recorded in selling, general, and administrative expenses in the 2007 Consolidated Statements of Loss.

The following summarizes the fiscal 2007 activity in the restructuring accrual (dollars in thousands):

	Employee Termination Benefits	Lease Termination and Other Exit Costs	Total
Balance, April 30, 2006	$ 799	201	1,000

Adjustments in fiscal 2007		(112)	10	(102)
Additions in fiscal 2007		-	128	128
Paid in fiscal 2007		(477)	(260)	(737)
Balance, January 28, 2007	$	210	79	289

As of January 28, 2007 and April 30, 2006, assets classified as held for sale consisted of equipment with a carrying value of approximately $871,000 and $1.3 million, respectively.

OCTOBER 2004 UPHOLSTERY FABRICS

During the first nine months of fiscal 2007, as a result of management's continual evaluation of the restructuring accrual, the reserve was decreased by $30,000 to reflect current estimates of future health care claims. This $30,000 decrease in the reserve was recorded as a credit to restructuring expense in the 2007 Consolidated Statement of Loss.

The following summarizes the fiscal 2007 activity in the restructuring accrual (dollars in thousands):

		Employee Termination Benefits	Lease Termination and Other Exit Costs	Total
Balance, April 30, 2006	$	64	-	64
Adjustments in fiscal 2007		(30)	-	(30)
Paid in fiscal 2007		(28)	-	(28)
Balance, January 28, 2007	$	6	-	6

As of January 28, 2007 and April 30, 2006, there were no assets classified as held for sale.

FISCAL 2003 CULP DECORATIVE FABRICS RESTRUCTURING

During the third quarter of fiscal 2007, the company recorded a restructuring related charge of $8,000 for operating costs associated with a closed plant facility. This $8,000 restructuring related charge was recorded in cost of sales in the 2007 Consolidated Statement of Loss.

During the first nine months of fiscal 2007, as a result of management's continual evaluation of the restructuring accrual, the reserve was decreased by approximately $22,000 to reflect current estimates of sub-lease income and other exit costs. This $22,000 decrease in the reserve was recorded as a credit to restructuring expense in the 2007 Consolidated Statement of Loss. Additionally, the company recorded a restructuring related charge of $24,000 for operating costs associated with a closed plant facility. This $24,000 restructuring related charge was recorded in cost of sales in the 2007 Consolidated Statement of Loss.

The following summarizes the fiscal 2007 activity in the restructuring accrual (dollars in thousands):

		Employee Termination Benefits	Lease Termination and Other Exit Costs	Total
Balance, April 30, 2006	$	88	2,324	2,412
Adjustments in fiscal 2007		-	(22)	(22)
Paid in fiscal 2007		(34)	(817)	(851)
Balance, January 28, 2007	$	54	1,485	1,539

As of January 28, 2007 and April 30, 2006, there were no assets classified as held for sale.

FISCAL 2001 CULP DECORATIVE FABRICS RESTRUCTURING

During the first nine months of fiscal 2007, as a result of management's continual evaluation of the restructuring accrual, the reserve was decreased by approximately $5,000 to reflect current estimates of future health care claims. This $5,000 decrease in the reserve was recorded as a credit to restructuring expense in the 2007 Consolidated Statement of Loss. Additionally, the company recorded a restructuring related charge of $26,000 for other operating costs associated with a closed plant facility. This $26,000 restructuring related charge was recorded in cost of sales in the 2007 Consolidated Statement of Loss.

The following summarizes the fiscal 2007 activity in the restructuring accrual (dollars in thousands):

		Employee Termination Benefits	Lease Termination and Other Exit Costs	Total
Balance, April 30, 2006	$	5	-	5
Adjustments in fiscal 2007		(5)	-	(5)
Paid in fiscal 2007		-	-	-
Balance, January 28, 2007	$	-	-	-

As of January 28, 2007 and April 30, 2006, there were no assets classified as held for sale.

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12. NET LOSS PER SHARE

Basic net loss per share is computed using the weighted-average number of shares outstanding during the period. Diluted net loss per share uses the weighted-average number of shares outstanding during the period plus the dilutive effect of stock options calculated using the treasury stock method. Weighted average shares used in the computation of basic and diluted net income loss per share follows:

(AMOUNTS IN THOUSANDS)	Three months ended January 28, 2007	January 29, 2006
Weighted-average common shares outstanding, basic	11,773	11,562
Effect of dilutive stock options	-	-
Weighted-average common shares outstanding, diluted	11,773	11,562

Options to purchase 458,750 and 498,125 shares of common stock were not included in the computation of diluted net loss per share for the three months ended January 28, 2007, and January 29, 2006, respectively, because the exercise price of the options was greater than the average market price of the common shares.

Options to purchase 2,847 and 74,129 shares of common stock were not included in the computation of diluted net loss per share for the three months ended January 28, 2007, and January 29, 2006, because the company incurred a net loss for the period.

(AMOUNTS IN THOUSANDS)	Nine months ended January 28, 2007	January 29, 2006
Weighted average common shares outstanding, basic	11,710	11,557
Effect of dilutive stock options	-	-
Weighted average common shares outstanding, diluted	11,710	11,557

Options to purchase 452,792 and 506,542 shares of common stock were not included in the computation of diluted net loss per share for the nine months ended January 28, 2007, and January 29, 2006, respectively, because the exercise price of the options was greater than the average market price of the common shares.

Options to purchase 3,168 and 52,824 shares of common stock were not included in the computation of diluted net loss per share for the nine months ended January 28, 2007, and January 29, 2006, because the company incurred a net loss for the period.

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13. SEGMENT INFORMATION

The company's operations are classified into two segments: mattress fabrics and upholstery fabrics. The mattress fabrics segment principally manufactures, sources, and sells fabrics to bedding manufacturers. The upholstery fabrics segment principally manufactures, sources, and sells fabrics primarily to residential and commercial (contract) furniture manufacturers.

Financial information for the company's operating segments follow:

(DOLLARS IN THOUSANDS)	Three months ended January 28, 2007		Three months ended January 29, 2006
Net sales:			
Mattress Fabrics	$ 24,396		$ 22,681
Upholstery Fabrics	31,316		38,354
	$ 55,712		$ 61,035
Gross profit:			
Mattress Fabrics	$ 4,215		$ 3,442
Upholstery Fabrics	3,269		2,070
Total segment gross profit	7,484		5,512
Restructuring related charges	(2,773)	(1)	(1,335)
	$ 4,711		$ 4,177
Selling, general, and administrative expenses:			
Mattress Fabrics	$ 1,706		$ 1,643
Upholstery Fabrics	3,765		3,717
Total segment selling, general, and administrative expenses	5,471		5,360
Unallocated corporate expenses	895		738
Restructuring related charges	28	(1)	-
	$ 6,394		$ 6,098
Operating income (loss):			
Mattress Fabrics	$ 2,509		$ 1,799
Upholstery Fabrics	(496)		(1,647)
Total segment operating income	2,013		152
Unallocated corporate expenses	(895)		(738)
Restructuring expense	(1,275)	(2)	(343)
Restructuring related charges	(2,801)	(1)	(1,335)
	$ (2,958)		$ (2,264)

(1) The $2.8 million represents restructuring related charges of $2.2 million for inventory markdowns, $665,000 for accelerated depreciation, and a credit of $24,000 for other operating costs associated with the closing of plant facilities. These charges relate to the Upholstery Fabrics segment.

(2) The $1.3 million represents restructuring expenses of $1.2 million for employee termination benefits, $272,000 for write-downs of equipment, $181,000 for asset movement costs, $61,000 for lease termination costs, and a credit of $455,000 for sales proceeds received on equipment with no carrying value. These charges relate to the Upholstery Fabrics segment.

(3) The $1.3 million represents restructuring related charges of $838,000 for inventory markdowns, $389,000 for other operating costs associated with

the closing of plant facilities, and $108,000 for accelerated depreciation. These charges relate to the Upholstery Fabrics segment.

(4) The $343,000 represents restructuring expenses of $371,000 for asset movement costs, $133,000 for employee termination benefits, and $51,000 for lease termination costs, a credit of $77,000 for sales proceeds received on equipment with no carrying value, and a credit of $135,000 to reflect current estimates of sub-lease income. These charges relate to the Upholstery Fabrics segment.

	Nine months ended				
(DOLLARS IN THOUSANDS)	January 28, 2007			January 29	
Net sales:					
Mattress Fabrics	$	69,734		$	69,
Upholstery Fabrics		107,603			120,
	$	177,337		$	190,
Gross profit:					
Mattress Fabrics	$	11,880		$	9,
Upholstery Fabrics		12,691			10,
Total segment gross profit		24,571			19,
Restructuring related charges		(3,809)	(5)		(3,
	$	20,762		$	16,
Selling, general, and administrative expenses:					
Mattress Fabrics	$	5,043		$	5,
Upholstery Fabrics		11,219			12,
Total segment selling, general, and administrative expenses		16,262			17,
Unallocated corporate expenses		2,920			2,
Restructuring related charges		58	(5)		3,
	$	19,240		$	22,
Operating income (loss):					
Mattress Fabrics	$	6,837		$	4,
Upholstery Fabrics		1,472			(2,
Total segment operating income		8,309			2,
Unallocated corporate expenses		(2,920)			(2,
Restructuring expense		(1,742)	(6)		(6,
Restructuring related charges		(3,867)	(5)		(6,
	$	(220)		$	(12,

(5) The $3.9 million represents restructuring related charges of $2.3 million for inventory markdowns, $802,000 for other operating costs associated with the closing of plant facilities, and $665,000 for accelerated depreciation. These charges relate to the Upholstery Fabrics segment.

(6) The $1.7 million represents restructuring expenses of $990,000 for employee termination benefits, $914,000 for asset movement costs, $395,000 for lease termination and other exit costs, $334,000 for write-downs of buildings and equipment, and a credit of $890,000 for sales proceeds on equipment with no carrying value. These charges relate to the Upholstery Fabrics segment.

(7) The $3.6 million represents restructuring related charges of $1.9 million for accelerated depreciation, $1.2 million for inventory markdowns, and $455,000 for other operating costs associated with the closing of plant facilities. These charges primarily relate to the Upholstery Fabrics segment.

(8) The $3.0 million represents accelerated depreciation. These charges primarily relate to the Upholstery Fabrics segment.

(9) The $6.6 million represents restructuring expenses of $2.8 million for write-downs of buildings and equipment, $1.9 million for asset movement costs, $1.5 million for employee termination benefits, and $292,000 for lease termination costs. These charges primarily relate to the Upholstery Fabrics segment.

(10) The $6.6 million represents restructuring related charges of $4.9 million for accelerated deprecation, $1.2 million for inventory markdowns, and $455,000 for other operating costs associated with the closing of plant facilities. These charges primarily relate to the Upholstery Fabrics segment. Balance sheet information for the company's operating segments follow:

(DOLLARS IN THOUSANDS)	January 28, 2007	April 30, 2006
Segment assets:		
Mattress Fabrics		
Current assets (13)	$ 28,338	$ 21,179
Property, plant and equipment (11)	22,600	25,357
Total mattress fabrics assets	50,938	46,536
Upholstery Fabrics		
Current assets (13)	38,134	44,563
Assets held for sale	1,231	3,111
Property, plant and equipment (12)	18,140	19,229
Total upholstery fabrics assets	57,505	66,903

Total segment assets	108,443	113,439
Non-segment assets:		
Cash and cash equivalents	10,675	9,714
Deferred income taxes	30,352	27,296
Other current assets	2,710	1,287
Property, plant & equipment	44	53
Goodwill	4,114	4,114
Other assets	2,683	1,564
Total assets	$ 159,021	$ 157,467

	Three months ended	
(DOLLARS IN THOUSANDS)	January 28, 2007	January 29, 2006
Capital expenditures:		
Mattress Fabrics	$ 78	$ 134
Upholstery Fabrics	506	256
	$ 584	$ 390
Depreciation expense:		
Mattress Fabrics	$ 912	$ 965
Upholstery Fabrics	710	1,366
Total segment depreciation expense	1,622	2,331
Accelerated depreciation	665	108
	$ 2,287	$ 2,439

CULP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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	Nine months ended	
(DOLLARS IN THOUSANDS)	January 28, 2007	January 29, 2006
Capital expenditures:		
Mattress Fabrics	$ 132	$ 3,550
Upholstery Fabrics	2,497	2,263
	$ 2,629	$ 5,813
Depreciation expense:		
Mattress Fabrics	$ 2,771	$ 2,714
Upholstery Fabrics	2,215	4,582

Total segment depreciation expense	4,986	7,296
Accelerated depreciation	665	4,979
	$ 5,651	$ 12,275

(11) Included in property, plant, and equipment are assets located in the U.S. totaling $12.0 million and $12.9 million at January 28, 2007 and April 30, 2006, respectively.

(12) Included in property, plant, and equipment are assets located in the U.S. totaling $10.6 million and $13.8 million at January 28, 2007 and April 30, 2006, respectively. Included in this U.S. property, plant, and equipment are various other corporate allocations totaling $3.9 million and $4.1 million at January 28, 2007 and April 30, 2006, respectively.

(13) Current assets represent accounts receivable and inventory for the respective segment.

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14. RECENT ACCOUNTING PRONOUNCEMENTS

In June 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes" ("FIN No. 48") which clarifies the criteria for the recognition of tax benefits under SFAS No. 109, "Accounting for Income Taxes." This Interpretation prescribes a comprehensive model for financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken, or expected to be taken, in income tax returns. FIN No. 48 is effective for fiscal years beginning after December 15, 2006 and requires that the cumulative effect of applying its provisions be disclosed as a one-time, non-cash charge or credit against the opening balance of retained earnings in the year of adoption. This Interpretation will be adopted by the company in the first quarter of fiscal 2008. The company is currently evaluating the potential impact of FIN No. 48 and any impact on its financial position cannot be readily determined at this time.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements," which provides enhanced guidance for using fair value to measure assets and liabilities. SFAS No. 157 establishes a common definition of fair value, provides a framework for measuring fair value under accounting principles generally accepted in the United States and expands disclosure requirements about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and is effective for the company in the first quarter of fiscal 2009. The company is currently evaluating the impact, if any, the adoption of SFAS No. 157 will have on its consolidated financial statements.

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CULP, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(UNAUDITED)

In February 2007, the FASB issued Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities." This statement, which is expected to expand fair value measurement, permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007 and is effective for the company in the first quarter of fiscal 2009. The company is currently evaluating the impact, if any, the adoption of SFAS No. 159 will have on its consolidated financial statements.

In September 2006, the SEC staff issued Staff Accounting Bulletin (SAB) No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements." SAB No. 108 was issued in order to eliminate the diversity of practice surrounding how public companies quantify financial statement misstatements. This SAB establishes a "dual approach" methodology that requires quantification of financial statement misstatements based on the effects of the misstatements on each of the company's financial statements (both the statement of operations and statement of financial position). The SEC has stated SAB No. 108 should be applied no later than the annual financial statements for the first fiscal year ending after November 15, 2006. SAB No. 108 permits a company to elect either a retrospective or prospective application. Prospective application requires recording a cumulative effect adjustment in the period of adoption, as well as detailed disclosure of the nature and amount of each individual error being corrected through the cumulative adjustment and how and when it arose. The company is currently evaluating the impact, if any, the application of SAB No 108 will have on the consolidated financial statements.

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CAUTIONARY STATEMENT CONCERNING FORWARD-LOOKING INFORMATION

This report and the exhibits attached hereto contain statements that may be deemed "forward-looking statements" within the meaning of the federal securities laws, including the Private Securities Litigation Reform Act of 1995 (Section 27A of the Securities Act of 1933 and Section 27A of the Securities and Exchange Act of 1934). Such statements are inherently subject to risks and uncertainties. Further, forward looking statements are intended to speak only as of the date on which they are made. Forward-looking statements are statements that include projections, expectations or beliefs about future events or results or otherwise are not statements of historical fact. Such statements are often but not always characterized by qualifying words such as "expect," "believe," "estimate," "plan" and "project" and their derivatives, and include but are not limited to statements about expectations for the company's future operations or success, sales, gross profit margins, operating income, SG&A or other expenses, and earnings, as well as any statements regarding future economic or industry trends or future developments. Factors that could influence the matters discussed in such statements include the level of housing starts and sales of existing homes, consumer confidence, trends in disposable income, and general economic conditions. Decreases in these economic indicators could have a negative effect on the company's business and prospects. Likewise, increases in interest rates, particularly home mortgage rates, and increases in consumer debt or the general rate of inflation, could affect the company adversely. In addition, changes in consumer preferences for various categories of furniture coverings, as well as changes in costs to produce such products (including import duties and quotas or other import costs) can have significant effect on demand for the company's products. Also, changes in the value of the U.S. dollar versus other currencies can affect the company's financial results because a significant portion of the company's operations are located outside the United States. Further, economic and political instability in international areas could affect the company's operations or sources of goods in those areas, as well as demand for the company's products in international markets. The company's level of success in integrating the acquisition of assets described in Item 2 and in capturing and retaining sales to customers related to the acquisition, will affect the company's ability to meet its sales goals. Finally, unanticipated delays or costs in executing restructuring actions could cause the cumulative effect of restructuring actions to fail to meet the objectives set forth by management.

Further information about these factors, as well as other factors that could affect the company's future operations or financial results are discussed in Item 1A.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

RESULTS OF OPERATIONS

The following analysis of financial condition and results of operations should be read in conjunction with the Financial Statements and Notes and other exhibits included elsewhere in this report.

OVERVIEW

Culp, Inc. (or the "company") has two operating segments - mattress fabrics and upholstery fabrics. The company manufactures, sources and markets fabrics that are used primarily in the production of bedding products and residential and commercial upholstered furniture, including mattresses, box springs, mattress sets, sofas, recliners, chairs, loveseats, sectionals, sofa-beds, and office seating. The company primarily markets fabrics that have broad appeal in the "good" and "better" priced categories of furniture and bedding. Management believes that Culp is the largest producer of mattress fabrics in North America, as measured by total sales, and one of the two largest marketers of upholstery fabrics for furniture in North America, again measured by total sales.

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The company's executive offices are located in High Point, North Carolina. The company was organized as a North Carolina corporation in 1972 and made its initial public offering in 1983. Since 1997, the company has been listed on the New York Stock Exchange and traded under the symbol "CFI." The company's fiscal year is the 52 or 53 week period ending on the Sunday closest to April 30. The company's nine months ended January 28, 2007, and January 29, 2006, represent 39 week periods.

The following tables set forth the company's net sales, gross profit, selling, general and administrative expenses and operating income (loss) by segment for the three and nine months ended January 28, 2007 and January 29, 2006.

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CULP, INC. FINANCIAL INFORMATION RELEASE
SALES, GROSS PROFIT AND OPERATING INCOME (LOSS) BY SEGMENT
FOR THE THREE MONTHS ENDED JANUARY 28, 2007 AND JANUARY 29, 2006

(Amounts in thousands)

		THREE MONTHS ENDED (UNAUD			
		Amounts			
Net Sales by Segment		January 28, 2007	January 29, 2006	% Over (Under)	Jan
Mattress Fabrics	$	24,396	22,681	7.6 %	
Upholstery Fabrics		31,316	38,354	(18.4)%	

Net Sales	$	55,712	61,035	(8.7)%	
Gross Profit by Segment					
Mattress Fabrics	$	4,215	3,442	22.5 %	
Upholstery Fabrics		3,269	2,070	57.9 %	
Subtotal		7,484	5,512	35.8 %	
Restructuring related charges		(2,773) (1)	(1,335) (3)	107.7 %	
Gross Profit	$	4,711	4,177	12.8 %	
Selling, General and Administrative expenses by Segment					
Mattress Fabrics	$	1,706	1,643	3.8 %	
Upholstery Fabrics		3,765	3,717	1.3 %	
Unallocated Corporate expenses		895	738	21.3 %	
		6,366	6,098	4.4 %	
Restructuring related charges		28 (1)	-	100.0 %	
Selling, General and Administrative expenses	$	6,394	6,098	4.9 %	
Operating Income (loss) by Segment					Ope
Mattress Fabrics	$	2,509	1,799	39.5 %	
Upholstery Fabrics		(496)	(1,647)	69.9 %	
Unallocated corporate expenses		(895)	(738)	21.3 %	
Subtotal		1,118	(586)	(290.8)%	
Restructuring expense		(1,275) (2)	(343) (4)	271.7 %	
Restructuring related charges		(2,801) (1)	(1,335) (3)	109.8 %	
Loss from operations	$	(2,958)	(2,264)	(30.7)%	
Depreciation by Segment					
Mattress Fabrics	$	912	965	(5.5)%	
Upholstery Fabrics		710	1,366	(48.0)%	
Subtotal		1,622	2,331	(30.4)%	
Accelerated Depreciation		665	108	515.7 %	
Total Depreciation	$	2,287	2,439	(6.2)%	

Notes:

(1) The $2.8 million represents restructuring related charges of $2.2 million for inventory markdowns, $665,000 for accelerated deprecation, and a credit

of $24,000 for other operating costs associated with the closing of plant facilities.

(2) The $1.3 million represents restructuring expenses of $1.2 million for employee termination benefits, $272,000 for write-downs of equipment, $181,000 for asset movement costs, $61,000 for lease termination costs, and a credit of $455,000 for sales proceeds received on equipment with no carrying value.

(3) The $1.3 million represents restructuring related charges of $838,000 for inventory markdowns, $389,000 for other operating costs associated with the closing of plant facilities, and $108,000 for accelerated depreciation.

(4) The $343,000 represents restructuring expenses of $371,000 for asset movement costs, $133,000 for employee termination benefits, $51,000 for lease termination costs, a credit of $77,000 for sales proceeds received on equipment with no carrying value, and a credit of $135,000 to reflect current estimates of sub-lease income.

CULP, INC. FINANCIAL INFORMATION RELEASE
SALES, GROSS PROFIT AND OPERATING INCOME (LOSS) BY SEGMENT
FOR THE NINE MONTHS ENDED JANUARY 28, 2007 AND JANUARY 29, 2006

(Amounts in thousands)

	NINE MONTHS ENDED (UNAUDITED			
	Amounts			Pe
Net Sales by Segment	January 28, 2007	January 29, 2006	% Over (Under)	Janua 20
Mattress Fabrics	$ 69,734	69,586	0.2 %	
Upholstery Fabrics	107,603	120,797	(10.9)%	
Net Sales	$ 177,337	190,383	(6.9)%	
Gross Profit by Segment				
Mattress Fabrics	$ 11,880	9,839	20.7 %	
Upholstery Fabrics	12,691	10,027	26.6 %	
Subtotal	24,571	19,866	23.7 %	
Restructuring related charges	(3,809) (1)	(3,581) (3)	6.4 %	
Gross Profit	$ 20,762	16,285	27.5 %	
Selling, General and Administrative expenses by Segment				
Mattress Fabrics	$ 5,043	5,016	0.5 %	
Upholstery Fabrics	11,219	12,120	(7.4)%	
Unallocated Corporate expenses	2,920	2,322	25.8 %	

Subtotal		19,182	19,458	(1.4)%	
Restructuring related charges		58 (1)	3,022 (4)	(98.1)%	
Selling, General and Administrative expenses	$	19,240	22,480	(14.4)%	
Operating Income (loss) by Segment					Opera
Mattress Fabrics	$	6,837	4,823	41.8 %	
Upholstery Fabrics		1,472	(2,093)	170.3 %	
Unallocated corporate expenses		(2,920)	(2,322)	25.8 %	
Subtotal		5,389	408	1,220.8 %	
Restructuring expense		(1,742)(2)	(6,581)(5)	(73.5)%	
Restructuring related charges		(3,867)(1)	(6,603)(3)(4)	(41.4)%	
Loss from operations	$	(220)	(12,776)	98.3 %	
Depreciation by Segment					
Mattress Fabrics	$	2,771	2,714	2.1 %	
Upholstery Fabrics		2,215	4,582	(51.7)%	
Subtotal		4,986	7,296	(31.7)%	
Accelerated Depreciation		665	4,979	(86.6)%	
Total Depreciation	$	5,651	12,275	(54.0)%	

Notes:

(1) The $3.9 million represents restructuring related charges of $2.3 million for inventory markdowns, $802,000 for other operating costs associated with the closing of plant facilities, and $665,000 for accelerated depreciation.

(2) The $1.7 million represents restructuring expenses of $990,000 for employee termination benefits, $914,000 for asset movement costs, $395,000 for lease termination and other exit costs, $334,000 for write-downs of buildings and equipment, and a credit of $890,000 for sales proceeds on equipment with no carrying value.

(3) The $3.6 million represents restructuring related charges of $1.9 million for accelerated depreciation, $1.2 million for inventory markdowns, and $455,000 other operating costs associated with the closing of plant facilities.

(4) The $3.0 million represents accelerated depreciation.

(5) The $6.6 million represents restructuring charges of $2.8 million for write-downs of buildings and equipment, $1.9 million for asset movement costs, $1.5 million for employee termination benefits, and $292,000 for lease termination costs.

THREE AND NINE MONTHS ENDED JANUARY 28, 2007 COMPARED WITH THE THREE AND NINE MONTHS ENDED JANUARY 29, 2006

For the third quarter of fiscal 2007, net sales were $55.7 million compared to $61.0 million for the third quarter of fiscal 2006. The company reported a net loss of $2.2 million or $0.19 per share diluted, in the third quarter of fiscal 2007, which included restructuring and related pre-tax charges of $4.1 million. Also, included in these results is a non-cash income tax charge of $452,000 or $0.04 per diluted share, related to the exercise of non-qualified stock options. The company reported a net loss of $2.2 million, or $0.19 per share diluted, in the third quarter of fiscal 2006, which included restructuring and related pre-tax charges of $1.7 million.

For the first nine months of fiscal 2007, net sales were $177.3 million compared to $190.4 million for the first nine months of fiscal 2006. The company reported a net loss of $1.3 million or $0.11 per share diluted, for the first nine months of fiscal 2007, which included restructuring and related pre-tax charges of $5.6 million. The company reported a net loss of $10.3 million, or $0.89 per share diluted, for the first nine months of fiscal 2006, which included restructuring and related pre-tax charges of $13.2 million.

RESTRUCTURING AND RELATED CHARGES

During the third quarter of fiscal 2007, total restructuring and related net charges incurred were $4.1 million, of which, $2.2 million related to inventory markdowns, $1.2 million related to employee termination benefits, $665,000 related to accelerated depreciation, $272,000 for write-downs of equipment, $181,000 for asset movement costs, $61,000 for lease termination costs, a net credit of $24,000 for other operating costs associated with the closing of plant facilities, and a credit of $455,000 for sales proceeds received on equipment with no carrying value. Of the total net charge, $2.8 million was recorded in cost of sales, $28,000 was recorded in selling, general, and administrative expenses, and $1.3 million was recorded in restructuring expense in the 2007 Consolidated Statement of Net Loss. These charges relate to the Upholstery Fabrics segment. During the third quarter of fiscal 2006, total restructuring and related net charges incurred were $1.7 million, of which, $838,000 related to inventory markdowns, $389,000 for other operating costs associated with the closing of plant facilities, $371,000 for asset movement costs, $133,000 for employee termination benefits, $108,000 for accelerated depreciation, $51,000 for lease termination costs, a credit of $77,000 for sales proceeds received on equipment with no carrying value, and a credit of $135,000 to reflect current estimates of sub-lease income. Of this total net charge, $1.3 million was recorded in cost of sales, and $343,000 was recorded in restructuring expense in the 2006 Consolidated Statement of Net Loss. These charges relate to the Upholstery Fabrics segment.

During the first nine months of fiscal 2007, total restructuring and related net charges incurred were $5.6 million, of which, $2.3 million related to inventory markdowns, $990,000 related to employee termination benefits, $914,000 related to asset movement costs, $802,000 represents operating costs associated with the closing of plant facilities, $665,000 for accelerated depreciation, $395,000 for lease termination and other exit costs, $334,000 for write-downs of buildings and equipment, and a credit of $890,000 for sales proceeds received on equipment with no carrying value associated with closed plant facilities. Of the total net charge, $3.8 million was recorded in cost of sales, $58,000 was recorded in selling, general, and administrative expenses, and $1.7 million was recorded in restructuring expense in the 2007 Consolidated Statement of Net Loss. These charges relate to the Upholstery Fabrics segment. During the first nine months of fiscal 2006, total restructuring and related net charges incurred were $13.2 million, of which, $4.9 million related to accelerated depreciation, $2.8 million related to write-downs of buildings and equipment, $1.9 million related to asset movement costs, $1.5 million related to employee termination benefits, $1.2 million related to inventory markdowns, $455,000 related to other operating costs associated with the closing of plant facilities, and $292,000 for lease termination costs. Of the total net charge, $3.6 million was recorded in cost of sales, $3.0 million was recorded in selling, general, and administrative expenses, and $6.6 million was recorded in restructuring expense in the 2006 Consolidated Statement of Net Loss. These charges primarily relate to the Upholstery Fabrics segment.

MATTRESS FABRICS SEGMENT

ASSET ACQUISITION

In January 2007, the company closed on an Asset Purchase Agreement (the "Agreement") for the purchase of certain assets from International Textile Group, Inc. ("ITG") related to the mattress fabrics product line of ITG's Burlington House division. The company purchased ITG's mattress fabrics finished goods inventory, a credit on future purchases of inventory manufactured by ITG during the transition period, along with certain proprietary rights (patterns, copyrights, artwork, and the like) and other records that relate to ITG's mattress fabrics product line. The company did not purchase any accounts receivable, property, plant, and equipment, and did not assume any liabilities other than certain purchase orders.

The consideration given for this transaction after adjustments to the closing date inventory as defined by the Agreement, was $8.1 million. Payment consisted of $2.5 million in cash financed by a term loan, the issuance of 798,582 shares of the company's common stock with a fair value of $5.1 million, and the company also incurred direct acquisition costs relating to legal, accounting, and other professional fees of $515,000. The total transaction cost allocation allocation is not final based on the ultimate settlement of certain direct acquisition costs. The final allocation may impact the ultimate valuation of the assets acquired. The total transaction cost was allocated as follows:

(DOLLARS IN THOUSANDS)	Fair Value
Inventories	$ 4,754
Other current assets (credit on future purchases of inventory)	2,210
Non-compete agreement	1,148
	$ 8,112

The company recorded the non-compete agreement at its fair value based on various valuation techniques, which is reflected in other assets in the accompanying consolidated balance sheet. The non-compete agreement will be amortized on a straight-line basis over the four year life of the agreement. Amortization expense during the next five fiscal years follows: FY 2007 - $72,000; FY 2008 - $287,000; FY 2009 - $287,000; FY 2010 - $287,000; and FY 2011 - $215,000.

The Agreement requires ITG to provide certain transition services to the company and will manufacture goods for the company for a limited period of time (expected to be approximately 120 days) to support the company's efforts to transition the former ITG mattress fabrics products into the company's operations. The company does not plan to hire any of ITG's employees after the transition is completed. ITG has also agreed that it will not compete with the company in the mattress fabrics business for a period of four years, except for mattress fabrics production in China for final consumption in China (meaning the mattress fabric and the mattress on which it is used is sold only in China).

In connection with the Agreement, the company issued 798,582 shares of common stock. As a result, the company entered into a Registration Rights and Shareholder Agreement ("the Registration Agreement"), which relates to the shares of the common stock issued by the company to ITG (the "Shares"). Under the terms of the Registration Agreement, ITG may demand that the company register the Shares with the Securities and Exchange Commission, which would allow the Shares to be sold to the public after the registration statement becomes effective. The Registration Agreement also contains provisions pursuant to which ITG will agree not to purchase additional company shares or take certain other actions to influence control of the company, and will agree to vote the shares in accordance with recommendations of the company's board of directors.

The acquisition of ITG's mattress fabrics product line enhances the company's competitive position in the mattress ticking industry. Management believes this transaction provides the opportunity to increase the company's annual sales by approximately $30 to $40 million, with only a modest investment in fixed assets. The company will be transitioning the ITG production to the company's facilities and suppliers over the next several months. The company estimates that one-time transition costs related to the acquisition will be approximately $750,000, of which approximately $650,000 will be incurred in the fourth quarter of fiscal 2007 and approximately $100,000 will be incurred in the first quarter of fiscal 2008. The company has the necessary capacity in place to absorb the additional business volume resulting from this transaction.

NET SALES -- Mattress fabric (known as mattress ticking) sales for the third quarter of fiscal 2007 increased 7.6% to $24.4 million compared to $22.7 million for the third quarter of fiscal 2006. These results include $1.0 million in incremental sales related to the company's acquisition of ITG's mattress fabrics product line. Mattress fabric sales accounted for approximately 44% of total net sales for the third quarter of fiscal 2007 compared to 37% for the third quarter of fiscal 2006. Mattress ticking yards sold during the third quarter of fiscal 2007 were 10.5 million compared to 9.6 million yards in the third quarter of fiscal 2006, an increase of 9%. The average selling price at the end of the third quarter of fiscal 2007 was $2.32 per yard and was essentially unchanged for the third quarter of fiscal 2007 compared to fiscal 2006. For the first nine months of fiscal 2007, net sales were $69.7 million compared to $69.6 million for the first nine months of fiscal 2006. Mattress ticking yards sold during the first nine months of fiscal 2007 were 30.2 million compared to 30.8 million for the first nine months of fiscal 2006, a decrease of 2%. For the first nine months of fiscal 2007, the average selling price for mattress fabrics was $2.31 per yard compared to $2.26 per yard for the first nine months of fiscal 2006, an increase of 2%. This increase is due to the shift in product mix to increased sales of substantially higher priced knitted ticking.

OPERATING INCOME -- For the third quarter of fiscal 2007, the mattress fabrics segment reported operating income of $2.5 million, or 10.3% of net sales, compared to $1.8 million, or 7.9% of net sales, for the third quarter of fiscal 2006. The company showed significant improvement in operating performance in mattress fabrics over the same period a year ago, with operating income up nearly 40% and operating margins over 10% for the second consecutive quarter. Operating margins improved due to productivity gains from the $10.0 million capital project implemented over the past 2 years. The company continues to see higher sales and gross margins in knitted ticking and expects this product line to represent a higher percentage of our mattress ticking business in the future. The company is experiencing a growing trend with our customers to use more knits on the top of the mattress and woven jacquards on the sides. For the first nine months of fiscal 2007, operating income was $6.8 million, or 9.8% of net sales, compared to $4.8 million, or 6.9% of net sales, for the first nine months of fiscal 2006. The trends (and the factors causing those trends) for the first nine months of fiscal 2007 compared with the first nine months of fiscal 2006 parallel those for the third quarter of fiscal 2007 compared with the third quarter of fiscal 2006.

SEGMENT ASSETS -- Segment assets consist of accounts receivable, inventory, and property, plant, and equipment. As of January 28, 2007, accounts receivable and inventory totaled $28.3 million compared to $21.2 million at April 30, 2006. This increase is primarily attributable to the purchase of finished goods inventories from ITG. Also as of January 28, 2007, property, plant and equipment totaled $22.6 million compared to $25.4 million at April 30, 2006. Included in property, plant, and equipment are assets located in the U.S. totaling $12.0 million and $12.9 million at January 28, 2007, and April 30, 2006, respectively.

UPHOLSTERY FABRICS SEGMENT

NET SALES -- Upholstery fabric sales for the third quarter of fiscal 2007 decreased 18.4% to $31.3 million compared with $38.4 million in the third quarter of fiscal 2006. Upholstery fabric yards sold during the third quarter of fiscal 2007 were 7.6 million compared to 9.2 million in the third quarter of fiscal 2006, a decline of 17%. The average selling price was $4.10 per yard for the third quarter of fiscal 2007, compared to $4.16 per yard in the third quarter of fiscal 2006, a decrease of 1%. Sales of upholstery fabrics reflect higher sales of non-U.S. produced fabrics, and continued very weak demand industry wide for U.S. produced fabrics, driven by consumer preference for leather and suede furniture and other imported fabrics, including an increasing amount of cut and sewn kits. While the company continues to see growth in sales of non-U.S. produced upholstery fabrics, the pace of growth has slowed down. Sales of non-U.S. produced fabrics were $17.4 million in the third quarter of fiscal 2007 compared with $14.7 million in the third quarter of fiscal 2006, an increase of 18%. Sales of U.S. produced fabrics decreased 41% to $14.0 million in the third quarter of fiscal 2007 compared to $23.6 million in the third quarter of fiscal 2006.

For the first nine months of fiscal 2007, net sales decreased 10.9% to $107.6 million compared to $120.8 million for the first nine months of fiscal 2006. Upholstery fabric yards sold during the first nine months of fiscal 2007 were 25.8 million compared to 28.5 million for the first nine months of fiscal 2006, a decline of 9%.The average selling price for the first nine months of fiscal 2007 was $4.17 per yard compared to $4.24 per yard for the first nine months of fiscal 2006, a decrease of 2%. Sales of non-U.S. produced fabrics were $61.5 million for the first nine months of fiscal 2007 compared with $38.9 million for the first nine months of fiscal 2006, an increase of 58% over the same period last year. Sales of U.S. produced fabrics decreased 44% to $46.1 million for the first nine months of fiscal 2007 compared with $81.9 million for the first nine months of fiscal 2006. The trends (and the factors causing those trends) for the first nine months of fiscal 2007 compared with the first nine months of fiscal 2006 parallel those for the third quarter of fiscal 2007 compared with the third quarter of fiscal 2006.

OPERATING INCOME (LOSS) - Operating loss for the third quarter of fiscal 2007 was $496,000 a significant improvement compared with an operating loss of $1.6 million for the third quarter of fiscal 2006. These results reflect higher gross profit on non-U.S. produced fabrics but continued low gross profit levels related to U.S. produced fabrics. Operating income for the first nine months of fiscal 2007 was $1.5 million compared with an operating loss of $2.1 million for the first nine months of fiscal 2006. The trends (and the factors causing those trends) for the first nine months of fiscal 2007 compared with the first nine months of fiscal 2006 parallel those for the third quarter of fiscal 2007 compared with the third quarter of fiscal 2006.

NON-U.S. PRODUCED SALES - Net sales of upholstery fabrics produced outside the company's U.S. manufacturing operations accounted for approximately 55% of total upholstery fabric sales in the third quarter of 2007, compared to 38% for the third quarter of fiscal 2006. Net sales of upholstery fabrics produced outside the company's U.S. manufacturing operations accounted for approximately 57% of total upholstery fabric sales for the first nine months of fiscal 2007, compared to 32% for the first nine months of fiscal 2006. The company has established an operation near Shanghai, China, designed to accommodate the growing customer demand for products sourced outside the U.S. The company is aggressively expanding its capabilities in China with a strong focus on product innovation, quality, and global logistics. During fiscal 2007, this operation has significantly increased its output of cut and sewn kits, started up its own velvet manufacturing, and built a 130,000 square foot fabric distribution center. The company now employs approximately 450 people in China and has five buildings approximating a total of 300,000 square feet.

U.S. PRODUCED SALES - Since the beginning of fiscal 2007, the company has made considerable progress in changing its product strategy, reducing manufacturing complexities, and improving its cost structure. However, the declining sales volume has continued to affect the profitability of the company's overall upholstery fabrics business. In December 2006, the company's board of directors approved a restructuring plan to further consolidate its U.S. upholstery fabrics manufacturing facilities and outsource its specialty yarn production. This process involves closing the company's weaving plant located in Graham, North Carolina, and closing its yarn plant located in Lincolnton, North Carolina, and transferring certain production from the Graham plant to the company's Anderson, South Carolina, and Shanghai, China, facilities, as well as a small portion to contract weavers. Once this restructuring initiative is complete, which is expected to be the end of fiscal 2007, the company will have one U.S. upholstery fabrics plant in Anderson, which will produce velvets and a limited amount decorative fabrics. This facility has a book value of fixed assets of approximately $2.2 million. In addition, the company intends to sell certain real estate and equipment associated with its plants in Graham and Lincolnton after production at those plants has ended. At that time, these assets will be classified as held for sale and are estimated to have a fair value of approximately $1 million. The company continues to consolidate its U.S. manufacturing operations and make greater use of lower-cost manufacturing alternatives, with the goal of reducing operating costs and improving domestic capacity utilization.

As a result of the continuing sharp declines in demand for U.S. produced fabrics, management will continue to evaluate its domestic strategy and production requirements. Management remains committed to take whatever additional steps are necessary to achieve profitable U.S. upholstery fabric operations, and the company could take additional restructuring actions. The company could experience additional markdowns of its inventory and write-downs of its property, plant, and equipment from any new restructuring initiatives.

SEGMENT ASSETS -- Segment assets consist of accounts receivable, inventory, and property, plant, and equipment. As of January 28, 2007, accounts receivable and inventory totaled $38.1 million compared to $44.6 million at April 30, 2006. As of January 28, 2007, assets held for sale totaled $1.2 million compared to $3.1 million at April 30, 2006. The company received sales proceeds of $2.4 million on assets held for sale during the nine month period ended January 28, 2007. The company expects these assets held for sale as of January 28, 2007, to be sold over the next twelve months. As of January 28, 2007, property, plant, and equipment totaled $18.1 million compared to $19.2 million at April 30, 2006. Included in property, plant, and equipment are assets located in the U.S.

totaling $10.6 million and $13.8 million at January 28, 2007, and April 30, 2006, respectively. Included in this U.S. property, plant, and equipment are corporate allocations totaling $3.9 million and $4.1 million at January 28, 2007, and April 30, 2006, respectively.

OTHER (INCOME) EXPENSE CATEGORIES

SELLING, GENERAL AND ADMINISTRATIVE EXPENSES - Selling, general, and administrative expenses were $6.4 million for the third quarter of fiscal 2007 compared with $6.1 million for the third quarter of fiscal 2006. Selling, general, and administrative expenses were $19.2 million for the first nine months of fiscal 2007 compared with $22.5 million for the first nine months of fiscal 2006. Included in the $22.5 million for the first nine months of fiscal 2006 was $3.0 million in accelerated depreciation associated with the company's design and distribution centers sold in June of 2005.

The company adopted SFAS No. 123R as of the beginning of the current fiscal year, which requires all share-based payments to be recognized as expense over the requisite service period based upon values as of the grant dates. Under the provisions of SFAS No. 123R, total stock-based compensation expense was $406,000 and $119,000 for the nine-month and three-month periods ended January 28, 2007. The company recorded $139,000 and $35,000 of stock-based compensation expense for stock options accounted for under the provisions of APB Opinion No.25 for the nine-month and three-month periods ended January 29, 2006.

INTEREST EXPENSE (INCOME) -- Interest expense for the third quarter of fiscal 2007 was $952,000 compared to $1.1 million for the third quarter of fiscal 2006. Interest expense for the first nine months of fiscal 2007 was $2.8 million compared to $3.0 million for the first nine months of fiscal 2006. The lower interest expense for fiscal 2007 primarily reflects lower outstanding balances on the company's unsecured senior term notes. Interest income for the third quarter of fiscal 2007 was $50,000 compared with $43,000 for the third quarter of fiscal 2006. Interest income for the first nine months of fiscal 2007 was $147,000 compared with $78,000 for the first nine months of fiscal 2006. The increase in interest income for fiscal 2007 reflects higher balances invested in money market funds.

OTHER (INCOME) EXPENSE - Other income for the third quarter of fiscal 2007 was $157,000 compared to other expense of $135,000 for the third quarter of fiscal 2006. Other income for the first nine months of fiscal 2007 was $98,000 compared to other expense of $481,000 for the first nine months of fiscal 2006. This change primarily reflects fluctuations in foreign currency exchange rates for subsidiaries domiciled in China and Canada.

INCOME TAXES -- The effective tax rate (taxes as a percentage of income (loss) before income taxes) for the third quarter of fiscal 2007 was an income tax benefit of 40.0% compared with 36.6% for the third quarter of fiscal 2006. The effective tax rate for the first nine months of fiscal 2007 was an income tax benefit of 54.7% compared with 36.4% for the first nine months of fiscal 2006. Changes in the effective income tax rate reflect losses from the company's U.S. operations due to its restructuring activities, lower income tax rates on income from foreign sources, and income tax expense of $452,000 or $0.04 per diluted share for the exercise of share options relating to the company's non-qualified stock option plan in the third quarter of fiscal 2007.

LIQUIDITY AND CAPITAL RESOURCES

LIQUIDITY -- The company's sources of liquidity include cash and cash equivalents, cash flow from operations, proceeds from the sale of buildings and equipment related to closed plant facilities, and amounts available under its revolving credit line. These sources have been adequate for day-to-day operations and capital expenditures. Cash and cash equivalents were $10.7 million and $12.9 million at January 28, 2007 and April 30, 2006, respectively. Cash flow provided by operating activities for the first nine months of fiscal 2007 was $4.4 million. Capital expenditures were $2.5 million, most of which related to the company's China operations. Payments on vendor-financed capital expenditures were $927,000 and payments on long-term debt were $3.5 million. Proceeds from the sale of buildings and equipment as part of the company's restructuring activities were $3.3 million, and proceeds from common stock issued in connection with stock option exercises were $194,000. The company paid the remaining $4.5 million due in March of 2007 on February 20, 2007.

WORKING CAPITAL -- Accounts receivable as of January 28, 2007, decreased 16.6% in comparison to January 29, 2006. Days sales outstanding totaled 36 days at January 28, 2007, compared with 39 days at January 29, 2006. Inventories at January 28, 2007, increased 1.5% from January 29, 2006. Inventory turns for the third quarter of fiscal 2007 were 5.3 versus 5.0 for the third quarter of fiscal 2006. Operating working capital (comprised of accounts receivable and inventories, less trade accounts payable) was $48.4 million at January 28, 2007, down from $49.9 million at January 29, 2006.

FINANCING ARRANGEMENTS

UNSECURED TERM NOTES

The company's unsecured term notes (the "Notes") have an outstanding balance of $39.4 million as of January 28, 2007 and are payable over an average remaining term of 2.5 years beginning February 2007 through March 2010. As of January 28, 2007, the principal payments that are required to be paid in periodic installments over the next four years are as follows: Year 1 - $4.5 million; Year 2 - $19.9 million; Year 3 - $7.5 million; and Year 4 - $7.5 million.

On December 6, 2006, the company entered into a Second Amendment to Note Purchase Agreements (the "Amendment"). Upon execution of this amendment, the company prepaid $3.0 million in principal amount and interest on the Notes, without prepayment penalty or "make whole" premium. The Amendment raised the interest rate from 7.76% to 8.80% on the remaining outstanding Notes and allows for an increase in the amount of other debt to be incurred by the company, including a provision that allows for debt of up to $5 million in the company's China subsidiary. The Amendment changed the financial covenants applicable to the company to provide additional flexibility to account for recent changes that the company has made or could make to its business and the accounting consequences of those changes. Beginning with the third quarter of fiscal 2007, these changes exclude from the financial covenants, all restructuring and related charges associated with the U.S. upholstery fabrics' operations, and any valuation allowance, if needed, against the company's net deferred tax assets from U.S. operations. The Amendment also provides for prepayments of the Notes (at the option of the noteholders and without prepayment penalty) to the extent that the company's cash balances exceed $8 million at the end of each fiscal quarter. The company paid the remaining $4.5 million due in March of 2007 on February 20, 2007, as part of this prepayment provision.

REAL ESTATE LOAN - I

The company has a real estate loan with an outstanding balance of $4.1 million as of January 28, 2007. This loan agreement is secured by a lien on the company's corporate headquarters office located in High Point, NC. This term loan bears interest at the one-month London Interbank Offered Rate plus an adjustable margin based on the company's debt/EBITDA ratio, as defined in the agreement, and is payable in varying monthly installments through September 2010, with a final payment of $3.3 million in October 2010.

REAL ESTATE LOAN - II

On January 22, 2007, the company entered into an agreement with a bank to provide for a term loan in the amount of $2.5 million in connection with the ITG asset purchase agreement. This term loan is secured by a lien on the company's corporate headquarters office located in High Point, NC and bears interest at the one-month London Interbank Offered Rate plus 3%. This agreement requires the company to pay interest monthly with the entire principal amount of $2.5 million due on June 30, 2010.

CANADIAN GOVERNMENT LOANS

In November 2005, the company entered into an agreement with the Canadian government to provide for a term loan in the amount of $680,000. The proceeds are to partially finance capital expenditures at the company's facility located in Quebec, Canada. This loan is non-interest bearing and is payable in 48 equal monthly installments commencing December 1, 2009. In addition to the term loan entered into in November 2005, the company had an existing non-interest bearing term loan with the Canadian government which was paid in May 2006.

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REVOLVING CREDIT AGREEMENT -UNITED STATES

On January 22, 2007, the company entered into a Tenth Amendment to this unsecured credit agreement dated August 23, 2002. This amendment reduced the line of credit available from $8.0 million to $6.5 million, including letters of credit up to $5.5 million and extended the term of the credit agreement from August 31, 2007 to December 31, 2007. The amendment also removed the liquidity provision that required the company to maintain collected deposit balances of at least $2.0 million. It also amended certain other financial covenants as defined in the agreement. Borrowings under the credit facility bear interest at the one-month London Interbank Offered Rate plus an adjustable margin based on the company's debt/EBITDA ratio, as defined in the agreement. As of January 28, 2007, there were $2.4 million in outstanding letters of credit (almost all of which related to workers compensation) and no borrowings outstanding under the agreement.

REVOLVING CREDIT AGREEMENT - CHINA

On February 1, 2007, the company's China subsidiary entered into an unsecured credit agreement with a bank to provide a line of credit available up to approximately $5.0 million, of which approximately $1.3 million includes letters of credit. The credit agreement expires on February 1, 2008, with an annual renewal option, and requires interest to be paid on a quarterly basis at a fixed annual rate of 5.8%. As of March 13, 2007, approximately $1.3 million was outstanding under the agreement.

OVERALL

The company's loan agreements require that the company maintain compliance with certain financial ratios. At January 28, 2007, the company was in compliance with these financial covenants.

As of January 28, 2007, the principal payment requirements of long-term debt during the next five years are: Year 1 - $4.7 million; Year 2 - $20.1 million; Year 3 - $7.8 million; Year 4 - $13.5 million; Year 5 - $169,000; and thereafter

- $480,000.

CAPITAL EXPENDITURES -- Capital spending for the first nine months of fiscal 2007 was $2.5 million, most of which related to the company's China operations. The company expects capital spending not to exceed $3.0 million in fiscal 2007. The company's capital budget for fiscal 2008 is $4.0 million, of which approximately $2.5 million and $1.5 million is for the mattress fabrics and upholstery fabrics segments, respectively. Depreciation for the first nine months of fiscal 2007 was $5.7 million, of which, $665,000 relates to accelerated depreciation. The company estimates depreciation for all of fiscal 2007 to be $8.5 million, which includes, $2.0 million for accelerated depreciation. The company estimates depreciation for all of fiscal 2008 to be approximately $6.0 million of which slightly more than half is attributable to the mattress fabric segment. The company expects that the availability of funds under the revolving credit line and cash flow from operations will be sufficient to fund its capital needs.

LIQUIDITY REQUIREMENTS -- As indicated earlier, the company's sources of liquidity include cash and cash equivalents, cash flow from operations, proceeds from the sale of buildings and equipment related to closed plant facilities and amounts available under its revolving credit line. The company believes its sources of liquidity continue to be adequate to meet its current operating needs. In addition, the company is taking further steps to improve its liquidity, including ongoing efforts to reduce inventories and operating expenses. However, the company's cash position could be adversely affected by factors beyond its control, such as weakening industry demand, delays in receipt of payment on accounts receivable and the availability of trade credit.

CRITICAL ACCOUNTING POLICIES AND RECENT ACCOUNTING DEVELOPMENTS

U.S. generally accepted accounting principles require the company to make estimates and assumptions that affect the reported amounts in the consolidated financial statements and accompanying notes. Some of these estimates require difficult, subjective and/or complex judgments about matters that are inherently uncertain, and as a result actual results could differ significantly from those estimates. Due to the estimation processes involved, management considers the following summarized accounting policies and their application to be critical to understanding the company's business operations, financial condition and results of operations.

ACCOUNTS RECEIVABLE - ALLOWANCE FOR DOUBTFUL ACCOUNTS. Substantially all of the company's accounts receivable are due from residential and commercial furniture and bedding manufacturers. Ownership of these manufacturers is increasingly concentrated and certain bedding manufacturers have a high degree of leverage. As of January 28, 2007, accounts receivable from furniture manufacturers totaled approximately $13.4 million, and from bedding manufacturers approximately $10.3 million. Additionally, as of January 28, 2007, the aggregate accounts receivable balance of the company's ten largest customers was $9.9 million, or 42% of trade accounts receivable.

The company continuously performs credit evaluations of its customers, considering numerous inputs including customers' financial position, past payment history, cash flows and management capability; historical loss experience; and economic conditions and prospects. Once evaluated, each customer is assigned a credit grade. Credit grades are adjusted as warranted. Significant management judgment and estimates must be used in connection with establishing the reserve for allowance for doubtful accounts. While management believes that adequate allowances for doubtful accounts have been provided in the consolidated financial statements, it is possible that the company could experience additional unexpected credit losses.

INVENTORY VALUATION. The company operates as a "make-to-order" and "make-to-stock" business. Although management closely monitors demand in each product area to decide which patterns and styles to hold in inventory, the increasing availability of low cost imports and the gradual shifts in consumer preferences expose the company to write-downs of inventory.

Management continually examines inventory to determine if there are indicators that the carrying value exceeds its net realizable value. Experience has shown that the most significant indicator of the need for inventory write-downs is the age of the inventory. As a result, the company provides inventory valuation write-downs based upon set percentages for inventory aging categories, generally using six, nine, twelve and fifteen month categories. While management believes that adequate write-downs for excess and obsolete inventory have been made in the consolidated financial statements, significant unanticipated changes in demand or changes in consumer tastes and preferences could result in additional excess and obsolete inventory in the future.

LONG-LIVED ASSETS. The company follows the provisions of SFAS No. 144, Accounting for the Impairment or Disposal of Long-Lived Assets. SFAS No. 144 establishes an impairment accounting model for long-lived assets to be held and used, disposed of by sale, or disposed of by abandonment or other means.

Management reviews long-lived assets, which consists of property, plant and equipment, for impairment whenever events or changes in circumstances indicate that the carrying value of the asset may not be recovered. During the first nine months of fiscal 2007, no events or changes in circumstances occurred that would require the company to test for impairment. Unforeseen events and changes in circumstances and market conditions could negatively affect the value of assets and result in an impairment charge.

The determination of future operating cash flows involves considerable estimation and judgment about future market conditions, future sales and profitability, and future asset utilization. Although the company believes it bases its impairment testing as required by SFAS No. 144 on reasonable estimates and assumptions, the use of different estimates and assumptions, or a decision to dispose of substantial portions of these assets, could result in materially different results.

GOODWILL. As of January 28, 2007, the company's remaining $4.1 million of goodwill relates to the mattress fabrics segment. The determination of fair value involves considerable estimation and judgment. In particular, determining the fair value of a business unit involves, among other things, developing forecasts of future cash flows and appropriate discount rates. During the first nine months of fiscal 2007, no events or changes in circumstances occurred that would require the company to test for impairment.

RESTRUCTURING CHARGES. In June 2002, the FASB issued SFAS No. 146, "Accounting for Costs Associated with Exit or Disposal Activities." This Statement addresses financial accounting and reporting for costs associated with exit or disposal activities and supersedes Emerging Issues Task Force (EITF) Issue No. 94-3, "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)." Under SFAS 146, a liability for a cost associated with an exit or disposal activity shall be recognized and measured initially at its fair value in the period in which the liability is incurred, except for certain employee termination benefits that qualify under SFAS No. 112, "Employers' Accounting for Postemployment Benefits."

The upholstery fabric industry continues to be under significant pressure from a variety of external forces, such as the current consumer preference for leather and suede furniture and the growing competition from imported fabrics and cut and sewn kits, primarily from China. In an effort to reduce operating expenses and scale U.S. productive capacity in line with demand, the company has undertaken restructuring initiatives during the past several years. These restructuring initiatives have resulted in restructuring charges related to the remaining lease costs of the closed facilities, the write-down of property, plant and equipment, workforce reduction and elimination of facilities.

As a result of the continuing sharp declines in demand for U.S. produced fabrics, management will continue to evaluate its domestic strategy and production requirements. Management remains committed to take whatever additional steps are necessary to achieve profitable U.S. upholstery fabric operations, and the company could take additional restructuring actions in the near future. The company could experience additional markdowns of its inventory and write-downs of its property, plant, and equipment from any new restructuring initiatives.

Severance and related charges are accrued at the date the restructuring was approved by the board of directors based on an estimate of amounts that will be paid to affected employees, in accordance with SFAS 112. Under SFAS 144, asset impairment charges related to the consolidation or closure of manufacturing facilities are based on an estimate of expected sales prices for the real estate and equipment. Other exit costs, which principally consist of charges for lease termination and losses from termination of existing contracts, equipment relocation costs and inventory markdowns that are related to the restructuring are accounted for in accordance with SFAS 146.

The company reassesses the individual accrual requirements at the end of each reporting period. If circumstances change, causing current estimates to differ from original estimates, adjustments are recorded in the period of change. Restructuring charges, and adjustments of those charges, are summarized in note 11 to the consolidated financial statements.

INCOME TAXES. The company is required to estimate its tax exposure and to assess temporary differences resulting from differing treatment of items for tax and accounting purposes. At April 30, 2006, the company had deferred tax assets of $31.4 million (all of which relate to U.S. operations) and U.S. deferred tax liabilities of $2.2 million (all of which reverse in the carryforward period), resulting in net U.S. deferred tax assets of $29.2 million. Total deferred tax liabilities at April 30, 2006 were $4.1 million, resulting in total net deferred tax assets of $27.3 million. As of January 28, 2007, the company's net deferred tax assets total $30.4 million, an increase of $3.1 million from the end of fiscal 2006, primarily reflecting the federal and state tax benefits recorded for the loss from U.S. operations during the first nine months of fiscal 2007. No valuation allowance has been recorded to reduce the company's deferred tax assets. Management has concluded that it is more likely than not that the company will be able to realize the benefit of the deferred tax assets.

In making the judgment about the realization of the deferred tax assets, management has considered both negative and positive evidence, and concluded that sufficient positive evidence exists to overcome the cumulative losses experienced in recent years. Specifically, management considered the following, among other factors: nature of the company's products; history of positive earnings in the mattress fabrics segment; capital projects in progress to further enhance the company's globally competitive cost structure in the mattress fabrics segment; recent significant restructuring actions in the domestic upholstery fabrics business to adjust the domestic cost structure and bring U.S. manufacturing capacity in line with demand; development of offshore manufacturing and sourcing programs to meet changing demands of upholstery fabric customers in the U.S; and the incremental sales volume from the purchase of certain assets from ITG related to the mattress fabric product line of ITG's Burlington House Division. Management's analysis of taxable income also included the following considerations: none of the company's net operating loss carryforwards has previously expired unused; the U.S. federal carryforward period is 20 years; and the company's current losses principally expire in 16-20 years, fiscal 2022 through 2026.

Considerable judgment is involved in this process as ultimate realization of benefits is dependent on the generation of income from future operations.

RECENTLY ISSUED ACCOUNTING STANDARDS

In June 2006, the Financial Accounting Standards Board ("FASB") issued Interpretation No.48, "Accounting for Uncertainty in Income Taxes" ("FIN No. 48") which clarifies the criteria for the recognition of tax benefits under SFAS No. 109, "Accounting for Income Taxes." This Interpretation prescribes a comprehensive model for financial statement recognition, measurement, presentation and disclosure of uncertain tax positions taken, or expected to be taken, in income tax returns. FIN No.48 is effective for fiscal years beginning after December 15, 2006 and requires that the cumulative effect of applying its provisions be disclosed as a one-time, non-cash charge or credit against the opening balance of retained earnings in the year of adoption. This Interpretation will be adopted by the company in the first quarter of fiscal 2008. The company is currently evaluating the potential impact of FIN No. 48 and any impact on its financial position cannot be readily determined at this time.

In September 2006, the FASB issued SFAS No. 157, "Fair Value Measurements," which provides enhanced guidance for using fair value to measure assets and liabilities. SFAS No. 157 establishes a common definition of fair value, provides a framework for measuring fair value under accounting principles generally accepted in the United States and expands disclosure requirements about fair value measurements. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 and is effective for the company in the first quarter of fiscal 2009. The company is currently evaluating the impact, if any, the adoption of SFAS No. 157 will have on its consolidated financial statements.

In February 2007, the FASB issued Statement No. 159, "The Fair Value Option for Financial Assets and Financial Liabilities." This statement, which is expected to expand fair value measurement, permits entities to choose to measure many financial instruments and certain other items at fair value. SFAS No. 159 is effective for fiscal years beginning after November 15, 2007 and is effective for the company in the first quarter of fiscal 2009. The company is currently evaluating the impact, if any, the adoption of SFAS No. 159 will have on its consolidated financial statements.

In September 2006, the SEC staff issued Staff Accounting Bulletin (SAB) No. 108, "Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements." SAB No. 108 was issued in order to eliminate the diversity of practice surrounding how public companies quantify financial statement misstatements. This SAB establishes a "dual approach" methodology that requires quantification of financial statement misstatements based on the effects of the misstatements on each of the company's financial statements (both the statement of operations and statement of financial position). The SEC has stated SAB No. 108 should be applied no later than the annual financial statements for the first fiscal year ending after

November 15, 2006. SAB No. 108 permits a company to elect either a retrospective or prospective application. Prospective application requires recording a cumulative effect adjustment in the period of adoption, as well as detailed disclosure of the nature and amount of each individual error being corrected through the cumulative adjustment and how and when it arose. The company is currently evaluating the impact, if any, the application of SAB No 108 will have on the consolidated financial statements.

INFLATION

The cost of certain company's raw materials, principally fibers from petroleum derivatives, and utility/energy costs, increased during the first nine months of fiscal 2007 as oil and energy prices increased and had an impact on the company's financial results. These increases, however, are often not directly related to general economic inflation, which has not been a material factor in the company's recent financial results. Any significant increase in the company's raw material costs, utility/energy costs and general economic inflation could have a material adverse impact on the company, because competitive conditions have limited the company's ability to pass significant operating cost increases on to its customers.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The company is exposed to market risk from changes in interest rates on debt and foreign currency exchange rates. The company's market risk sensitive instruments are not entered into for trading purposes. The company's exposure to interest rate risk consists of floating rate debt based on the London Interbank Offered Rate plus an adjustable margin under the company's revolving credit agreement and real estate term loans. As of January 28, 2007, there were $6.6 million in borrowings outstanding under the real estate term loans and no borrowings under the company's revolving credit agreement. In connection with the first real estate term loan, the company entered into a $2,170,000 notional principal interest rate swap agreement, which represents 50% of the principal amount on the first real estate loan, and effectively converts the floating rate LIBOR based payments to fixed payments at 4.99% plus the spread calculated under the first real estate term loan agreement. The company's unsecured term notes have a fixed interest rate of 8.80% and the Canadian government loan is non-interest bearing. Additionally, approximately 90% of the company's long-term debt is at a fixed rate or is non-interest bearing. Thus, any foreseeable change in interest rates would have a minimal material effect on the company's interest expense.

The company's exposure to fluctuations in foreign currency exchange rates are due to foreign subsidiaries domiciled in China and Canada. These subsidiaries use the United States dollar as their functional currency. The company generally does not use financial derivative instruments to hedge foreign currency exchange rate risks associated with its foreign subsidiaries. A 10% change in either exchange rate at January 28, 2007 would not have a significant impact on the company's results of operations or financial position.

ITEM 4. CONTROLS AND PROCEDURES

The company conducted a review and evaluation of its disclosure controls and procedures, under the supervision and with the participation of the company's principal executive officer and principal financial officer as of January 28, 2007, and the principal executive officer and principal financial officer have concluded that the company's disclosure controls and procedures are adequate and effective. In addition, no change in the company's internal control over financial reporting has occurred during, or subsequent to, the period covered by this report that has materially affected, or is reasonably likely to materially affect, the company's internal control over financial reporting.

PART II - OTHER INFORMATION

ITEM 1A. RISK FACTORS

Our business is subject to risks and uncertainties. In addition to the matters described in the "Cautionary Statement Concerning Forward-Looking Information," set forth below are some of the risks and uncertainties that could cause a material adverse change in our results of operations or financial condition.

RESTRUCTURING INITIATIVES CREATE SHORT-TERM COSTS THAT MAY NOT BE OFFSET BY INCREASED SAVINGS OR EFFICIENCIES.

Over the past seven years, we have undertaken significant restructuring activities, which have involved closing manufacturing plants, realigning manufacturing assets, reducing selling general and administrative (SG&A) expenses, and changing our upholstery product strategy. These actions have been intended to lower manufacturing costs and increase efficiency, but they involve significant costs, including the write-off or write-down of assets, severance costs for terminated employees, contract termination costs, equipment moving costs, and similar charges. These charges have caused a decrease in earnings over this time period. In addition, during the time that restructuring activities are underway, manufacturing inefficiencies are caused by moving equipment, realignment of assets, personnel changes, and by the consolidation process for certain functions. Unanticipated difficulties in restructuring activities or delays in accomplishing our goals could cause the costs of our restructuring initiatives to be greater than anticipated and the results achieved to be significantly lower, which would negatively impact our results of operations and financial condition.

OUR SALES HAVE BEEN DECLINING, AND WE HAVE REPORTED NET LOSSES IN NINE OF THE PAST ELEVEN FISCAL QUARTERS.

We may not be able to restore the upholstery fabrics segment to consistent profitability. In the upholstery fabrics segment, sales are down significantly, and they have been declining rapidly for U.S. produced fabrics. We have undertaken a number of significant restructuring actions in recent years to address our profitability, including (i) consolidating production assets and purchasing more efficient equipment in the mattress fabrics segment, (ii) closing a number of U.S. manufacturing facilities in the upholstery fabrics segment, (iii) establishing upholstery fabrics facilities in China to take advantage of a lower cost environment and greater product diversity, (iv) reducing SG&A expenses substantially, and (v) outsourcing certain production functions, in the U.S., including yarn production, some weaving, and finishing of decorative fabrics. Successful completion of our restructuring plans depends on a number of variables, including our ability to consolidate certain functions, manage manufacturing processes with lower direct involvement, managing a longer supply chain, and similar issues. There is no assurance that we will be able to manage our restructuring activities successfully to restore the company, especially the upholstery fabrics segment, to profitability.

INCREASED RELIANCE ON OFFSHORE OPERATIONS AND FOREIGN SOURCES OF PRODUCTS OR RAW MATERIALS INCREASES THE LIKELIHOOD OF DISRUPTIONS TO OUR SUPPLY CHAIN OR OUR ABILITY TO DELIVER PRODUCTS TO OUR CUSTOMERS ON A TIMELY BASIS.

During recent years, the company has established operations in China, and in addition we have been purchasing an increasing share of our products and raw materials from offshore sources, primarily in China. At the same time, our domestic manufacturing capacity for the upholstery fabrics segment has been greatly reduced. These changes have caused the company to place greater reliance on a much longer supply chain and on a larger number of suppliers that we do not control, which are inherently subject to greater risks of delay or disruption. In addition, operations and sourcing in foreign areas are subject to the risk of changing local governmental rules, taxes, changes in import rules or customs, potential political unrest, or other threats that could disrupt or increase the costs of operating in foreign areas or sourcing products overseas. Also, changes in relative values of currencies could increase our costs. Any of the risks associated with foreign operations and sources could cause unanticipated increases in operating costs or disruptions in business, which could negatively impact the company's ultimate financial results.

WE MAY HAVE DIFFICULTY MANAGING THE OUTSOURCING ARRANGEMENTS INCREASINGLY BEING USED BY THE COMPANY FOR PRODUCTS AND SERVICES.

The company is relying more on outside sources for various products and services, including raw material, greige (unfinished) fabrics, finished fabrics, and services such as weaving and finishing. Increased reliance on outsourcing lowers our capital investment and fixed costs, but it decreases the amount of control that we have over certain elements of our production capacity. Interruptions in our ability to obtain raw materials, other required products or services from our outside suppliers on a timely and cost effective basis, especially if alternative suppliers cannot be immediately obtained, could disrupt our production and damage our financial results.

FURTHER WRITE-OFFS OR WRITE-DOWNS OF UPHOLSTERY FABRICS SEGMENT ASSETS WOULD RESULT IN A DECREASE IN OUR EARNINGS.

The company has long-lived assets, consisting mainly of property, plant and equipment. Accounting rules require that these assets be tested for impairment of their valuation at least annually, as well as upon the occurrence of certain events. When assets are taken out of service, which has occurred recently on several occasions in connection with our restructuring activities, they must be tested for impairment, which can result in significant write-downs in the value of those assets. Restructuring activities and other tests for impairment have resulted and could in the future result in the write-down of a portion of our long-lived assets and a corresponding reduction in earnings and net worth. In fiscal 2006, the company experienced asset write-downs of approximately $6.0 million, all in the upholstery fabrics segment. The company has announced restructuring actions in the upholstery fabrics segment during fiscal 2007 that are expected to result in further net asset write downs of approximately $1.5 million during the fiscal year.

WRITE-OFFS OF ASSETS OR WEAK FINANCIAL PERFORMANCE COULD CAUSE US TO BREACH FINANCIAL COVENANTS IN OUR DEBT AGREEMENTS.

At the end of the third quarter of fiscal 2007, the company had $46.7 million of long-term debt, of which approximately $39.4 million was owed on unsecured senior notes issued in 1998. Under the debt agreements that govern our long-term debt, we are required to maintain compliance with certain financial covenants, including minimum tangible net worth, debt to tangible capitalization, debt to capital, minimum earnings before interest, taxes, depreciation and amortization, and interest and lease payment coverage. The company has been able to maintain compliance with these financial covenants. However, in some cases the "cushion" between the required financial covenants and our actual financial performance has been shrinking. For example, our tangible net worth has decreased significantly in recent years due to asset write offs and operating losses. Additional write-offs of assets or continued operating losses could lead to a breach of financial covenants and a default under our loan agreements. A breach of our debt covenants would give the lenders under our long-term debt agreements the right to declare all of the debt immediately due and payable and to terminate our right to obtain further borrowings. If such an event occurred, it is unlikely that we would be able to repay all of our debt from current resources, and there is no assurance that we would be able to find alternative sources of financing.

CHANGES IN THE PRICE, AVAILABILITY AND QUALITY OF RAW MATERIALS COULD INCREASE OUR COSTS OR CAUSE PRODUCTION DELAYS AND SALES INTERRUPTIONS, WHICH WOULD RESULT IN DECREASED EARNINGS.

The company depends upon outside suppliers for most of its raw material needs, and increasingly we rely upon outside suppliers for component materials such as yarn and unfinished fabrics, as well as for certain services such as finishing and weaving. Fluctuations in the price, availability and quality of these goods and services could have a negative effect on our production costs and ability to meet the demands of our customers, which would affect our ability to generate sales and earnings. In many cases, we are not able to pass through increased costs of raw materials or increased production costs to our customers through price increases. In particular, many of our basic raw materials are petrochemical products or are produced from such products. For this reason, our material costs are especially sensitive to changes in prices for petrochemicals and the underlying price of oil. Increases in prices for oil, petrochemical products or other raw materials and services provided by outside suppliers could significantly increase our costs and negatively affect earnings.

INCREASES IN ENERGY COSTS WOULD INCREASE OUR OPERATING COSTS AND COULD ADVERSELY AFFECT EARNINGS.

Higher prices for electricity, natural gas and fuel increase our production and shipping costs. A significant shortage, increased prices, or interruptions in the availability of these energy sources would increase the costs of producing and delivering products to our customers, and would be likely to adversely affect our earnings. In many cases, we are not able to pass along the full extent of increases in our production costs to customers through price increases. During fiscal 2006, energy prices increased significantly, in part due to supply disruptions caused by hurricanes. Although some price increases were implemented to offset the effect of these increased costs, we were not able to fully recoup these costs, and operating margins were negatively affected. Further increases in energy costs could have a negative effect on our earnings.

BUSINESS DIFFICULTIES OR FAILURES OF LARGE CUSTOMERS COULD RESULT IN A DECREASE IN OUR SALES AND EARNINGS.

The company currently has several customers that account for a substantial portion of its sales. In the mattress fabric segment, several large bedding manufacturers have large market shares and comprise a significant portion of our mattress fabric sales. In the upholstery fabrics segment, La-Z-Boy Inc. accounted for 13% of consolidated net sales during fiscal 2006, and several other large furniture manufacturers comprised a significant portion of sales. A business failure or other significant financial difficulty by one or more of our major customers could cause a significant loss in sales, an adverse effect on our earnings, and collection of our trade accounts receivable.

IF WE ARE UNABLE TO MANAGE OUR CASH EFFECTIVELY, WE WILL NOT HAVE FUNDS AVAILABLE TO REPAY DEBT AND TO MAINTAIN THE FLEXIBILITY NECESSARY FOR SUCCESSFUL OPERATION OF OUR BUSINESS.

Our ability to meet our cash obligations depends on our operating cash flow, access to trade credit, and our ability to borrow under our debt agreements. In addition to the cash needs of operating our business, we have substantial debt repayments that are due over the next several years on our unsecured senior notes. During fiscal 2006, in spite of incurring losses, we were able to generate substantial cash flow through reductions of working capital. Our ability to generate cash flow going forward will rely to a heavier degree on our ability to generate profits from our business, and we have not been able to generate earnings on a consistent basis in recent quarters. If we are not able to generate cash during upcoming fiscal periods, we may not be able to provide the funds needed to operate and maintain our business or to make payments on our debt as they become due.

FURTHER LOSS OF MARKET SHARE DUE TO COMPETITION WOULD RESULT IN FURTHER DECLINES IN SALES AND COULD RESULT IN ADDITIONAL LOSSES OR DECREASES IN EARNINGS.

Our business is highly competitive, and in particular the upholstery fabric industry is fragmented and is experiencing an increase in the number of competitors. As a result, we face significant competition from a large number of competitors, both foreign and domestic. We compete with many other manufacturers of fabric, as well as converters who source fabrics from various producers and market them to manufacturers of furniture and bedding. In many cases, these fabrics are sourced from foreign suppliers who have a lower cost structure than the company. The highly competitive nature of our business means we are constantly subject to the risk of losing market share. Our sales have decreased significantly over the past six years due in part to the increased number of competitors in the marketplace, especially foreign sources of fabric. As a result of increased competition, there have been deflationary pressures on the prices for many of our products, which makes it more difficult to pass along increased operating costs such as raw materials, energy or labor in the form of price increases and puts downward pressure on our profit margins. Also, the large number of competitors and wide range of product offerings in our business can make it more difficult to differentiate our products through design, styling, finish and other techniques.

IF WE FAIL TO ANTICIPATE AND RESPOND TO CHANGES IN CONSUMER TASTES AND FASHION TRENDS, OUR SALES AND EARNINGS MAY DECLINE.

Demand for various types of upholstery fabrics and mattress coverings change over time due to fashion trends and changing consumer tastes for furniture and bedding. Our success in marketing our fabrics depends upon our ability to anticipate and respond in a timely manner to fashion trends in home furnishings. If we fail to identify and respond to these changes, our sales of these products may decline. In addition, incorrect projections about the demand for certain products could cause the accumulation of excess raw material or finished goods inventory, which could lead to inventory write-downs and further decreases in earnings.

AN ECONOMIC DOWNTURN COULD RESULT IN A DECREASE IN OUR SALES AND EARNINGS.

Overall demand for our products depends upon consumer demand for furniture and bedding, which is subject to variations in the general economy. Because purchases of furniture or bedding are discretionary purchases for most individuals and businesses, demand for these products is sometimes more easily influenced by economic trends than demand for other products. Economic downturns can affect consumer spending habits and demand for home furnishings, which reduces the demand for our products and therefore could cause a decrease in our sales and earnings.

WE ARE SUBJECT TO LITIGATION AND ENVIRONMENTAL REGULATIONS THAT COULD ADVERSELY IMPACT OUR SALES AND EARNINGS.

We are, and in the future may be, a party to legal proceedings and claims, including environmental matters, product liability and employment disputes, some of which claim significant damages. We face the continual business risk of exposure to claims that our business operations have caused personal injury or property damage. We maintain insurance against product liability claims and in some cases have indemnification agreements with regard to environmental claims, but there can be no assurance that these arrangements will continue to be available on acceptable terms or that such arrangements will be adequate for liabilities actually incurred. Given the inherent uncertainty of litigation, there can be no assurance that claims against the company will not have a material adverse impact on our earnings or financial condition. We are also subject to various laws and regulations in our business, including those relating to environmental protection and the discharge of materials into the environment. We could incur substantial costs as a result of noncompliance with or liability for cleanup or other costs or damages under environmental laws or other regulations.

THE COMPANY MUST COMPLY WITH A NUMBER OF GOVERNMENTAL REGULATIONS APPLICABLE TO OUR BUSINESS, AND CHANGES IN THOSE REGULATIONS COULD ADVERSELY AFFECT OUR BUSINESS.

Our products and raw materials are and will continue to be subject to regulation in the United States by various federal, state and local regulatory authorities. In addition, other governments and agencies in other jurisdictions regulate the manufacture, sale and distribution of our products and raw materials. For example, standards for flame resistance of fabrics have been recently introduced in the state of California, and additional standards are scheduled to apply on a nationwide basis beginning July 1, 2007. Also, rules and restrictions regarding the importation of fabrics and other materials, including custom duties, quotas and other regulations, are continually changing. Environmental laws, labor laws, tax regulations and other regulations also continually affect our business. All of these rules and regulations can and do change from time to time, which can increase our costs or require us to make changes in our manufacturing processes, product mix, sources of products and raw materials, or distribution. Changes in the rules and regulations applicable to our business may negatively impact our sales and earnings.

THE COMPANY'S MARKET CAPITALIZATION AND SHAREHOLDERS' EQUITY HAVE FALLEN BELOW THE LEVEL REQUIRED FOR CONTINUED LISTING ON THE NEW YORK STOCK EXCHANGE.

Our common stock is currently traded on the New York Stock Exchange (NYSE). Under the NYSE's current listing standards, we are required to have market capitalization or shareholders' equity of more than $75 million to maintain compliance with continued listing standards. During the past year, the company was below the NYSE required minimum for both of these listing standards. As a result, we have been listed as "below compliance" with NYSE listing standards. In accordance with NYSE rules, we submitted a plan for returning to compliance with the listing standards, and this plan has been accepted by the NYSE. As of the end of the third quarter of fiscal 2007, our shareholders' equity was approximately $78.9 million. If the company is not able to return to and maintain compliance with NYSE listing standards, our stock will be delisted from trading on the NYSE, resulting in the need to find another market on which our stock can be listed or causing our stock to cease to be traded on an active market, which could result in a reduction in the liquidity for our stock and a reduction in demand for our stock.

DIFFICULTIES IN INTEGRATING OUR RECENT ACQUISITION COULD NEGATIVELY AFFECT THE SALES AND PROFITS OF OUR MATTRESS FABRICS BUSINESS.

On January 22, 2007, we completed an asset purchase from International Textile Group, Inc. (ITG) in our mattress fabrics business. In order to realize the benefits of that transaction, we must successfully integrate the products and fabric patterns acquired into our business. We are making substantial changes to the mattress fabric product line formerly offered by ITG. We expect the asset acquisition to increase the sales and profits of our mattress fabrics business, but our success will depend upon our ability to retain a substantial portion of the sales to mattress manufacturers formerly served by ITG. If we are not able to retain this business and to maintain service levels, our sales and profits will be adversely affected. In addition, integration activities will place substantial demands on our management, operational resources, and service capabilities. If we experience customer dissatisfaction or operational problems as a result of integrating the additional business acquired, our mattress fabrics business could be negatively affected.

ITEM 5. OTHER INFORMATION.

In a letter dated October 27, 2006, the New York Stock Exchange (NYSE) notified the company that the NYSE has accepted the company's plan for continued listing on the NYSE. As a result of the acceptance, the company's common stock will continue to be listed on the NYSE pending quarterly reviews by the NYSE's Listing and Compliance Committee to ensure progress against the plan. The company previously announced that the NYSE notified the company that it was considered "below criteria" because the company's average total market capitalization was less than $75 million over a consecutive 30 trading-day period and its shareholders' equity was less than $75 million. As of January 28, 2007, the end of the company's most recent fiscal quarter, the company's shareholders' equity was approximately $78.9 million.

ITEM 6. EXHIBITS

THE FOLLOWING EXHIBITS ARE FILED AS PART OF THIS REPORT.

3(i) Articles of Incorporation of the company, as amended, were filed as Exhibit 3(i) to the company's Form 10-Q for the quarter ended July 28, 2002, filed September 11, 2002, and are incorporated herein by reference.

3(ii) Restated and Amended Bylaws of the company, as amended June 12, 2001, were filed as Exhibit 3(ii) to the company's Form 10-Q for the quarter ended July 29, 2001, filed September 12, 2001, and are incorporated herein by reference.

10.1 Second Amendment to Note Purchase Agreement by and between Culp, Inc. and the holders of its Senior Notes dated December 6, 2006, filed as Exhibit 99(c) to the Company's Form 8-K dated December 7, 2006, and incorporated herein by reference.

10.2 Written Summary of Culp Home Fashions Division Management Incentive Plan, filed as Exhibit 10(a) to the Company's Form 8-K dated December 13, 2006, and incorporated herein by reference.

10.3 Asset Purchase Agreement between Culp, Inc. and International Textile Group, Inc. dated as of January 11, 2007, filed Exhibit 10.1 to the Company's Form 8-K dated January 26, 2007, and incorporated herein by reference.

10.4	Registration Rights and Shareholder Agreement between Culp, Inc. and International Textile Group, Inc. dated as of January 22, 2007, filed Exhibit 10.1 to the Company's Form 8-K dated January 26, 2007, and incorporated herein by reference.
10.5	Promissory Note to Wachovia Bank, National Association dated January 22, 2007, filed as Exhibit 10.2 to the Company's Form 8-K dated January 26, 2007, and incorporated herein by reference.
10.6	Tenth Amendment to Amended and Restated Credit Agreement dated January 22, 2007, filed as Exhibit 10.3 to the Company's Form 8-K dated January 26, 2007, and incorporated herein by reference.
31.1	Certification of Chief Executive Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Section 302 of Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer Pursuant to Section 906 of Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer Pursuant to Section 906 of Sarbanes-Oxley Act of 2002.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CULP, INC.
(REGISTRANT)

Date: March 14, 2007 By: /S/ FRANKLIN N. SAXON

Franklin N. Saxon
President
(Authorized to sign on behalf of the registrant and also signing as principal financial officer)

By: /S/ KENNETH R. BOWLING

Kenneth R. Bowling
Vice President-Finance, Treasurer
(Authorized to sign on behalf of the registrant and also signing as principal accounting officer)

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EXHIBIT INDEX

EXHIBIT NUMBER	EXHIBIT
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