

CULP INC
Form 10-Q
December 06, 2013

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 October 27, 2013
Commission File No. 1-12597

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

NORTH CAROLINA
(State or other jurisdiction of
incorporation or other organization)

56-1001967
(I.R.S. Employer Identification No.)

1823 Eastchester Drive
High Point, North Carolina
(Address of principal executive
offices)

27265-1402
(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 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to the filing requirements for at least the past 90 days. x
YES NO o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period after the registrant was required to submit and post such files). x
YES NO o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See definitions of "accelerated filer, large accelerated filer, and smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one);

Large accelerated filer o Accelerated filer x Non-accelerated filer o

Smaller Reporting Company

o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). o
YES NO x

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common shares outstanding at October 27, 2013: 12,250,030
Par Value: \$0.05 per share

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For the period ended October 27, 2013

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Item 1: Financial Statements

CULP, INC.

CONSOLIDATED STATEMENTS OF NET INCOME

FOR THE THREE AND SIX MONTHS ENDED OCTOBER 27, 2013 AND OCTOBER 28, 2012

UNAUDITED

(Amounts in Thousands, Except for Per Share Data)

	THREE MONTHS ENDED	
	October 27, 2013	October 28, 2012
Net sales	\$ 70,589	65,560
Cost of sales	58,354	53,683
Gross profit	12,235	11,877
Selling, general and administrative expenses	7,200	7,209
Income from operations	5,035	4,668
Interest expense	99	156
Interest income	(102)	(96)
Other expense	224	76
Income before income taxes	4,814	4,532
Income taxes	1,718	(3,736)
Net income	\$ 3,096	8,268
Net income per share, basic	\$ 0.25	0.68
Net income per share, diluted	0.25	0.67
Average shares outstanding, basic	12,183	12,191
Average shares outstanding, diluted	12,389	12,348

SIX MONTHS ENDED

	October 27, 2013	October 28, 2012
Net sales	\$ 140,730	134,744
Cost of sales	115,422	109,746
Gross profit	25,308	24,998
Selling, general and administrative expenses	14,299	14,850

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Income from operations	11,009	10,148
Interest expense	239	346
Interest income	(195)	(222)
Other expense	616	121
Income before income taxes	10,349	9,903
Income taxes	4,023	(1,889)
Net income	\$ 6,326	11,792
Net income per share, basic	\$ 0.52	0.95
Net income per share, diluted	0.51	0.94
Average shares outstanding, basic	12,165	12,371
Average shares outstanding, diluted	12,391	12,541

See accompanying notes to consolidated financial statements.

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CULP, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

FOR THE THREE AND SIX MONTHS ENDED OCTOBER 27, 2013 AND OCTOBER 28, 2012

(UNAUDITED)

THREE MONTHS ENDED

	October 27, 2013	October 28, 2012
Net income	\$ 3,096	\$ 8,268
Other comprehensive income		
Unrealized gains on short-term investments	22	11
Total other comprehensive income	22	11
Comprehensive income	\$ 3,118	\$ 8,279

SIX MONTHS ENDED

	October 27, 2013	October 28, 2012
Net income	\$ 6,326	\$ 11,792
Other comprehensive (loss) income		
Unrealized (losses) gains on short-term investments	(113)	44
Total other comprehensive (loss) income	(113)	44
Comprehensive income	\$ 6,213	\$ 11,836

See accompanying notes to consolidated financial statements.

CULP, INC.
CONSOLIDATED BALANCE SHEETS
OCTOBER 27, 2013, OCTOBER 28, 2012 AND APRIL 28, 2013
UNAUDITED
(Amounts in Thousands)

	October 27, 2013	October 28 2012	* April 28, 2013
Current assets:			
Cash and cash equivalents	\$ 24,267	23,464	23,530
Short-term investments	6,220	5,241	5,286
Accounts receivable, net	24,937	20,678	23,392
Inventories	44,882	38,261	38,418
Deferred income taxes	7,745	4,470	7,709
Income taxes receivable	-	-	318
Other current assets	2,550	1,640	2,093
Total current assets	110,601	93,754	100,746
Property, plant and equipment, net	30,559	30,621	30,594
Goodwill	11,462	11,462	11,462
Deferred income taxes	661	4,738	753
Other assets	2,959	1,868	1,151
Total assets	\$ 156,242	142,443	144,706
Current liabilities:			
Current maturities of long-term debt	\$ 2,200	2,401	2,200
Line of credit	-	875	561
Accounts payable-trade	28,543	23,219	22,357
Accounts payable - capital expenditures	66	104	225
Accrued expenses	11,672	10,611	11,829
Income taxes payable - current	304	385	285
Total current liabilities	42,785	37,595	37,457
Income taxes payable - long-term	4,141	4,188	4,191
Deferred income taxes	5,016	856	3,075
Line of credit	585	-	-
Long-term debt, less current maturities	2,200	4,416	4,400
Total liabilities	54,727	47,055	49,123
Commitments and Contingencies (Note 16)			
Shareholders' equity	101,515	95,388	95,583

Total liabilities and shareholders' equity	\$ 156,242	142,443	144,706
Shares outstanding	12,250	12,209	12,225

* 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 SIX MONTHS ENDED OCTOBER 27, 2013 AND OCTOBER 28, 2012
UNAUDITED
(Amounts in Thousands)

	SIX MONTHS ENDED	
	October 27, 2013	October 28, 2012
Cash flows from operating activities:		
Net income	\$ 6,326	11,792
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	2,636	2,539
Amortization of other assets	81	119
Stock-based compensation	376	197
Excess tax benefit related to stock-based compensation	(143)	(60)
Deferred income taxes	2,140	(3,325)
Gain on sale of equipment	(74)	-
Foreign currency exchange losses (gains)	203	(66)
Changes in assets and liabilities, net of effects of acquisition of assets:		
Accounts receivable	(1,419)	4,353
Inventories	(6,331)	(1,882)
Other current assets	(437)	373
Other assets	(47)	(80)
Accounts payable - trade	5,923	(7,397)
Accrued expenses	(158)	1,310
Accrued restructuring	-	(40)
Income taxes	367	(183)
Net cash provided by operating activities	9,443	7,650
Cash flows from investing activities:		
Capital expenditures	(1,900)	(1,946)
Net cash paid for acquisition of assets	(2,640)	-
Proceeds from the sale of equipment	113	-
Payments on life insurance policies	(30)	-
Purchase of short-term investments	(1,047)	(54)
Proceeds from the sale of short-term investments	-	795
Net cash used in investing activities	(5,504)	(1,205)
Cash flows from financing activities:		
Proceeds from lines of credit	-	1,000
Payments on lines of credit	-	(1,000)
Payments on long-term debt	(2,200)	(2,300)
Proceeds from common stock issued	194	64

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Common stock repurchased	-	(5,022)
Dividends paid	(979)	(747)
Debt issuance costs	(62)	-
Excess tax benefit related to stock-based compensation	143	60
Net cash used in financing activities	(2,904)	(7,945)
Effect of exchange rate changes on cash and cash equivalents	(298)	(59)
Increase (decrease) in cash and cash equivalents	737	(1,559)
Cash and cash equivalents at beginning of period	23,530	25,023
Cash and cash equivalents at end of period	\$ 24,267	23,464

See accompanying notes to consolidated financial statements.

CULP, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
UNAUDITED
(Dollars in thousands, except share data)

	Common Stock		Capital Contributed	Accumulated	Accumulated Other Comprehensive Income	Total Shareholders' Equity
	Shares	Amount	in Excess of Par Value	Earnings	(Loss)	
Balance, April 29, 2012	12,702,806	\$ 635	46,056	42,293	16	\$ 89,000
Net income	-	-	-	18,317	-	18,317
Stock-based compensation	-	-	562	-	-	562
Unrealized gain on short-term investments	-	-	-	-	38	38
Excess tax benefit related to stock based compensation	-	-	76	-	-	76
Common stock repurchased	(502,595)	(25)	(4,997)	-	-	(5,022)
Fully vested common stock award	1,658	-	-	-	-	-
Common stock issued in connection with stock option plans	23,025	1	204	-	-	205
Dividends paid	-	-	-	(7,593)	-	(7,593)
Balance, April 28, 2013 *	12,224,894	611	41,901	53,017	54	95,583
Net income	-	-	-	6,326	-	6,326
Stock-based compensation	-	-	376	-	-	376
Unrealized loss on short-term investments	-	-	-	-	(113)	(113)
Excess tax benefit related to stock based compensation	-	-	143	-	-	143
Common stock issued in connection with stock option plans	23,125 3,000	1 -	193 -	- -	- -	194 -

Fully vested common stock award						
Common stock surrendered for withholding taxes payable	(989)	-	(15)	-	-	(15)
Dividends paid	-		-	(979)	-	(979)
Balance, October 27, 2013	12,250,030	\$ 612	42,598	58,364	(59)	\$ 101,515

* Derived from audited financial statements.

See accompanying notes to consolidated financial
statements.

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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 note 3 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 12, 2013 for the fiscal year ended April 28, 2013.

The company’s six months ended October 27, 2013 and October 28, 2012, represent 26 week periods, respectively.

2. Significant Accounting Policies

As of October 27, 2013, there were no changes in the nature of our significant accounting policies or the application of those policies from those reported in our annual report on Form 10-K for the year then ended April 28, 2013.

Recently Adopted Accounting Pronouncements

None

Recently Issued Accounting Pronouncements

Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists

In July 2013, the Financial Accounting Standards Board (“FASB”) issued an accounting standards update which requires an unrecognized tax benefit to be presented as a reduction to a deferred tax asset for a net operating loss carryforward, a similar tax loss or a tax credit carryforward that the entity intends to use and is available for settlement at the reporting date. This update will be effective for us in the fourth quarter of fiscal 2014 and will not have an impact on our financial position, results of operations, or cash flows.

3. Business Combination – Mattress Fabric Segment

On May 8, 2013, we entered into an asset purchase and consulting agreement with Bodet & Horst GMBH & Co. KG and certain affiliates (“Bodet & Horst”) that provides for, among other things, the purchase of equipment and certain other assets from Bodet & Horst and the restructuring of existing consulting and non-compete agreements pursuant to an earlier asset purchase and consulting agreement with Bodet & Horst dated August 11, 2008. This agreement was accounted for as a business combination in accordance with ASC Topic 805, Business Combinations. We agreed with Bodet & Horst to replace the prior non-compete agreement that prevented us from selling certain mattress fabrics and products to a leading manufacturer, which now allows us to make such sales. In addition, the prior consulting and non-compete agreement, under which Bodet & Horst agreed not to sell most mattress fabrics in North America, was replaced, expanded, and extended pursuant to the new asset purchase and consulting agreement.

Culp, Inc.
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 (Unaudited)

The purchase price for the equipment and the other certain assets noted below was \$2.6 million in cash.

Direct acquisition costs related to this business combination totaled \$83,000.

The following table presents the allocation of the acquisition cost to the assets acquired based on their fair values:

(dollars in thousands)	Fair Value
Equipment	\$ 890
Non-compete agreement (Notes 7 and 10)	882
Customer relationships (Notes 7 and 10)	868
	\$ 2,640

The company recorded its non-compete at its fair value based on a discounted cash flow valuation model. The company recorded its customer relationships at its fair value based on a multi-period excess earnings valuation model. This non-compete agreement will be amortized on a straight line basis over the fifteen year life of the agreement. The customer relationships will be amortized on a straight line basis over their useful life of seventeen years. The equipment will be amortized on a straight line basis over their useful life of seven years.

The following unaudited pro forma consolidated results of operations for the three and six month periods ending October 27, 2013 and October 28, 2012 have been prepared as if the acquisition of Bodet & Horst had occurred on April 30, 2012:

(dollars in thousands)	Three months ended	
	October 27, 2013	October 28, 2012
Net Sales	\$ 70,589	\$ 68,027
Income operations	5,035	4,659
Net income	3,096	8,192
Net income per share, basic	0.25	0.67
Net income per share, diluted	0.25	0.66

Culp, Inc.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(dollars in thousands)	Six months ended October 27, 2013	October 28, 2012
Net Sales	\$ 140,730	\$ 139,678
Income from operations	11,009	10,129
Net income	6,326	11,675
Net income per share, basic	0.52	0.94
Net income per share, diluted	0.51	0.93

The unaudited pro forma information is presented for informational purposes only and is not necessarily indicative of the results of operations that actually would have been achieved had the acquisition been consummated as of that time, nor is it intended to be a projection of future results.

4. Stock-Based Compensation

Incentive Stock Option Awards

We did not grant any incentive stock option awards through the second quarter of fiscal 2014.

At October 27, 2013, options to purchase 153,950 shares of common stock were outstanding, had a weighted average exercise price of \$6.70 per share, and a weighted average contractual term of 4.1 years. At October 27, 2013, the aggregate intrinsic value for options outstanding was \$2.0 million.

At October 27, 2013, outstanding options to purchase 145,950 shares of common stock were exercisable, had a weighted average exercise price of \$6.96 per share, and a weighted average contractual term of 4.1 years. At October 27, 2013, the aggregate intrinsic value for options exercisable was \$1.9 million.

The aggregate intrinsic value for options exercised for the six months ending October 27, 2013 and October 28, 2012, was \$224,000 and \$18,000, respectively.

The remaining unrecognized compensation cost related to incentive stock option awards at October 27, 2013, was \$2,000 which is expected to be recognized over a weighted average period of 0.2 years.

We recorded \$8,000 and \$44,000 of compensation expense on incentive stock option grants within selling, general, and administrative expense for the six months ended October 27, 2013, and October 28, 2012, respectively.

Common Stock Awards

On October 1, 2013, we granted a total of 3,000 shares of common stock to our outside directors. These shares of common stock vested immediately and were measured at \$18.84 per share, which represents the closing price of the company's common stock at the date of grant.

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Culp, Inc.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

On October 8, 2012, we granted a total of 1,658 shares of common stock to certain outside directors. These shares of common stock vested immediately and were measured at \$12.13 per share, which represents the closing price of the company's common stock at the date of grant.

We recorded \$57,000 and \$20,000 of compensation expense within selling, general, and administrative expense for these common stock awards for the six month periods ending October 27, 2013, an October 28, 2012, respectively.

Time Vested Restricted Stock Awards

We did not grant any time vested restricted stock awards through the second quarter of fiscal 2014.

We recorded \$38,000 and \$65,000 of compensation expense within selling, general, and administrative expense for time vested restricted stock awards for the six month periods ending October 27, 2013, and October 28, 2012, respectively.

At October 27, 2013, there were 61,667 shares of time vested restricted stock outstanding and unvested. Of the 61,667 shares outstanding and unvested, 35,000 shares (granted on January 7, 2009) will vest on May 1, 2014. The remaining 26,667 shares (granted on July 1, 2009) will vest on July 1, 2014. At October 27, 2013, the weighted average fair value of these outstanding and unvested shares was \$4.19 per share.

During the six month period ended October 27, 2013, 61,667 shares of time vested restricted stock vested and had a weighted average fair value of \$249,000 or \$4.04 per share. During the six month period ended October 28, 2012, 61,665 shares of time vested restricted stock vested and had a weighted average fair value of \$232,000 or \$3.76 per share.

At October 27, 2013, the remaining unrecognized compensation cost related to the unvested restricted stock awards was \$30,000, which is expected to be recognized over a weighted average vesting period of 0.6 years.

Performance Based Restricted Stock Units

Fiscal 2014 Grant

On June 25, 2013, certain key members of management were granted performance based restricted common stock units which could earn up to 72,380 shares of common stock if certain performance targets are met as defined in the related restricted stock unit agreements. These awards were valued based on the fair market value on the date of grant. The fair value of these awards was \$17.12, which represents the closing price of our common stock on the date of grant. The vesting of these awards is over the requisite service period of three years.

Fiscal 2013 Grant

On July 11, 2012, certain key members of management were granted performance based restricted common stock units which could earn up to 120,000 shares of common stock if certain performance targets are met as defined in the related restricted stock unit agreements. These awards were valued based on the fair market value on the date of grant. The fair value of these awards was \$10.21, which represents the closing price of our common stock on the date of grant. The vesting of these awards is over the requisite service period of three years.

Culp, Inc.
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
 (Unaudited)

Overall

The company recorded compensation expense of \$273,000 and \$68,000 within selling, general, and administrative expense for performance based restricted stock units for the six month periods ending October 27, 2013 and October 28, 2012, respectively. Compensation cost is recorded based on an assessment each reporting period of the probability that certain performance goals will be met during the vesting period. If performance goals are not probable of occurrence, no compensation cost will be recognized and any recognized compensation cost would be reversed.

As of October 27, 2013, the remaining unrecognized compensation cost related to the performance based restricted stock units was \$1.2 million, which is expected to be recognized over a weighted average vesting period of 2.1 years.

5. Accounts Receivable

A summary of accounts receivable follows:

(dollars in thousands)	October 27, 2013	October 28, 2012	April 28, 2013
Customers	\$ 26,022	\$ 21,790	\$ 24,715
Allowance for doubtful accounts	(513)	(559)	(780)
Reserve for returns and allowances and discounts	(572)	(553)	(543)
	\$ 24,937	\$ 20,678	\$ 23,392

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

(dollars in thousands)	Six months ended	
	October 27, 2013	October 28, 2012
Beginning balance	\$ (780)	\$ (567)
Provision for bad debts	211	(27)
Net write-offs, net of recoveries	56	35
Ending balance	\$ (513)	\$ (559)

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

(dollars in thousands)	Six months ended	
	October 27, 2013	October 28, 2012
Beginning balance	\$ (543)	\$ (478)
Provision for returns, allowances and discounts	(1,129)	(1,551)
Credits issued	1,100	1,476
Ending balance	\$ (572)	\$ (553)

6. Inventories

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

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Culp, Inc.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

A summary of inventories follows:

(dollars in thousands)	October 27, 2013	October 28, 2012	April 28, 2013
Raw materials	\$ 5,592	\$ 5,884	\$ 5,311
Work-in-process	2,383	2,789	2,539
Finished goods	36,907		