

ALLIED HOLDINGS INC  
Form 10-Q  
November 14, 2003

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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 September 30, 2003

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES  
EXCHANGE ACT OF 1934 - For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 0-22276

**ALLIED HOLDINGS, INC.**

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(Exact name of registrant as specified in its charter)

**GEORGIA**

**58-0360550**

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(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification Number)

**Suite 200, 160 Clairemont Avenue, Decatur, Georgia 30030**

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(Address of principal executive offices)

**(404) 373-4285**

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(Registrant's telephone number, including area code)

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(Former name, former address and former fiscal year, if changed since last report)

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 such filing requirements for the past 90 days.  Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act of 1934).  
 Yes  No

Outstanding common stock, no par value at October 31, 2003

8,741,830

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**Item 1 - FINANCIAL STATEMENTS****ALLIED HOLDINGS, INC. AND SUBSIDIARIES****CONSOLIDATED BALANCE SHEETS**  
**(In Thousands)**

	<b>September 30, 2003</b>	<b>December 31, 2002</b>
	<b>(unaudited)</b>	
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 83,349	\$ 10,253
Short-term investments		60,732
Receivables, net of allowance for doubtful accounts of \$3,389 and \$5,587 respectively	58,078	58,512
Inventories	4,874	5,071
Deferred tax assets	24,034	39,826
Prepayments and other current assets	12,672	28,685
	<u>183,007</u>	<u>203,079</u>
Total current assets	183,007	203,079
<b>PROPERTY AND EQUIPMENT, NET</b>	<u>158,539</u>	<u>176,663</u>
<b>GOODWILL, NET</b>	88,998	85,241
<b>OTHER</b>	33,805	20,525
	<u>464,349</u>	<u>485,508</u>
Total assets	\$ 464,349	\$ 485,508
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
<b>CURRENT LIABILITIES:</b>		
Current maturities of long-term debt	\$ 17,854	\$ 10,785
Trade accounts payable	27,817	36,585
Accrued liabilities	93,421	92,881
	<u>139,092</u>	<u>140,251</u>
Total current liabilities	139,092	140,251
<b>LONG-TERM DEBT, less current maturities</b>	<u>236,376</u>	<u>237,690</u>
<b>POSTRETIREMENT BENEFITS OTHER THAN PENSIONS</b>	6,530	7,467
<b>DEFERRED INCOME TAXES</b>	11,364	27,746
<b>OTHER LONG-TERM LIABILITIES</b>	59,653	62,040
<b>STOCKHOLDERS EQUITY:</b>		
Preferred stock, no par value; 5,000 shares authorized, none outstanding		
Common stock, no par value; 20,000 shares authorized, 8,722 and 8,421 shares outstanding at September 30, 2003 and December 31, 2002,		

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respectively		
Additional paid-in capital	47,373	46,801
Treasury stock at cost, 139 shares at September 30, 2003 and December 31, 2002	(707)	(707)
Accumulated deficit	(30,687)	(26,420)
Accumulated other comprehensive loss, net of tax	(4,645)	(9,360)
	<u>          </u>	<u>          </u>
Total stockholders' equity	11,334	10,314
	<u>          </u>	<u>          </u>
Total liabilities and stockholders' equity	\$464,349	\$485,508
	<u>          </u>	<u>          </u>

The accompanying notes are an integral part of these consolidated balance sheets.

**Table of Contents****ALLIED HOLDINGS, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF OPERATIONS****(In Thousands, Except Per Share Data)****(Unaudited)**

	<b>For the Three Months Ended September 30,</b>		<b>For the Nine Months Ended September 30,</b>	
	<b>2003</b>	<b>2002</b>	<b>2003</b>	<b>2002</b>
<b>REVENUES</b>	\$ 197,089	\$ 212,985	\$ 640,759	\$ 665,228
<b>OPERATING EXPENSES:</b>				
Salaries, wages and fringe benefits	107,369	117,804	348,446	363,853
Operating supplies and expenses	29,960	33,257	103,108	100,068
Purchased transportation	24,082	25,331	74,632	72,438
Insurance and claims	8,260	10,844	29,094	34,344
Operating taxes and licenses	6,992	7,638	22,989	24,731
Depreciation and amortization	11,011	13,142	34,688	40,087
Rents	1,579	1,685	4,819	4,895
Communications and utilities	1,745	1,425	5,213	5,290
Other operating expenses	2,791	2,859	8,175	7,607
Loss (gain) on disposal of operating assets, net	153	367	612	(347)
Total operating expenses	193,942	214,352	631,776	652,966
Operating income (loss)	3,147	(1,367)	8,983	12,262
<b>OTHER INCOME (EXPENSE):</b>				
Interest expense	(7,366)	(7,611)	(22,120)	(23,343)
Investment income (loss)	(398)	203	2,935	1,090
Gain on early extinguishment of debt				2,750
Foreign exchange gain (loss), net	(62)	124	2,386	157
Other, net	1,976	(57)	1,976	(264)
	(5,850)	(7,341)	(14,823)	(19,610)
<b>LOSS BEFORE INCOME TAXES AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE</b>	(2,703)	(8,708)	(5,840)	(7,348)
<b>INCOME TAX BENEFIT</b>	728	2,226	1,573	1,819
<b>LOSS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE</b>	(1,975)	(6,482)	(4,267)	(5,529)
<b>CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET OF TAX</b>				(4,092)
<b>NET LOSS</b>	(\$ 1,975)	(\$ 6,482)	(\$ 4,267)	(\$ 9,621)
<b>BASIC AND DILUTED LOSS PER COMMON SHARE: LOSS BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE</b>	(\$ 0.23)	(\$ 0.78)	(\$ 0.50)	(\$ 0.67)
				(\$ 0.49)

<b>CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET OF TAX</b>				
<b>NET LOSS</b>	(\$ 0.23)	(\$ 0.78)	(\$ 0.50)	(\$ 1.16)
<b>BASIC AND DILUTED WEIGHTED AVERAGE COMMON SHARES OUTSTANDING</b>	8,507	8,324	8,459	8,282

The accompanying notes are an integral part of these consolidated financial statements.



**Table of Contents****ALLIED HOLDINGS, INC. AND SUBSIDIARIES****CONSOLIDATED STATEMENTS OF CASH FLOWS****(In Thousands)****(Unaudited)**

	<b>For the Nine Months Ended September 30,</b>	
	<b>2003</b>	<b>2002</b>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net loss	(\$ 4,267)	(\$ 9,621)
Reconciliation of net loss to net cash provided by operating activities:		
Gain on early extinguishment of debt		(2,750)
Interest expense paid in kind	1,065	746
Amortization of deferred financing costs	3,007	3,013
Depreciation and amortization	34,688	40,087
Loss (gain) on disposal of assets and other, net	612	(83)
Foreign exchange gain, net	(2,386)	(157)
Cumulative effect of change in accounting principle		4,092
Deferred income taxes	(3,402)	(2,569)
Compensation expense related to stock options and grants	290	(210)
Amortization of Teamsters Union contract costs	1,000	1,800
Change in operating assets and liabilities:		
Receivables, net of allowance for doubtful accounts	1,840	12,276
Inventories	336	55
Prepayments and other current assets	16,359	1,556
Short-term investments	60,732	2,367
Trade accounts payable	(9,676)	(4,057)
Accrued liabilities and other	(18,596)	8,533
Net change in operating assets and liabilities	50,995	20,730
Net cash provided by operating activities	81,602	55,078
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(11,547)	(13,313)
Proceeds from sale of property and equipment	287	3,005
Proceeds from sale of equity investment in joint venture		2,700
Decrease in the cash surrender value of life insurance	2	1,341
Net cash used in investing activities	(11,258)	(6,267)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Additions to (repayments of) revolving credit facilities, net	(20,280)	(62,384)
Additions to long-term debt	99,875	82,750
Repayment of long-term debt	(74,905)	(46,360)
Payment of deferred financing costs	(3,031)	(9,262)
Proceeds from issuance of common stock	282	262
Repurchase of common stock		
Other, net	65	549
Net cash provided by (used in) financing activities	2,006	(34,445)

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<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>	746	16
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	73,096	14,382
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	10,253	10,543
	<u>          </u>	<u>          </u>
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<b>\$ 83,349</b>	<b>\$ 24,925</b>
	<u>          </u>	<u>          </u>

The accompanying notes are an integral part of these consolidated financial statements.

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**ALLIED HOLDINGS, INC. AND SUBSIDIARIES**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(UNAUDITED)**

**September 30, 2003 and 2002**

**(1) Basis of Presentation**

The unaudited consolidated financial statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. The statements contained herein reflect all adjustments, all of which are of a normal, recurring nature, which are, in the opinion of management, necessary to present fairly the financial condition, results of operations and cash flows for the periods presented. Operating results for the three and nine month periods ended September 30, 2003 are not necessarily indicative of the results that may be expected for the year ended December 31, 2003. The interim financial statements should be read in conjunction with the financial statements and notes thereto of Allied Holdings, Inc. and Subsidiaries (the Company) included in the Company's 2002 Annual Report on Form 10-K.

Certain amounts in the prior year financial statements have been reclassified to conform to the current year presentation.

**(2) Use of Estimates**

The preparation of the consolidated financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amount of assets and liabilities and revenues and expenses during the period to disclose contingent assets and liabilities at the date of the consolidated financial statements. Significant items subject to such estimates and assumptions include the carrying amount of intangibles; property, plant and equipment; valuation allowances for receivables, inventories and deferred income tax assets; self-insurance reserves; and assets and obligations related to employee benefits. Actual results could differ from those estimates.

**(3) Recent Accounting Pronouncements**

In June 2001, FASB issued SFAS No. 143, *Accounting for Asset Retirement Obligations*. SFAS No. 143 requires the Company to record the fair value of an asset retirement obligation as a liability in the period in which it incurs a legal obligation associated with the retirement of tangible long-lived assets that result from the acquisition, construction, development, and/or normal use of the assets. The Company also records a corresponding asset that is depreciated over the life of the asset. Subsequent to the initial measurement of the asset retirement obligation, the obligation will be adjusted at the end of each period to reflect the passage of time and changes in the estimated future cash flows underlying the obligation. The Company adopted the provisions of SFAS No. 143 effective January 1, 2003. The Statement did not have a material impact on the financial position or results of operations of the Company as of the date of adoption.

In July 2002, the FASB issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*. The Statement addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies 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)*. This Statement requires recognition of a liability for a cost associated with an exit or disposal activity when the liability is incurred, as opposed to when the entity commits to an exit plan under EITF No. 94-3. The Company adopted the provisions of SFAS No. 146 effective January 1, 2003. The Statement did not have a material impact on the financial position or results of operations of the Company as of the date of adoption.

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In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness to Others, an interpretation of FASB Statements No. 5, 57 and 107 and a rescission of FASB Interpretation No. 34*. This Interpretation elaborates on the disclosures to be made by a guarantor in its interim and annual financial statements about its obligations under guarantees issued. The Interpretation also clarifies that a guarantor is required to recognize, at inception of a guarantee, a liability for the fair value of the obligation undertaken. The initial recognition and measurement provisions of the Interpretation are applicable to guarantees issued or modified after December 31, 2002. The Company adopted the recognition and measurement provisions of the Interpretation effective January 1, 2003 for guarantees issued or modified after December 31, 2002. The adoption of this Interpretation did not have a material impact on the financial position or results of operations of the Company as of the date of adoption. See note 11, Guarantees and Indemnifications.

In December 2002, the FASB issued SFAS No. 148, *Accounting for Stock-Based Compensation - Transition and Disclosure, an amendment of FASB Statement No. 123*. This Statement amends FASB Statement No. 123, *Accounting for Stock-Based Compensation*, to provide alternative methods of transition for a voluntary change to the fair value method of accounting for stock-based employee compensation. In addition, this Statement amends the disclosure requirements of Statement No. 123 to require prominent disclosures in both annual and interim financial statements. Certain of the disclosure modifications are required for fiscal years and interim periods ending after December 15, 2002 and are included in the notes to these consolidated financial statements.

In January 2003, the FASB issued FASB Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51*. This Interpretation addresses the consolidation of business enterprises (variable interest entities) to which the usual condition of consolidation does not apply. This interpretation focuses on financial interests that indicate control. It concludes that in the absence of clear control through voting interests, a company's exposure (variable interest) to the economic risks and potential rewards from the variable interest entity's assets and activities are the best evidence of control. Variable interests are rights and obligations that convey economic gains or losses from changes in the values of the variable interest entity's assets and liabilities. Variable interests may arise from financial instruments, service contracts, nonvoting ownership interests and other arrangements. If an enterprise holds a majority of the variable interests of an entity, it would be considered the primary beneficiary. The primary beneficiary would be required to include assets, liabilities and the results of operations of the variable interest entity in its financial statements. This interpretation applies immediately to variable interest entities that are created after or for which control is obtained after January 31, 2003. For variable interest entities created prior to February 1, 2003, the provisions would be applied effective July 1, 2003. Since the release of this interpretation, the FASB has issued numerous FASB Staff positions ( FSP ) regarding it, three of which remain in proposed form. On October 9, 2003, the FASB released FSP 46-6, which deferred the effective date for the consolidation guidance of this interpretation from July 1, 2003 to December 31, 2003, for variable interest entities existing prior to February 1, 2003. This Interpretation is not expected to have a material impact on the financial position or results of operations of the Company.

In April 2003, the FASB issued SFAS 149, *Amendment of Statement 133 on Derivative Instruments and Hedging Activities*. This Statement clarifies under which circumstances a contract with an initial net investment meets the characteristics of a derivative and clarifies when a derivative contains a financing component that warrants special reporting in the statement of cash flows. SFAS 149 amends certain other existing pronouncements. SFAS 149 is generally effective for contracts entered into or modified after June 30, 2003 and should be applied prospectively. The adoption of SFAS 149 is not expected to have a material impact on the financial position, results of operations or cash flows of the Company.

In May 2003, the Financial Accounting Standards Board (FASB) issued SFAS No. 150, *Accounting for Certain Instruments with Characteristics of Both Liabilities and Equity*. This Statement requires that certain financial instruments embodying an obligation to transfer assets or to issue equity securities be classified as liabilities. It is effective for financial instruments entered into or modified after May 31, 2003, and pre-existing instruments as of July 1, 2003. On October 29, 2003, the FASB voted to indefinitely defer the effective date of SFAS 150 for mandatorily redeemable instruments as they relate to minority interests in consolidated finite-lived entities through the issuance of FSP 150-3. The adoption of SFAS 150, as modified by FSP 150-3, did not have a material impact on the financial position or results of operations of the Company.

**Table of Contents****(4) Prepayments and Other Current Assets**

Prepayments and other current assets consist of the following at September 30, 2003 and December 31, 2002 (in thousands):

	September 30, 2003	December 31, 2002
Tires on tractors and trailers	\$ 7,179	\$ 7,082
Prepaid insurance	975	1,773
Other	4,518	19,830
	<u>12,672</u>	<u>28,685</u>

**(5) Property and Equipment**

Property and equipment consists of the following at September 30, 2003 and December 31, 2002 (in thousands):

	September 30, 2003	December 31, 2002
Tractors and trailers	\$ 436,581	\$ 421,615
Buildings and facilities (including leasehold improvements)	46,224	44,925
Land	12,287	11,958
Furniture, fixtures, and equipment	42,714	41,819
Service cars and equipment	3,547	3,111
	<u>541,353</u>	<u>523,428</u>
Less accumulated depreciation and amortization	<u>(382,814)</u>	<u>(346,765)</u>
	<u>\$ 158,539</u>	<u>\$ 176,663</u>

Depreciation expense amounted to \$10,966,000 and \$12,945,000 for the quarters ended September 30, 2003 and 2002, respectively and \$34,553,000 and \$39,924,000 for the nine months ended September 30, 2003 and 2002, respectively.

**(6) Goodwill**

In accordance with SFAS No. 142, *Goodwill and Other Intangible Assets*, the Company reviews goodwill annually for impairment, or on an interim basis if an event occurs or circumstances change that could potentially reduce the fair value of goodwill below its carrying value. The Company performs its annual analysis during the fourth calendar quarter of each year. No indicators of impairment were identified during the first nine months of 2003.

The Company's reporting units are the Allied Automotive Group and the Axis Group. The following table sets forth the carrying value of goodwill by reporting unit as of September 30, 2003 and December 31, 2002 (in thousands):

	Allied Automotive Group	Axis Group	Total
Balance as of December 31, 2002	\$ 73,043	\$ 12,198	\$ 85,241
	3,740	17	3,757

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Increase in carrying amount due to a  
change in currency rates

	—	—	—
Balance as of September 30, 2003	\$ 76,783	\$ 12,215	\$ 88,998
	—	—	—

**Table of Contents****(7) Impairment of Long-Lived Assets**

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, long-lived assets, such as property, plant, and equipment, and purchased intangibles subject to amortization, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized for the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the balance sheet and reported at the lower of the carrying amount or fair value less costs to sell, and would no longer be depreciated. The assets and liabilities of a disposed group classified as held for sale would be presented separately in the appropriate asset and liability sections of the balance sheet.

During 2002, the Company performed an analysis of certain fleet equipment that was idled. The assets were evaluated in order to determine if they were candidates for the fleet remanufacturing and engine replacement program. Approximately 1,000 tractors or trailers were not considered viable candidates for the program and a decision was made that they would not be placed back into operations. As a result, depreciation was accelerated to the reduced useful life resulting in an additional charge of \$2.1 million to depreciation expense in the fourth quarter of 2002. During the second quarter of 2003, the Company began disposal of these assets and anticipates substantial completion by the end of 2003.

**(8) Accrued Liabilities**

Accrued liabilities consists of the following at September 30, 2003 and December 31, 2002 (in thousands):

	September 30, 2003	December 31, 2002
Wages and benefits	\$38,464	\$41,903
Claims and insurance reserves	35,680	35,487
Other	19,277	15,491
	<u>\$93,421</u>	<u>\$92,881</u>

**(9) Long-Term Debt**

Long-term debt consisted of the following at September 30, 2003 and December 31, 2002 (in thousands):

	September 30, 2003	December 31, 2002
Revolving credit facility	\$ 4,354	\$ 24,635
Term Loan	99,876	0
Term Loan A	0	7,474
Term Loan B	0	25,684
Term Loan C	0	11,432
Term Loan D	0	29,250
Senior notes	150,000	150,000
	<u>254,230</u>	<u>248,475</u>
Less current maturities of long-term debt	(17,854)	(10,785)
	<u>\$236,376</u>	<u>\$237,690</u>





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On September 30, 1997, the Company issued \$150.0 million of 8 5/8% senior notes (the Notes ) through a private placement. Subsequently, the Notes were registered with the Securities and Exchange Commission. The net proceeds from the Notes were used to fund the acquisition of Ryder Automotive Carrier Services, Inc. and RC Management Corp., pay related fees and expenses, and reduce outstanding indebtedness. The Notes mature on October 1, 2007.

Borrowings under the Notes are general unsecured obligations of the Company. The Company's obligations under the Notes are guaranteed by substantially all of the subsidiaries of the Company (the Guarantor Subsidiaries ). Haul Insurance Ltd., Arrendadora de Equipo Para el Transporte de Automoviles, S. de R.L. de C.V. and Axis Logistica, S. de R.L. de C.V. do not guarantee the Company's obligations under the Notes (the Nonguarantor Subsidiaries ). See Note 17. There are no restrictions on the ability of Guarantors to make distributions to the Company.

The Notes set forth a number of negative covenants which are binding on the Company. The covenants limit the Company's ability to, among other things, purchase or redeem stock, make dividend or other distributions, make investments, and incur or repay debt (with the exception of payment of interest or principal at stated maturity).

On February 25, 2002, the Company entered into a new credit facility which includes certain term loans (the Term Loans ) and a revolving credit facility. Proceeds from the Term Loans were used in February 2002 to repurchase \$40 million of senior subordinated notes for \$37.25 million. In conjunction with the extinguishment of these senior subordinated notes, the Company recognized a pre-tax gain of \$2.75 million during the first quarter of 2002.

The Company amended the facility in September 2003 (the Credit Facility and amendments thereto are collectively referred to as the Credit Facility ). The Credit Facility as amended in September 2003 provides the Company with a \$90.0 million revolving credit facility (the Revolver ) and a \$100 million term loan (the New Term Loan ). At its inception, the Credit Facility consisted of a \$120 million revolving credit facility and four Term Loans that totaled \$82.75 million. As part of the amendment, the maturity date of the Credit Facility was extended to September 2007.

The interest rate for the Revolver is based upon the prime rate plus 1.5%, or LIBOR plus 4.5%, at management's discretion, with a minimum interest rate of 6.5%. The Credit Facility as amended provides that the New Term Loan bear interest between 8.5% and 11.5% to be determined solely on the Company's leverage as defined in the agreement. Prior to the amendment, the interest rate on the Term Loans was based solely on a spread over the prime rate. Annual commitment fees are due on the undrawn portion of the commitment.

At September 30, 2003, \$4.4 million was outstanding under the Revolver, and approximately \$24.3 million was committed under letters of credit. The Company had approximately \$58.2 million available under the Revolver as of September 30, 2003.

Borrowings under the Company's Credit Facility are secured by first priority security interest on assets of the Company and certain of its subsidiaries, including a pledge of stock of certain subsidiaries. If the Company were unable to repay any borrowing under its Credit Facility when due, the lenders thereunder would have the right to proceed against the collateral granted to them to secure the debt. Any default under the Company's debt instruments, particularly any default that resulted in acceleration of indebtedness or foreclosure on collateral, would have a material adverse effect on the Company.

The Credit Facility agreement sets forth a number of affirmative, negative, and financial covenants binding on the Company. The negative covenants limit the ability of the Company to, among other things, incur debt, incur liens, make investments, sell assets, or declare or pay any dividends on its capital stock. The financial covenants require the Company to maintain a minimum consolidated earnings before interest, taxes, depreciation and amortization, and gains and losses on disposal of operating assets amount and also include a maximum leverage ratio. The Company was in compliance with the various covenants set forth in the Credit Facility at September 30, 2003.

There can be no assurance that the Company will be able to comply with these covenants or its other debt covenants or that if it fails to do so, it will be able to obtain amendments to or waivers of such covenants. Failure of the Company to

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comply with covenants contained in its debt instruments, if not waived, or to adequately service debt obligations, could result in a default under the Credit Facility. Any default under the Company's debt instruments, particularly any default that results in an acceleration of indebtedness or foreclosure on collateral could have a material adverse effect on the Company.

**(10) Commitments and Contingencies**

The Company is involved in various litigation and environmental matters relating to employment practices, damages, and other matters arising from operations in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position or results of operations.

Since its last quarterly filing, Allied has settled all outstanding litigation with Ryder System, Inc., which litigation was previously disclosed in company filings. The litigation arose in connection with the acquisition by the Company of Ryder Automotive Carrier Services, Inc. and RC Management Corp. from Ryder System, Inc. in September 1997, and consisted of three actions. In *Ryder System, Inc. v. Allied Holdings, Inc., AH Acquisition Corp. and Allied Automotive Group* (the "Ryder Action"), Ryder alleged that the Company failed to substitute itself for Ryder under an insurance policy covering third-party claims and with various state agencies that regulate matters such as self-insured workers compensation. Ryder also alleged that the Company was obligated to take certain steps to transfer from Ryder to itself the ownership and administrative responsibility for two pension plans. The other two actions, *Gateway Development & Manufacturing, Inc. v. Commercial Carriers, Inc., et al.* and *Commercial Carriers, Inc. v. Gateway Development & Manufacturing, Inc., et al.* (collectively the "Gateway/CCI Actions"), both centered around the contention that the Company breached legal duties with respect to a failed business transaction involving Gateway Development, Ryder Truck Rental, Inc., and Ryder System.

Under terms of the settlement agreement, Ryder System has paid the Company approximately \$1.4 million, and Ryder's insurance carrier has paid the Company approximately \$1.6 million. The payment from Ryder represents the settlement of various claims and disputes that have arisen since the 1997 acquisition. The payment from Ryder's insurance carrier represents a reimbursement for amounts paid by the Company in excess of the self-insured retention for workers' compensation and automobile liability claims assumed in the acquisition of Ryder's Automotive Carrier Group. The Company and Ryder System have agreed to dismiss all litigation each party had brought against the other as part of the settlement, which has resulted in the complete dismissal of the Ryder Action. Except with respect to expenses already incurred, Ryder has agreed to indemnify Allied for all costs, including legal fees and any potential judgment against Allied, arising out of the Gateway/CCI Actions. Therefore, although the Gateway/CCI Actions remain pending, the settlement provides Allied with indemnification from Ryder System as to exposure to future legal fees or any potential judgment against the Company.

As part of the settlement agreement, the Company has issued a letter of credit for \$3.5 million in favor of Ryder System and has agreed to increase the letter of credit by \$1 million each quarter starting in the fourth quarter of 2003 through the third quarter of 2005. The letter of credit may only be drawn by Ryder System if the Company fails to pay workers' compensation and liability claims assumed by the Company in the Ryder Automotive Carrier Group acquisition. The Company has provided the letter of credit in favor of Ryder System because Ryder has issued a letter of credit to its insurance carrier relating to the workers' compensation and liability claims assumed by the Company. By September 30, 2005, and periodically thereafter, an actuarial valuation will be made to determine the remaining outstanding amount of workers' compensation and liability claims assumed by Allied, and the letter of credit issued by the Company in favor of Ryder System will be adjusted accordingly.

**Table of Contents****(11) Guarantees and Indemnifications***Guarantees*

The Company leases office space and certain terminal facilities under noncancelable and cancelable (i.e. month-to-month) operating lease agreements, some of which provide guarantees to third parties. With respect to the guarantees that the Company issued in the nine months ended September 30, 2003, the Company assessed the fair value of its obligation to stand ready to perform under these guarantees by considering the likelihood of the occurrence of the specified triggering events or conditions requiring performance as well as other assumptions and factors. The Company has not entered into any guarantees of significance in the nine months ended September 30, 2003.

*Indemnifications*

The Company enters into indemnification provisions under its agreements with certain of its customers, suppliers, service providers, and business partners in the ordinary course of business. Under these provisions, subject to various limitations and qualifications, the Company generally indemnifies and holds harmless the indemnified party for losses suffered or incurred by the indemnified party as a result of the Company's activities. The potential losses primarily relate to obligations that are insured under the Company's insurance programs. These indemnification provisions generally survive termination of the underlying agreement. The maximum potential amount of future payments the Company could be required to make under these indemnification provisions is unlimited. The Company has not incurred material costs to defend lawsuits or settle claims related to these indemnification agreements and does not expect to at this time. The fair value of these agreements is estimated to be minimal. The Company has no liabilities recorded for these agreements as of September 30, 2003.

In addition, the Company is obligated to indemnify its directors and officers who are, or were, serving at the Company's request in such capacities, subject to the Company's By-laws. The maximum potential amount of future payments that the Company could be required to make under the By-laws is unlimited; however the Company has Director and Officer insurance policies that, in most cases, would enable it to recover a portion of any future amounts paid. Historically, the Company has never incurred any costs to settle claims related to these indemnifications, and there are no claims outstanding as of September 30, 2003. Accordingly, no liabilities for indemnifications have been recorded as of September 30, 2003.

**(12) Net Income (Loss) Per Common Share**

SFAS No. 128, *Earnings Per Share*, requires presentation of basic and diluted earnings per share. Basic earnings per share are calculated by dividing net income available to common stockholders by the weighted average number of common shares outstanding for the years presented. Diluted earnings per share reflect the potential dilution that could occur if securities and other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that would then share in the earnings of the entity.

A reconciliation of net income (loss) and the weighted average number of common shares outstanding used to calculate basic and diluted net income (loss) per common share for the three and nine months ended September 30, 2003 and 2002 is as follows:

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>
<b>Basic and Diluted Earnings Per Share:</b>				
Weighted average number of common shares outstanding	8,507	8,324	8,459	8,282

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Loss before cumulative effect of a change in accounting principle	(\$ 1,975)	(\$ 6,482)	(\$ 4,267)	(\$ 5,529)
Cumulative effect of a change in accounting principle, net of taxes				(4,092)
Net loss	(\$ 1,975)	(\$ 6,482)	(\$ 4,267)	(\$ 9,621)
Net loss per share:				
Loss before cumulative effect of a change in accounting principle	(\$ 0.23)	(\$ 0.78)	(\$ 0.50)	(\$ 0.67)
Cumulative effect of a change in accounting principle, net of taxes				(\$ 0.49)
Net loss per common share	(\$ 0.23)	(\$ 0.78)	(\$ 0.50)	(\$ 1.16)

Common stock equivalents for approximately 291,000 and 318,000 shares outstanding for the three months ended September 30, 2003 and 2002, respectively, and 285,000 and 365,000 for the nine months ended September 30, 2003 and 2002, respectively, were excluded from the calculation of diluted earnings per share, as the impact would have been antidilutive.

**(13) Stock Option Plan**

The Company applies the intrinsic-value-based method of accounting prescribed by Accounting Principles Board (APB) Opinion No. 25, *Accounting for Stock Issued to Employees*, and related interpretations including FASB Interpretation No. 44, *Accounting for Certain Transactions Involving Stock Compensation, an interpretation of APB Opinion No. 25*, to account for its fixed-plan stock options. Under this method, compensation expense is recorded on the date of grant only if the current market price of the underlying stock exceeded the exercise price. SFAS No. 123, *Accounting for Stock-Based Compensation*, established accounting and disclosure requirements using a fair-value-based method of accounting for stock-based employee compensation plans. As allowed by SFAS No. 123, the Company has elected to continue to apply the intrinsic value based method of accounting described above, and has adopted only the disclosure requirements of SFAS No. 123.

The Company did not grant any significant stock options during the third quarter of 2003. If the Company had elected to recognize compensation cost based on the fair value at the grant dates, consistent with the method prescribed by SFAS No. 123, net income and earnings per share, using the Black-Scholes option pricing valuation model, would have been changed to the pro forma amounts indicated below for the three and nine months ended September 30, 2003 and 2002 (in thousands, except per share data):

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	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Reported net loss	(\$ 1,975)	(\$ 6,482)	(\$ 4,267)	(\$ 9,621)
Plus: stock-based employee compensation included in reported net income (loss), net of related taxes				
Less: stock-based employee compensation determined under the fair value method, net of related taxes	(138)	(174)	(394)	(470)
Pro forma net loss	(\$ 2,113)	(\$ 6,656)	(\$ 4,661)	(\$ 10,091)
Loss per share:				
As reported:				
Basic and diluted	(\$ 0.23)	(\$ 0.78)	(\$ 0.50)	(\$ 1.16)
Pro forma:				
Basic and diluted	(\$ 0.25)	(\$ 0.80)	(\$ 0.56)	(\$ 1.22)

**(14) Comprehensive Income**

Statement of Financial Accounting Standards ( SFAS ) No. 130, *Reporting Comprehensive Income*, requires companies to report all changes in equity during a period, except those resulting from investment by owners and distribution to owners. The Company had a comprehensive loss of \$2.2 million in the third quarter of 2003 versus a comprehensive loss of \$4.8 million in the third quarter of 2002. For the first nine months of 2003, the Company had comprehensive income of \$0.5 million versus a comprehensive loss of \$6.1 million for the first nine months of 2002. The difference between comprehensive income (loss) and net income (loss) is the foreign currency translation adjustment and minimum pension liability, net of income taxes.

**(15) Investment Income (Loss)**

Investment income (loss) consists of the following for the three and nine-months ended September 30, 2003 and 2002 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Interest and dividend income	\$ 341	\$ 892	\$ 1,870	\$ 2,609
Realized gains (losses)	2,011	(3,599)	2,593	(3,405)
Unrealized (losses) gains	(2,750)	2,910	(1,528)	1,886
Total	\$ (398)	\$ 203	\$ 2,935	\$ 1,090

**(16) Industry Segment and Geographic Information**

In accordance with the requirements of SFAS No. 131, *Disclosure About Segments of an Enterprise and Related Information*, the Company has identified two reportable industry segments through which it conducts its operating activities: Allied Automotive Group and Axis Group. These two segments reflect the organization used by management for internal reporting. Allied Automotive Group is engaged in the business of transporting automobiles, light trucks and SUVs from manufacturing plants, ports, auctions, and railway distribution points to automobile



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dealerships. Axis Group, through its subsidiaries, is engaged in the business of securing and managing vehicle distribution services, automobile inspections, auction and yard management services, intra-modal transport, vehicle tracking, vehicle accessorization, and dealer preparatory services for the automotive industry.

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
<b>Revenues unaffiliated customers:</b>				
Allied Automotive Group	\$ 190,532	\$ 205,679	\$ 619,832	\$ 643,769
Axis Group	6,557	7,306	20,927	21,459
<b>Total</b>	<b>\$ 197,089</b>	<b>\$ 212,985</b>	<b>\$ 640,759</b>	<b>\$ 665,228</b>
<b>Depreciation and amortization:</b>				
Allied Automotive Group	\$ 9,518	\$ 11,655	\$ 30,005	\$ 35,653
Axis Group	723	769	2,186	2,206
Corporate/Other	770	718	2,497	2,228
<b>Total</b>	<b>\$ 11,011</b>	<b>\$ 13,142</b>	<b>\$ 34,688</b>	<b>\$ 40,087</b>
<b>Operating profit (loss):</b>				
Allied Automotive Group	\$ 5,370	\$ (580)	\$ 11,987	\$ 15,430
Axis Group	886	1,371	2,550	2,965
Corporate/Other	(3,109)	(2,158)	(5,554)	(6,133)
<b>Total</b>	<b>\$ 3,147</b>	<b>\$ (1,367)</b>	<b>\$ 8,983</b>	<b>\$ 12,262</b>
<b>Reconciling items:</b>				
Interest expense	\$ (7,366)	\$ (7,611)	\$ (22,120)	\$ (23,343)
Investment (loss) income	(398)	203	2,935	1,090
Gain on early extinguishment of debt				2,750
Foreign exchange (loss) gain, net	(62)	124	2,386	157
Other, net	1,976	(57)	1,976	(264)
<b>Loss before income taxes and cumulative effect of change in accounting principle</b>	<b>\$ (2,703)</b>	<b>\$ (8,708)</b>	<b>\$ (5,840)</b>	<b>\$ (7,348)</b>
<b>Capital expenditures:</b>				
Allied Automotive Group	\$ 2,990	\$ 5,739	\$ 11,013	\$ 13,125
Axis Group	64	98	265	182
Corporate /Other	76	6	269	6
<b>Total</b>	<b>\$ 3,130</b>	<b>\$ 5,843</b>	<b>\$ 11,547</b>	<b>\$ 13,313</b>

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	<u>September 30, 2003</u>	<u>December 31, 2002</u>
Total assets:		
Allied Automotive Group	\$ 280,870	\$ 296,935
Axis Group	32,878	35,663
Corporate/Other	150,601	152,910
<b>Total</b>	<b>\$ 464,349</b>	<b>\$ 485,508</b>

Geographical information for the three and nine months ended September 30, 2003 and 2002 is as follows (in thousands):

	<u>Three Months Ended September 30,</u>		<u>Nine Months Ended September 30,</u>	
	<u>2003</u>	<u>2002</u>	<u>2003</u>	<u>2002</u>
Revenues:				
United States	\$ 166,678	\$ 179,155	\$ 525,435	\$ 551,127
Canada	30,411	33,830	115,324	114,101
<b>Total</b>	<b>\$ 197,089</b>	<b>\$ 212,985</b>	<b>\$ 640,759</b>	<b>\$ 665,228</b>

	<u>September 30, 2003</u>	<u>December 31, 2002</u>
Long-lived assets:		
United States	\$ 217,760	\$ 224,119
Canada	63,582	58,310
<b>Total</b>	<b>\$ 281,342</b>	<b>\$ 282,429</b>

Revenues are attributed to the respective countries based on the location of the origination terminal. Substantially all of the Company's revenues and receivables are realized in the automotive industry by the Allied Automotive Group.

**(17) Supplemental Guarantor Information**

The following consolidating balance sheet information, statements of operations information, and statements of cash flows information present the financial statement information of the parent company and the combined financial statements information of the Guarantor subsidiaries and Nonguarantor Subsidiaries. The Guarantors are jointly and severally liable for the Company's obligations under the Notes and there are no restrictions on the ability of the Guarantors to make distributions to the Company.



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**SUPPLEMENTAL CONDENSED CONSOLIDATING BALANCE SHEET INFORMATION**  
**SEPTEMBER 30, 2003**  
(In Thousands)

	<u>ALLIED HOLDINGS</u>	<u>GUARANTOR SUBSIDIARIES</u>	<u>NONGUARANTOR SUBSIDIARIES</u>	<u>ELIMINATIONS</u>	<u>CONSOLIDATED</u>
<b>CURRENT ASSETS:</b>					
Cash and cash equivalents	\$	\$ 414	\$ 82,935	\$	\$ 83,349
Short-term investments					
Receivables, net of allowance for doubtful accounts		52,411	5,667		58,078
Inventories		4,874			4,874
Deferred tax asset - current	21,795	2,239			24,034
Prepayments and other current assets	1,297	11,287	88		12,672
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total current assets	23,092	71,225	88,690		183,007
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>PROPERTY AND EQUIPMENT, NET</b>	7,294	148,212	3,033		158,539
<b>OTHER ASSETS:</b>					
Goodwill, net	1,515	87,483			88,998
Other	31,286	1,710	809		33,805
Deferred tax asset - noncurrent	23,654			(23,654)	
Intercompany receivables	59,897			(59,897)	
Investment in subsidiaries	32,144	5,544		(37,688)	
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total other assets	148,496	94,737	809	(121,239)	122,803
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total assets	\$ 178,882	\$ 314,174	\$ 92,532	\$ (121,239)	\$ 464,349
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>CURRENT LIABILITIES:</b>					
Current maturities of long-term debt	\$	\$ 17,854	\$	\$	\$ 17,854
Trade accounts payable	2,468	25,229	120		27,817
Intercompany payables		54,618	5,279	(59,897)	
Accrued liabilities	14,049	52,845	26,527		93,421
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total current liabilities	16,517	150,546	31,926	(59,897)	139,092
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>LONG-TERM DEBT, less current maturities</b>	150,000	86,376			236,376
<b>POSTRETIREMENT BENEFITS OTHER THAN PENSIONS</b>		6,530			6,530
<b>DEFERRED INCOME TAXES</b>		34,570	448	(23,654)	11,364
<b>OTHER LONG-TERM LIABILITIES</b>	1,031	26,915	31,707		59,653
<b>STOCKHOLDERS EQUITY:</b>					
Common stock, no par value					
Additional paid-in capital	47,373	166,130	2,488	(168,618)	47,373
Treasury stock	(707)				(707)
(Accumulated deficit) retained earnings	(30,687)	(145,349)	25,963	119,386	(30,687)
Accumulated other comprehensive loss, net of tax	(4,645)	(11,544)		11,544	(4,645)
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total stockholders equity	11,334	9,237	28,451	(37,688)	11,334
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total liabilities and stockholders equity	\$ 178,882	\$ 314,174	\$ 92,532	\$ (121,239)	\$ 464,349
		<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>



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**SUPPLEMENTAL CONDENSED CONSOLIDATING BALANCE SHEET INFORMATION**  
**DECEMBER 31, 2002**  
(In Thousands)

	<u>ALLIED HOLDINGS</u>	<u>GUARANTOR SUBSIDIARIES</u>	<u>NONGUARANTOR SUBSIDIARIES</u>	<u>ELIMINATIONS</u>	<u>CONSOLIDATED</u>
<b>CURRENT ASSETS:</b>					
Cash and cash equivalents	\$ 7	\$ 1,936	\$ 8,310	\$	\$ 10,253
Short-term investments			60,732		60,732
Receivables, net of allowance for doubtful accounts		56,003	2,509		58,512
Inventories		5,071			5,071
Deferred tax assets	37,615	2,211			39,826
Prepayments and other current assets	17,645	10,826	214		28,685
	<u>55,267</u>	<u>76,047</u>	<u>71,765</u>	<u></u>	<u>203,079</u>
<b>PROPERTY AND EQUIPMENT, NET</b>	8,957	164,501	3,205		176,663
<b>OTHER ASSETS:</b>					
Goodwill, net	1,515	83,726			85,241
Other	16,860	2,743	922		20,525
Deferred tax asset	7,445			(7,445)	
Intercompany receivables	55,952		91	(56,043)	
Investment in subsidiaries	28,466	5,111		(33,577)	
	<u>110,238</u>	<u>91,580</u>	<u>1,013</u>	<u>(97,065)</u>	<u>105,766</u>
<b>Total assets</b>	<u>\$ 174,462</u>	<u>\$ 332,128</u>	<u>\$ 75,983</u>	<u>\$ (97,065)</u>	<u>\$ 485,508</u>
<b>CURRENT LIABILITIES:</b>					
Current maturities of long-term debt	\$	\$ 10,785	\$	\$	\$ 10,785
Trade accounts payable	3,362	32,930	293		36,585
Intercompany payables		56,043		(56,043)	
Accrued liabilities	9,755	63,835	19,291		92,881
	<u>13,117</u>	<u>163,593</u>	<u>19,584</u>	<u>(56,043)</u>	<u>140,251</u>
<b>LONG-TERM DEBT, less current maturities</b>	150,000	87,690			237,690
<b>POSTRETIREMENT BENEFITS OTHER THAN PENSIONS</b>		7,467			7,467
<b>DEFERRED INCOME TAXES</b>		34,743	448	(7,445)	27,746
<b>OTHER LONG-TERM LIABILITIES</b>	1,031	31,572	29,437		62,040
<b>STOCKHOLDERS EQUITY:</b>					
Common stock, no par value					
Additional paid-in capital	46,801	166,130	2,488	(168,618)	46,801
Treasury stock	(707)				(707)
(Accumulated deficit) retained earnings	(26,420)	(146,278)	24,026	122,252	(26,420)
Accumulated other comprehensive loss, net of tax	(9,360)	(12,789)		12,789	(9,360)
	<u>10,314</u>	<u>7,063</u>	<u>26,514</u>	<u>(33,577)</u>	<u>10,314</u>
<b>Total liabilities and stockholders equity</b>	<u>\$ 174,462</u>	<u>\$ 332,128</u>	<u>\$ 75,983</u>	<u>\$ (97,065)</u>	<u>\$ 485,508</u>



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**SUPPLEMENTAL CONDENSED CONSOLIDATED INCOME STATEMENT INFORMATION**  
**THREE MONTHS ENDED SEPTEMBER 30, 2003**  
(In Thousands)

	<u>ALLIED HOLDINGS</u>	<u>GUARANTOR SUBSIDIARIES</u>	<u>NONGUARANTOR SUBSIDIARIES</u>	<u>ELIMINATIONS</u>	<u>CONSOLIDATED</u>
<b>REVENUES</b>	\$ 6,805	\$ 196,733	\$ 9,251	\$ (15,700)	\$ 197,089
<b>OPERATING EXPENSES:</b>					
Salaries, wages and fringe benefits	3,469	103,900			107,369
Operating supplies and expenses	2,298	27,609	53		29,960
Purchased transportation		24,082			24,082
Insurance and claims		8,260	8,895	(8,895)	8,260
Operating taxes and licenses	59	6,933			6,992
Depreciation and amortization	770	10,120	121		11,011
Rents	473	1,104	2		1,579
Communications and utilities	1,256	484	5		1,745
Other operating expenses	1,550	8,003	43	(6,805)	2,791
Loss on disposal of operating assets, net		153			153
<b>Total operating expenses</b>	<b>9,875</b>	<b>190,648</b>	<b>9,119</b>	<b>(15,700)</b>	<b>193,942</b>
<b>Operating (loss) income</b>	<b>(3,070)</b>	<b>6,085</b>	<b>132</b>		<b>3,147</b>
<b>OTHER INCOME (EXPENSE):</b>					
Interest expense	(1,640)	(5,632)	(94)		(7,366)
Investment income		12	(410)		(398)
Foreign exchange loss, net		(23)	(39)		(62)
Equity in earnings of subsidiaries	142	86		(228)	
Other, net	1,976				1,976
	478	(5,557)	(543)	(228)	(5,850)
<b>(LOSS) INCOME BEFORE INCOME TAXES</b>	<b>(2,592)</b>	<b>528</b>	<b>(411)</b>	<b>(228)</b>	<b>(2,703)</b>
<b>INCOME TAX BENEFIT (EXPENSE)</b>	<b>617</b>		<b>111</b>		<b>728</b>
<b>NET (LOSS) INCOME</b>	<b>\$ (1,975)</b>	<b>\$ 528</b>	<b>\$ (300)</b>	<b>\$ (228)</b>	<b>\$ (1,975)</b>

**SUPPLEMENTAL CONDENSED CONSOLIDATED INCOME STATEMENT INFORMATION**  
**THREE MONTHS ENDED SEPTEMBER 30, 2002**  
(In Thousands)

	<u>ALLIED HOLDINGS</u>	<u>GUARANTOR SUBSIDIARIES</u>	<u>NONGUARANTOR SUBSIDIARIES</u>	<u>ELIMINATIONS</u>	<u>CONSOLIDATED</u>
<b>REVENUES</b>	\$ 6,435	\$ 212,625	\$ 9,490	\$ (15,565)	\$ 212,985
<b>OPERATING EXPENSES:</b>					
Salaries, wages and fringe benefits	3,634	114,170			117,804
Operating supplies and expenses	1,941	31,259	57		33,257
Purchased transportation		25,331			25,331
Insurance and claims		10,844	9,130	(9,130)	10,844

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Operating taxes and licenses	58	7,580			7,638
Depreciation and amortization	718	12,306	118		13,142
Rents	547	1,136	2		1,685
Communications and utilities	541	882	2		1,425
Other operating expenses	1,056	8,174	64	(6,435)	2,859
Loss on disposal of operating assets, net		160	207		367
Total operating expenses	8,495	211,842	9,580	(15,565)	214,352
Operating (loss) income	(2,060)	783	(90)		(1,367)
<b>OTHER INCOME (EXPENSE):</b>					
Interest expense	(4,791)	(2,831)	(39)	50	(7,611)
Investment income		1	252	(50)	203
Intercompany dividends	166	(166)			
Foreign exchange gain, net		124			124
Other, net		(206)	149		(57)
Equity in (losses) earnings of subsidiaries	(2,665)	156		2,509	
	(7,290)	(2,922)	362	2,509	(7,341)
<b>(LOSS) INCOME BEFORE INCOME TAXES &amp; CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE</b>					
	(9,350)	(2,139)	272	2,509	(8,708)
<b>INCOME TAX BENEFIT (EXPENSE)</b>					
	2,868	(39)	(603)		2,226
<b>(LOSS) INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE</b>					
	(6,482)	(2,178)	(331)	2,509	(6,482)
<b>CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET OF TAX</b>					
<b>NET LOSS</b>	<b>\$ (6,482)</b>	<b>\$ (2,178)</b>	<b>\$ (331)</b>	<b>\$ 2,509</b>	<b>\$ (6,482)</b>

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**SUPPLEMENTAL CONDENSED CONSOLIDATED INCOME STATEMENT INFORMATION**  
**NINE MONTHS ENDED SEPTEMBER 30, 2003**  
(In Thousands)

	<b>ALLIED HOLDINGS</b>	<b>GUARANTOR SUBSIDIARIES</b>	<b>NONGUARANTOR SUBSIDIARIES</b>	<b>ELIMINATIONS</b>	<b>CONSOLIDATED</b>
<b>REVENUES</b>	\$ 20,909	\$ 639,719	\$ 27,509	\$ (47,378)	\$ 640,759
<b>OPERATING EXPENSES:</b>					
Salaries, wages and fringe benefits	8,634	339,812			348,446
Operating supplies and expenses	6,841	96,136	131		103,108
Purchased transportation		74,632			74,632
Insurance and claims		29,247	26,316	(26,469)	29,094
Operating taxes and licenses	182	22,807			22,989
Depreciation and amortization	2,497	31,838	353		34,688
Rents	1,461	3,353	5		4,819
Communications and utilities	3,106	2,096	11		5,213
Other operating expenses	3,693	25,153	238	(20,909)	8,175
Loss on disposal of operating assets, net		612			612
<b>Total operating expenses</b>	<b>26,414</b>	<b>625,686</b>	<b>27,054</b>	<b>(47,378)</b>	<b>631,776</b>
<b>Operating (loss) income</b>	<b>(5,505)</b>	<b>14,033</b>	<b>455</b>		<b>8,983</b>
<b>OTHER INCOME (EXPENSE):</b>					
Interest expense	(5,614)	(16,312)	(194)		(22,120)
Investment income		54	2,881		2,935
Foreign exchange gain (loss) gains, net		2,398	(12)		2,386
Equity in earnings of subsidiaries	2,433	433		(2,866)	
Other, net	1,976				1,976
	<b>(1,205)</b>	<b>(13,427)</b>	<b>2,675</b>	<b>(2,866)</b>	<b>(14,823)</b>
<b>(LOSS) INCOME BEFORE INCOME TAXES</b>	<b>(6,710)</b>	<b>606</b>	<b>3,130</b>	<b>(2,866)</b>	<b>(5,840)</b>
<b>INCOME TAX BENEFIT (EXPENSE)</b>	<b>2,443</b>	<b>323</b>	<b>(1,193)</b>		<b>1,573</b>
<b>NET (LOSS) INCOME</b>	<b>\$ (4,267)</b>	<b>\$ 929</b>	<b>\$ 1,937</b>	<b>\$ (2,866)</b>	<b>\$ (4,267)</b>

**SUPPLEMENTAL CONDENSED CONSOLIDATED INCOME STATEMENT INFORMATION**  
**NINE MONTHS ENDED SEPTEMBER 30, 2002**  
(In Thousands)

	<b>ALLIED HOLDINGS</b>	<b>GUARANTOR SUBSIDIARIES</b>	<b>NONGUARANTOR SUBSIDIARIES</b>	<b>ELIMINATIONS</b>	<b>CONSOLIDATED</b>
<b>REVENUES</b>	\$ 11,505	\$ 664,108	\$ 28,509	\$ (38,894)	\$ 665,228
<b>OPERATING EXPENSES:</b>					
Salaries, wages and fringe benefits	7,069	356,784			363,853
Operating supplies and expenses	2,728	97,198	142		100,068
Purchased transportation		72,438			72,438

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Insurance and claims		34,342	27,391	(27,389)	34,344
Operating taxes and licenses	166	24,565			24,731
Depreciation and amortization	2,228	37,504	355		40,087
Rents	1,394	3,496	5		4,895
Communications and utilities	867	4,415	8		5,290
Other operating expenses	2,904	15,923	285	(11,505)	7,607
(Gain) loss on disposal of operating assets, net		(554)	207		(347)
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Total operating expenses	17,356	646,111	28,393	(38,894)	652,966
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Operating (loss) income	(5,851)	17,997	116		12,262
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>OTHER INCOME (EXPENSE):</b>					
Interest expense	(12,307)	(11,005)	(171)	140	(23,343)
Investment income	1	27	1,202	(140)	1,090
Gain on early extinguishment of debt	2,750				2,750
Intercompany dividends	1,144	(1,144)			
Foreign exchange (loss) gain, net	(8)	165			157
Other, net		(206)	(58)		(264)
Equity in earnings of subsidiaries	1,575	289		(1,864)	
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
	(6,845)	(11,874)	973	(1,864)	(19,610)
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>(LOSS) INCOME BEFORE INCOME TAXES &amp; CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE</b>					
	(12,696)	6,123	1,089	(1,864)	(7,348)
<b>INCOME TAX BENEFIT (EXPENSE)</b>	3,075	933	(2,189)		1,819
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>(LOSS) INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE</b>					
	(9,621)	7,056	(1,100)	(1,864)	(5,529)
<b>CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE, NET OF TAX</b>		(4,092)			(4,092)
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>NET (LOSS) INCOME</b>	\$ (9,621)	\$ 2,964	\$ (1,100)	\$ (1,864)	\$ (9,621)
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>



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**SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS INFORMATION**  
**NINE MONTHS ENDED SEPTEMBER 30, 2003**  
(In Thousands)

	<u>ALLIED HOLDINGS</u>	<u>GUARANTOR SUBSIDIARIES</u>	<u>NONGUARANTOR SUBSIDIARIES</u>	<u>ELIMINATIONS</u>	<u>CONSOLIDATED</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>					
Net (loss) income	\$ (4,267)	\$ 929	\$ 1,937	\$ (2,866)	\$ (4,267)
Reconciliation of net (loss) income to net cash provided by operating activities:					
Interest expense paid in kind		1,065			1,065
Amortization of deferred financing costs	3,007				3,007
Depreciation and amortization	2,497	31,838	353		34,688
Loss on disposal of assets and other, net		612			612
Foreign exchange gain, net		(2,386)			(2,386)
Deferred income taxes	(3,402)				(3,402)
Compensation expense related to stock options and grants	290				290
Equity in earnings of subsidiaries	(2,433)	(433)		(2,866)	
Amortization of Teamsters Union contract costs		1,000			1,000
Change in operating assets and liabilities:					
Receivables, net of allowance for doubtful accounts		4,998	(3,158)		1,840
Inventories		336			336
Prepayments and other current assets	16,348	(115)	126		16,359
Short-term investments			60,732		60,732
Trade accounts payable	(894)	(8,609)	(173)		(9,676)
Intercompany receivables	2,535	(7,905)	5,370		
Accrued liabilities and other	(10,152)	(17,950)	9,506		(18,596)
Net change in operating assets and liabilities	7,837	(29,245)	72,403		50,995
Net cash provided by operating activities	3,529	3,380	74,693		81,602
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>					
Purchases of property and equipment	(269)	(11,210)	(68)		(11,547)
Proceeds from sale of property and equipment		287			287
Decrease in cash surrender value of life insurance	2				2
Net cash used in investing activities	(267)	(10,923)	(68)		(11,258)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>					
Repayments of revolving credit facilities, net		(20,280)			(20,280)
Additions to long-term debt		99,875			99,875
Repayment of long-term debt		(74,905)			(74,905)
Payment of deferred financing costs	(3,031)				(3,031)
Proceeds from issuance of common stock	282				282
Other, net	(520)	585			65
Net cash (used in) provided by financing activities	(3,269)	5,275			2,006

<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>		746			746
<b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	(7)	(1,522)	74,625		73,096
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	7	1,936	8,310		10,253
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	\$	\$ 414	\$ 82,935	\$	\$ 83,349

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**SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS**  
**NINE MONTHS ENDED SEPTEMBER 30, 2002**  
**In Thousands**

	<u>ALLIED HOLDINGS</u>	<u>GUARANTOR SUBSIDIARIES</u>	<u>NONGUARANTOR SUBSIDIARIES</u>	<u>ELIMINATIONS</u>	<u>CONSOLIDATED</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>					
Net (loss) income	\$ (9,621)	\$ 2,964	\$ (1,100)	\$ (1,864)	\$ (9,621)
Adjustments to reconcile net (loss) income to net cash provided by (used in) operating activities:					
Gain on early extinguishment of debt	(2,750)				(2,750)
Interest expense paid in kind		746			746
Amortization of deferred financing costs	3,013				3,013
Depreciation and amortization	2,228	37,504	355		40,087
Gain on disposal of assets and other, net		(83)			(83)
Foreign exchange gain, net	8	(165)			(157)
Cumulative effect of change in accounting principle		4,092			4,092
Deferred income taxes	704	(2,698)	(575)		(2,569)
Compensation expense related to stock options and grants	(210)				(210)
Equity in earnings of subsidiaries	(1,575)	(289)		1,864	
Amortization of Teamsters Union contract costs		1,800			1,800
Change in operating assets and liabilities:					
Receivables, net of allowance for doubtful accounts	24	11,826	426		12,276
Inventories		50	5		55
Prepayments and other current assets	(635)	2,136	55		1,556
Short-term investments			2,367		2,367
Trade accounts payable	48	(4,181)	76		(4,057)
Intercompany payables	186,845	(180,485)	(6,360)		
Accrued liabilities	(2,080)	(3,483)	14,096		8,533
Net change in operating assets and liabilities	184,202	(174,137)	10,665		20,730
Net cash provided by (used in) operating activities	175,999	(130,266)	9,345		55,078
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>					
Purchases of property and equipment	(6)	(13,303)	(4)		(13,313)
Intercompany sale of property and equipment	(2)	2			
Proceeds from sale of property and equipment		3,005			3,005
Proceeds from sale of equity investment in joint venture			2,700		2,700
Capital contribution	(73,178)	73,100	78		
Return of capital	40,881	(39,829)	(1,052)		
Increase in cash surrender value of life insurance	1,341				1,341
Net cash (used in) provided by investing activities	(30,964)	22,975	1,722		(6,267)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>					

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(Repayments) additions to revolving credit facilities, net	(98,900)	36,516			(62,384)
Additions to long-term debt		82,750			82,750
Repayment of long-term debt	(37,498)	(8,862)			(46,360)
Payment of deferred financing costs	(9,262)				(9,262)
Proceeds from issuance of common stock	262				262
Other, net	154	95	300		549
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Net cash (used in) provided by financing activities	(145,244)	110,499	300		(34,445)
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
<b>EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS</b>		16			16
<b>NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS</b>	(209)	3,224	11,367		14,382
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD</b>	<u>209</u>	<u>1,063</u>	<u>9,271</u>	<u>          </u>	<u>10,543</u>
<b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
	<u>          </u>	<u>4,287</u>	<u>20,638</u>	<u>          </u>	<u>24,925</u>

**Table of Contents****Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations****Results of Operations**

The Company, through its subsidiaries, generates revenues by providing services to the automotive industry. Allied Automotive Group, Inc. ( AAG ) is the largest motor carrier in North America specializing in the transportation of new automobiles, light trucks and SUVs, for most of the major domestic and foreign automotive manufacturers.

The following table sets forth the percentage relationship of expense items to revenues for the periods indicated:

	Three Months Ended September 30		Nine Months Ended September 30	
	2003	2002	2003	2002
Revenues	100.0%	100.0%	100.0%	100.0%
Operating expenses:				
Salaries, wages and fringe benefits	54.5	55.3	54.4	54.7
Operating supplies and expenses	15.2	15.6	16.1	15.1
Purchased transportation	12.2	11.9	11.6	10.9
Insurance and claims	4.2	5.1	4.5	5.2
Operating taxes and licenses	3.5	3.6	3.6	3.7
Depreciation and amortization	5.6	6.2	5.4	6.0
Rents	0.8	0.8	0.8	0.8
Communications and utilities	0.9	0.7	0.8	0.8
Other operating expenses	1.4	1.3	1.3	1.1
Loss (gain) on sale of operating assets, net	0.1	0.2	0.1	(0.1)
Total operating expenses	98.4	100.7	98.6	(98.2)
Operating income (loss)	1.6	(0.7)	1.4	1.8
Other income (expense):				
Interest expense	(3.8)	(3.6)	(3.5)	(3.5)
Investment income (loss)	(0.2)	0.1	0.5	0.2
Gain on early extinguishment of debt	0.0	0.0	0.0	0.4
Foreign exchange gain, net	0.0	0.1	0.4	0.0
Other, net	1.0	0.0	0.3	0.0
	(3.0)	(3.4)	(2.3)	(2.9)
Loss before income taxes and cumulative effect of change in accounting principle	(1.4)	(4.1)	(0.9)	(1.1)
Income tax benefit	0.4	1.1	0.2	0.3
Loss before cumulative effect of change in accounting principle	(1.0)	(3.0)	(0.7)	(0.8)
Cumulative effect of change in accounting principle, net of tax	0.0	0.0	0.0	(0.6)
Net Loss	(1.0)%	(3.0)%	(0.7)%	(1.4)%

**Three and Nine Months Ended September 30, 2003 Compared to Three and Nine Months Ended September 30, 2002**

Revenues were \$197.1 million in the third quarter of 2003 compared to revenues of \$213.0 million in the third quarter of 2002, a decrease of \$15.9 million, or 7.5%. For the nine-month period ended September 30, 2003, revenues were \$640.8 million, versus revenues of \$665.2 million

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for the nine-month period ended September 30, 2002, a decrease of \$24.4 million, or 3.7%. The decline in revenues in the third quarter and for the first nine months of 2003 versus 2002

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was due primarily to a decline in the number of vehicle deliveries, lower production levels by the automotive manufacturers, as well the Company's decision to exit non-performing business, including the traffic for General Motors in Jessup, Maryland. During the fourth quarter of 2003, the Company will cease delivering a portion of the business it currently transports from the General Motor's Saturn Spring Hill, Tennessee location. Both pieces of traffic at these locations has historically generated operating losses with aggregate annual revenues of \$16.6 million.

Vehicle deliveries declined by 6.2% in the first nine months of 2003, while North American new vehicle production declined by 4.2%. Offsetting the decline in revenues due to the decrease in vehicle deliveries was an increase in the revenue generated per vehicle delivered of 6.9% in the third quarter of 2003 and 2.7% for the first nine months of 2003 compared to the same period in 2002. The increase in revenue per vehicle is due primarily to ancillary revenue in the US operations related to the model changeovers and new product launches. These vehicles are held until all launch related issues are resolved. During this time the Company will shuttle the vehicles to a holding yard and may shuttle them back to the plant as necessary until the vehicles are cleared for delivery to the dealerships. Accordingly, the changeovers and new product launches cause an increase in revenues without a corresponding increase in the number of vehicles delivered. In addition, revenue per vehicle delivered in Canada increased due to the higher Canadian dollar exchange rates.

The Company recorded a net loss of \$2.0 million in the third quarter of 2003 versus a net loss of \$6.5 million in the third quarter of 2002. Results for the third quarter of 2003 include a gain of approximately \$2.0 million related to the settlement of the Ryder litigation claim discussed in footnote 10. This amount is included in the statement of operations as other income. Basic and diluted loss per share in the third quarter of 2003 was \$0.23 versus \$0.78 in the third quarter of 2002. For the nine-month period ended September 30, 2003, the Company experienced a net loss of \$4.3 million versus a net loss of \$9.6 million for the nine-month period ended September 30, 2002. Results for the first nine months of 2002 include a \$2.8 million pre-tax gain on the early extinguishment of the Company's subordinated notes and a \$4.1 million after-tax charge (\$5.2 million pre-tax) related to the impairment of goodwill at the Company's Axis Group subsidiary. Basic and diluted loss per share were \$0.50 for the nine-month period ended September 30, 2003 versus basic and diluted loss per share of \$1.16 for the nine-month period ended September 30, 2002.

Earnings before interest, taxes, depreciation and amortization, gains and losses on disposal of assets, gain on the early extinguishment of debt, foreign exchange gains and losses, investment income and losses, cumulative effect of accounting changes and other income ( Adjusted EBITDA ) for the third quarter of 2003 were \$14.3 million compared to \$12.1 million of Adjusted EBITDA reported during the third quarter of 2002. Adjusted EBITDA for the third quarter of 2003 was adversely affected by decreased vehicle deliveries arising from original equipment manufacturer ( OEM ) production declines in 2003 versus 2002. The decline in revenue was more than offset by the Company's internal initiatives that continued to gain traction. These initiatives, which include management's focus to improve quality and safety, led to a decline in incidents and amounts expensed by \$2.6 million for cargo damage and worker injuries as compared to the same period in 2002.

For the nine-month period ended September 30, 2003 Adjusted EBITDA was \$44.3 million versus \$52.0 million for the nine-month period ended September 30, 2002. During the first nine months of 2003, Adjusted EBITDA was adversely affected by a decrease in vehicle deliveries and increased fuel and wages costs, which were partially offset by the positive impact of the Company's internal initiatives to reduce costs related to insurance and claims expense and improved operating efficiencies.

Adjusted EBITDA is presented because management believes it provides useful information to investors regarding the Company's ability to generate cash flows that can be used to service debt and provide for capital expenditures. Adjusted EBITDA is also a component of certain financial covenants in the Company's debt agreements. The Company's net loss is the closest measure in the Company's financial statements prepared in accordance with Generally Accepted Accounting Principles ( GAAP ), in terms of comparability to Adjusted EBITDA. As such, a reconciliation of Adjusted EBITDA to the net loss for the quarters and nine months ended September 30, 2003 and 2002 are provided below. Because Adjusted EBITDA is not a measure determined in accordance with GAAP and is thus susceptible to varying calculations, Adjusted EBITDA as presented may not be comparable to other similarly titled measures used by other companies.

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The following table reconciles Adjusted EBITDA to Net loss for the three and nine months ended September 30, 2003 and 2002 (in thousands):

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2003	2002	2003	2002
Reconciliation of Net loss to Adjusted EBITDA:				
Net loss	(\$ 1,975)	(\$ 6,482)	(\$ 4,267)	(\$ 9,621)
Income tax benefit	(728)	(2,226)	(1,573)	(1,819)
Interest expense	7,366	7,611	22,120	23,343
Investment losses (income)	398	(203)	(2,935)	(1,090)
Gain on early extinguishment of debt				(2,750)
Foreign exchange losses (gains), net	62	(124)	(2,386)	(157)
Other, net	(1,976)	57	(1,976)	264
Cumulative effect of change in accounting principle, net of tax				4,092
Loss (gain) on disposal of operating assets	153	367	612	(347)
Depreciation and Amortization	11,011	13,142	34,688	40,087
Adjusted EBITDA	<u>\$ 14,311</u>	<u>\$ 12,142</u>	<u>\$ 44,283</u>	<u>\$ 52,002</u>

The following is a discussion of the changes in the Company's major expense categories:

Salaries, wages and fringe benefits decreased from 55.3% of revenues in the third quarter of 2002 to 54.5% of revenues in the third quarter of 2003, and decreased from 54.7% of revenues for the nine-month period ended September 30, 2002 to 54.4% of revenues for the nine-month period ended September 30, 2003. The decrease is due primarily to increased driver productivity and a reduction in workers' compensation expense, which are a result of the Company's ongoing initiatives to improve productivity and to reduce worker injuries. The benefit of the internal initiatives more than offset the impact of Teamster wage and benefit inflation.

During the second quarter of 2003, the Company began operating under a new five-year agreement with the International Brotherhood of Teamsters (Teamsters) in the United States. The agreement was effective beginning June 1, 2003. The new agreement with the Teamsters in the United States covers approximately 70% of the Company's employees. Economic provisions of the new agreement include a wage freeze for the first two years of the agreement and wage increases of approximately 2.0% on June 1, 2005, 2.0% on June 1, 2006, and an additional 2.5% on June 1, 2007. The agreement provides for increases in health, welfare and pension contributions by the Company during each year of the agreement. The economic provisions of the contract are anticipated to increase the Company's U.S. Teamster labor costs approximately 1.1% in year one of the agreement, 1.3% in year two, 2.5% in year three, 2.5% in year four, and 3.0% in year five of the agreement.

During March 2003, the Company renegotiated a contract that expired October 31, 2002 with the Teamsters Union in Eastern Canada. The employees governed by this contract represent approximately 70% of the Company's total bargaining unit employees in Canada. The employees in Eastern Canada agreed to a three-year contract with a wage freeze in the first two years and increases in the third year. Health and welfare costs were frozen for the entire three-year agreement and there were pension increases each year of the new contract. The additional pension contributions will increase costs approximately 0.2% in year one of the agreement and approximately 0.6% in year two of the agreement. The wage and pension increases in year three of the agreement will increase costs approximately 3.2%.



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During the third quarter of 2003, the Company granted 250 shares of the Company's common stock to all non-bargaining employees. In order to earn the stock, employees were required to take a one-week furlough and remain working with the Company for one year from the date of grant. The Company recorded a charge to deferred compensation of approximately \$660,000 as a result of the grant, of which \$110,000 was recorded as expense during the third quarter of 2003.

Operating supplies and expenses decreased from 15.6% of revenues in the third quarter of 2002 to 15.2% of revenues in the third quarter of 2003, and increased from 15.1% of revenues for the nine-month period ended September 30, 2002 to 16.1% of revenues for the nine-month period ended September 30, 2003. The increase for the nine-month period was due primarily to an increase in fuel costs experienced in 2003. Fuel costs increased by an average of 19% per gallon, resulting in higher fuel expense of \$5.1 million in the first nine months of 2003 versus the first nine months of 2002. The Company has negotiated fuel surcharges with customers representing approximately 64.0% of the Company's customers, which enables it to pass on fuel costs to such customers. However, the customer fuel surcharges typically reset at the beginning of each quarter based on the fuel prices from the previous quarter. Therefore, there is a one-quarter lag between the time fuel prices change and the adjustment to the fuel surcharge. Fuel surcharges are recorded as a component of revenue.

Purchased transportation increased from 11.9% of revenues in the third quarter of 2002 to 12.2% of revenues in the third quarter of 2003, and increased from 10.9% of revenues for the nine-month period ended September 30, 2002 to 11.6% of revenues for the nine-month period ended September 30, 2003. The increase was due primarily to a shift in the mix of owner-operators versus company drivers and an increase in business at locations where owner-operators are utilized for vehicle deliveries. All costs for owner-operators are included in purchased transportation expense.

Insurance and claims expense decreased from 5.1% of revenues in the third quarter of 2002 to 4.2% of revenues in the third quarter of 2003, and decreased from 5.2% of revenues for the nine-month period ended September 30, 2002 to 4.5% of revenues for the nine-month period ended September 30, 2003. The decrease was due primarily to lower cargo claims experienced on shipped vehicles, resulting from the Company's ongoing initiatives to improve quality and safety measures, as well as improve claims processing to eliminate payment of claims not caused by the Company.

Depreciation and amortization decreased from 6.2% of revenues in the third quarter of 2002 to 5.6% of revenues in the third quarter of 2003, and decreased from 6.0% of revenues for the nine-month period ended September 30, 2002 to 5.4% of revenues for the nine-month period ended September 30, 2003. The decrease is due primarily to the disposal of assets in 2002 with a net book value of approximately \$5.1 million, combined with capital spending that was lower than depreciation and amortization expense in calendar year 2002 as well as for the first nine months of 2003.

During 2002, the Company performed an analysis of certain fleet equipment that was idled. The assets were evaluated in order to determine if they were candidates for the fleet remanufacturing and engine replacement program. Approximately 1,000 tractors or trailers were not considered viable candidates for the program and a decision was made that they would not be placed back into operations. As a result, depreciation was accelerated to the reduced useful life resulting in an additional charge of \$2.1 million to depreciation expense in the fourth quarter of 2002. During the second quarter of 2003, the Company began disposal of these assets and anticipates substantial completion by the end of 2003.

The Company continues its tractor and trailer ( Rig ) remanufacturing program to remanufacture existing owned Rigs rather than purchasing new Rigs. Remanufacturing existing Rigs requires less capital spending than purchasing new Rigs. During the third quarter of 2003, the Company remanufactured approximately 38 Rigs and replaced approximately 36 engines in its tractors. The total remanufactured Rigs and replaced engines during the life of the program are approximately 478 and 536, respectively. During the first nine months of 2003 the Company spent \$8.9 million on Rigs as a part of the remanufacturing program. Total capital expenditures for the first nine months of 2003 were \$11.5 million. The Company expects to spend between \$15.0 and \$20.0 million on capital expenditures during calendar year 2003 related primarily to the fleet remanufacturing program.

Other operating expenses increased from 1.3% of revenues in the third quarter of 2002 to 1.4% of revenues in the third quarter of 2003, and increased from 1.1% of revenues for the nine-month period ended September 30, 2002 to 1.3% of

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revenues for the nine-month period ended September 30, 2003. The increase was due primarily to additional expenses related to the negotiation of the new agreement with the Teamsters that were incurred mainly during the second and third quarters of 2003 and to the professional fees incurred to settle litigation during the third quarter. The settlement of this litigation is described in more detail in Part II, Item 1. Legal Proceedings.

Investment income decreased from \$0.2 million in the third quarter of 2002 to a loss of \$0.4 million in the third quarter of 2003, and increased from \$1.1 million for the nine-month period ended September 30, 2002 to \$2.9 million for the nine-month period ended September 30, 2003, which included \$1.8 million interest and dividend income, \$2.6 million realized gains and \$1.5 million unrealized losses. The net increase for the nine-month period was due to an increase in value on marketable debt and equity securities held by the Company's captive insurance company. The reduction in investment income during the third quarter of 2003 was due to a rise in interest rates that reduced the value of the Company's marketable debt securities as well as the conversion of marketable debt and equity securities to cash during July 2003.

Foreign exchange gains, net decreased from \$0.1 million in the third quarter of 2002 to a loss of \$62,000 in the third quarter of 2003, and increased from \$0.2 million for the nine-month period ended September 30, 2002 to \$2.4 million for the nine-month period ended September 30, 2003. The increase for the nine-month period was due primarily to favorable exchange rate changes related to the Company's operating subsidiary in Canada that resulted from a strengthening of the Canadian dollar in relation to the U.S. dollar, which did not continue during the third quarter of 2003. The Canadian dollar has increased in value by approximately 16%, as compared to the U.S. dollar, since the beginning of 2003.

## **Financial Condition, Liquidity and Capital Resources**

The Company's sources of liquidity are funds provided by operations and borrowings under its revolving credit facility with a syndicate of lenders. The Company's primary liquidity needs are for the payment of operating expenses, the refurbishment and maintenance of Rigs and terminal facilities, and the payment of interest and principal associated with long-term debt.

Net cash provided by operating activities totaled \$81.6 million for the nine-month period ended September 30, 2003 versus \$55.1 million for the nine-month period ended September 30, 2002. The increase in cash provided by operations was due primarily to the movement of the Company's captive insurance company's short-term investments to cash and cash equivalents in July 2003. The \$60.7 million of cash provided by this change was partly offset by reduced operating cash flows, increased funding of the Company's captive insurance company, as well as changes in working capital. During the three month period ended September 30, 2003, the Company's captive insurance company converted approximately \$60.7 million of marketable debt and equity securities to cash and cash equivalents. The change in short-term investments resulted from increased collateral requirements due to a change in insurance carriers. The Company is aggressively pursuing alternatives to resolve the collateral requirements. As a result, the investments held by the captive insurance company have been converted into cash and cash equivalents that are highly liquid, which will reduce the amount of assets necessary to secure the lines of credit. The increase in cash provided by the conversion of the short-term investments was partially offset by a decrease in cash generated from accounts receivable as compared to the prior period as well as an increase in cash used to settle accounts payable and accrued liabilities. During 2002, the Company reduced its accounts receivable outstanding with customers by \$13.8 million. As of December 31, 2001 the average days outstanding in accounts receivable were 31.2, which was reduced to 23.2 and 19.8 at December 31, 2002 and September 30, 2003 respectively.

Net cash used in investing activities totaled \$11.3 million for the nine-month period ended September 30, 2003 versus \$6.3 million for the nine-month period ended September 30, 2002. Cash paid to purchase capital items, which are related mainly to the fleet remanufacturing program, decreased by \$1.8 million while cash proceeds from the sale of assets and joint ventures decreased by \$5.4 million. The Company did not sell any significant assets in the first nine months of 2003. The Company reduced the number of Rigs remanufactured during the third quarter of 2003 primarily due to cutbacks in production levels by the OEMs. The Company will continue to evaluate the

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progression of the remanufacturing program throughout 2003. Capital expenditures for fiscal year 2003 are expected to be in the range of \$15.0 million to \$20.0 million related mainly to the fleet remanufacturing program.

Net cash provided by financing activities totaled \$2.0 million for the nine-month period ended September 30, 2003 versus net cash used in financing activities of \$34.4 million for the nine-month period ended September 30, 2002. Debt repayments were lower in 2003 due to reduced operating cash flows, increased working capital requirements, lower cash proceeds from asset sales, and the increase in funding requirements of the Company's captive insurance company.

On February 25, 2002, the Company entered into a new credit facility which includes certain term loans (the Term Loans) and a revolving credit facility. Proceeds from the Term Loans were used in February 2002 to repurchase \$40 million of senior subordinated notes for \$37.25 million. In conjunction with the extinguishment of these senior subordinated notes, the Company recognized a pre-tax gain of \$2.75 million during the first quarter of 2002.

The Company amended the facility in September 2003 (the Credit Facility and amendments thereto are collectively referred to as the Credit Facility). The Credit Facility as amended in September 2003 provides the Company with a \$90.0 million revolving credit facility (the Revolver) and a \$100 million term loan (the New Term Loan). At its inception, the Credit Facility consisted of a \$120 million revolving credit facility and four Term Loans that totaled \$82.75 million. As part of the amendment, the maturity date of the Credit Facility was extended to September 2007.

The interest rate for the Revolver is based upon the prime rate plus 1.5%, or LIBOR plus 4.5%, at management's discretion, with a minimum interest rate of 6.5%. The Credit Facility as amended provides that the New Term Loan bear interest between 8.5% and 11.5% to be determined solely on the Company's leverage as defined in the agreement. Prior to the amendment, the interest rate on the Term Loans was based solely on a spread over the prime rate. Annual commitment fees are due on the undrawn portion of the commitment.

At September 30, 2003, \$4.4 million was outstanding under the Revolver, and approximately \$24.3 million was committed under letters of credit. The Company had approximately \$58.2 million available under the Revolver as of September 30, 2003.

Borrowings under the Company's Credit Facility are secured by a first priority security interest on assets of the Company and certain of its subsidiaries, including a pledge of stock of certain subsidiaries. In addition, certain subsidiaries of the Company jointly and severally guarantee the obligations of the Company under the Credit Facility.

The Credit Facility agreement sets forth a number of affirmative, negative and financial covenants binding on the Company. The negative covenants limit the ability of the Company to, among other things, incur debt, incur liens, make investments, sell assets, or declare or pay any dividends on its capital stock. The financial covenants require the Company to maintain minimum consolidated earnings before interest, taxes, depreciation and amortization, and gains and losses on disposal of operating assets, and also include a maximum leverage ratio. The minimum consolidated EBITDA, as defined in the Credit Facility, is \$50.0 million and is tested monthly based on the prior rolling twelve-month period.

Future maturities of long-term debt are as follows at September 30, 2003 (in thousands):

October 1, 2003 to September 30, 2004	\$ 17,854
October 1, 2004 to September 30, 2005	13,500
October 1, 2005 to September 30, 2006	13,500
October 1, 2006 to September 30, 2007	13,500
October 1, 2007	195,876
	<u>          </u>
	\$254,230
	<u>          </u>

The Company has certain long-term contractual obligations, including operating lease obligations and purchase and service contract commitments that are not required to be recorded in the Company's consolidated balance sheet. The Company has no material changes to this disclosure as made in its Annual Report on Form 10-K for the year ended December 31, 2002.

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### **Quantitative and Qualitative Disclosures about Market Risk**

#### *Disclosures About Market Risks*

The market risk inherent in the Company's market risk sensitive instruments and positions is the potential loss arising from adverse changes in short-term investment prices, interest rates, fuel prices, and foreign currency exchange rates.

#### *Investments*

The Company does not use derivative financial instruments in its investment portfolio. The Company places its investments in instruments that meet high credit quality standards, as specified in the Company's investment policy guidelines. The policy also limits the amount of credit exposure to any one issue, issuer, and type of instrument.

#### *Interest Rates*

The Company primarily issues long-term debt obligations to support general corporate purposes including capital expenditures and working capital needs. The majority of the Company's long-term debt obligations bear a fixed rate of interest. A one-percentage point increase in interest rates affecting the Company's floating rate long-term debt would reduce pre-tax income by \$1.5 million over the next fiscal year. A one-percentage point change in interest rates would not have a material effect on the fair value of the Company's fixed rate long-term debt.

#### *Substantial Leverage*

The Company has consolidated indebtedness, which is substantial in relation to its stockholders' equity. As of September 30, 2003, the Company had total long-term debt of approximately \$254.2 million (excluding approximately \$121.2 million of trade payables and other accrued liabilities) and stockholders' equity of approximately \$11.3 million. In addition, the Company has additional capacity for borrowings available under its revolving credit facility, which is discussed in the Financial Condition, Liquidity and Capital Resources section of Item 2.

*Management's Discussion and Analysis of Financial Condition and Results of Operations* included in this Quarterly Report on Form 10-Q. The Company's leveraged financial position exposes it to the risk of increased interest rates, may impede its ability to obtain financing in the future for working capital, capital expenditures and general corporate purposes, and may make the Company more vulnerable to economic downturns and work stoppages, and limit its ability to withstand competitive pressures.

The Company's debt instruments contain a number of affirmative, negative, and financial covenants, which limit the ability of the Company to, among other things, incur debt, incur liens, make investments, make capital expenditures, make dividend or other distributions or enter into a merger or consolidation transaction. As of September 30, 2003, the Company was in compliance with the terms of its various debt covenants. There can be no assurance, however, that the Company will be able to comply with its debt covenants in the future or that, if it fails to do so, it will be able to obtain amendments to or waivers of such covenants on commercially reasonable terms, if at all.

The Company will need to use a large portion of its future earnings to pay principal and interest on its substantial debt obligations, which will reduce the amount of money available for use in its operations, capital reinvestment, or for responding to potential business opportunities as they arise. The ability of the Company to generate the cash necessary to service its debt is subject to a number of external factors beyond its control, and there can be no assurance that the Company will be able to generate sufficient cash through its operations to enable it to meet its obligations. If the Company does not generate enough cash to enable it to meet its debt obligations, it may be

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required to take actions such as reducing or delaying capital expenditures, selling assets, restructuring or financing its debt or seeking additional equity capital. There can be no assurance that any of these actions could be effected on commercially reasonable terms, if at all, and the terms of existing or future indebtedness may restrict the Company from adopting any of these alternatives.

Any failure of the Company to comply with the covenants contained in its debt instruments, if not waived, or to adequately service its debt obligations, could result in a default under its debt instruments. If a default occurs under any of the Company's debt instruments, the lenders thereunder may elect to declare all borrowings outstanding, together with interest and other fees, to be immediately due and payable. Borrowings under the Company's credit facility are collateralized with the assets of the Company and certain of its subsidiaries. If the Company were unable to repay any borrowing under its credit facility when due, the lenders thereunder would have the right to proceed against the collateral granted to them to secure the debt. Any default under the Company's debt instruments, particularly any default that resulted in acceleration of indebtedness or foreclosure on collateral, would have a material adverse effect on the Company.

### *Labor Matters*

Employees of the Company's subsidiary, Allied Systems, which represents approximately 70% of the Company's workforce, are represented by the International Brotherhood of Teamsters Union in the United States. A new collective bargaining agreement, which covers the Company's employees represented by the Teamsters, commenced on June 1, 2003 and will expire on May 31, 2008.

Economic provisions of the agreement include a wage freeze for the first two years of the agreement and wage increases of approximately 2% on June 1, 2005, 2% on June 1, 2006, and an additional 2.5% on June 1, 2007. The agreement provides for increases in health, welfare and pension contributions by the Company during each year of the agreement. The economic provisions of the contract will increase the Company's U.S. Teamster labor costs approximately 1.1% in year one of the agreement, 1.3% in year two, 2.5% in year three, 2.5% in year four, and 3.0% in year five of the agreement. In addition to the economic provisions, the agreement contains key changes in work-rule provisions that provide increased flexibility in the Company's operations in order to meet evolving client expectations and potentially improve the Company's ability to compete for new business.

### *Fuel Prices*

Allied Automotive Group is dependent on diesel fuel to operate its fleet of Rigs. Diesel fuel prices are subject to fluctuations due to unpredictable factors such as weather, government policies, and changes in global demand and global production. To reduce price risk caused by market fluctuations, Allied Automotive Group periodically purchases fuel in advance of consumption. As of September 30, 2003 the Company had no fuel purchase commitments outstanding. A 10% increase in diesel fuel prices would reduce pre-tax income by \$4.5 million over the next fiscal year assuming levels of fuel consumption and pricing in the remainder of 2003 is consistent with the first nine months of 2003, without taking into account any positive impact arising from fuel surcharges.

### *Competition*

The automotive transportation industry is highly competitive, as Allied Automotive Group currently competes with other motor carriers of varying sizes, as well as with railroads. Allied Automotive Group also competes with non-union motor carriers and broker operations that sub-contract carhaul transportation services to low-cost independent owner-operators. The development of new methods of hauling vehicles could also lead to competition.

The carhaul business is labor intensive for union carhaul companies. Wages and benefits represented approximately \$107.4 million of the Company's consolidated operating expenses for the quarter ended September 30, 2003. There

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has been an increase in the number of carhaul companies that utilize non-union labor, and the market share represented by such companies has increased. Carhaul companies that utilize non-union labor operate at a significant cost advantage as compared to Allied Automotive Group and other union carhaul companies due to lower labor costs, primarily as a result of lower benefit and pension costs. Non-union competitors also operate without work rules which apply to Allied Automotive Group and other union companies, which provide non-union companies with a competitive advantage. Non-union companies, which operate at a significant cost advantage to Allied Automotive Group, may be able to provide delivery services at a cost to customers that are less than the cost of Allied Automotive Group's services. Railroads, which specialize in long-haul transportation, may be able to provide delivery services at a cost to customers that are less than the long-haul delivery cost of Allied Automotive Group's services.

*Self Insurance Claims*

Each of the Company's operating subsidiaries is responsible for defining risks and securing appropriate insurance programs and coverage at cost effective rates for the Company. The Company records the insurance program premiums and the estimated cost of the uninsured portion of loss claims as insurance expense. The amount recorded for estimated loss claims is based on management's evaluation of the nature and severity of claims and actuarially determined estimates of future claim development based on historical trends. The Company formed Haul Insurance Limited in December 1995 as a captive insurance subsidiary to provide reinsurance coverage to its licensed insurance carriers for certain types of losses within retentions (as noted below), for non-self insured workers' compensation, automobile liability and general liability, as indicated above. Other coverages are provided by non-related primary and reinsurance companies.

For the period of January 1, 2003 through September 30, 2003, in the United States, AAG retains up to \$650,000 of liability for each claim for workers' compensation and up to \$500,000 of liability for automobile and general liability, including personal injury and property damage claims. In addition to the \$500,000 per occurrence deductible for automobile liability, there is a \$1.5 million aggregate deductible for those claims which exceed the \$500,000 per occurrence deductible subject to a \$1.0 million per claim limit. AAG also has a \$1.0 million interaggregate limit for losses from \$1.0 million to \$2.0 million, and an additional \$3.0 million aggregate limit for losses from \$2.0 million to \$5.0 million. AAG also retains up to \$250,000 of liability for each cargo damage claim and physical damage claim to its owned and leased automobiles and tractor trailer units. In Canada, AAG retains up to CDN \$500,000 of liability for each claim for personal injury, property damage or cargo damage. Also, in Canada, there is a CDN \$500,000 aggregate limit for losses above CDN \$500,000.

Effective October 1, 2003, AAG changed its retention limits for automobile claims. The \$3.0 million aggregate limit for losses exceeding \$2.0 million will increase to \$4.0 million. These new retention limits are in place for the fourth quarter 2003. Effective January 1, 2004, AAG will retain up to \$1.0 million of liability for automobile claims. In addition to the \$1.0 million deductible, there will be a \$7.0 million aggregate deductible for those claims which exceed \$1.0 million.

If Allied Automotive Group were to experience a material increase in the frequency or severity of accidents, workers' compensation claims, stolen equipment or other loss events or unfavorable developments in existing claims over those anticipated, the Company's operating results could be adversely affected. The insurance market is contracting and it is becoming increasingly more difficult to obtain insurance coverage. While the Company currently has insurance coverage, there can be no assurance that the Company will be able to obtain insurance coverage in the future.

*Dependence on Major Customers*

Allied Automotive Group's business is highly dependent upon General Motors, Ford, DaimlerChrysler, Toyota and Honda, its largest customers. The Company operates under written contracts with General Motors, UPS Autogistics, Inc. on behalf of Ford, DaimlerChrysler, Toyota and Honda. The contracts with UPS Autogistics, DaimlerChrysler and Toyota can be terminated by location for any reason or no reason based on 60 to 150 days

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notice. Although Allied Automotive Group believes that its relationships with these customers is mutually satisfactory, there can be no assurance that these relationships will not be terminated in whole or in part in the future. Furthermore, automotive manufacturers are relying increasingly on fourth party logistics companies and re-engineering vehicle delivery practices, which could result in a reduction of services provided by the Company for some or all of its major customers. A significant reduction in the production levels, plant closings or the imposition of vendor price reductions by these manufacturers, or the loss of General Motors, UPS Autogistics, DaimlerChrysler, Toyota or Honda as a customer, or a significant reduction in the services provided for any of these customers by Allied Automotive Group would have a material adverse effect upon the Company. General Motors, DaimlerChrysler and Ford, in particular, have publicly announced plans to significantly reduce vendor costs including those costs associated with logistics services.

### *Foreign Currency Exchange Rates*

Although the majority of the Company's operations are in the United States, the Company does have foreign subsidiaries (primarily Canada). The net investment in foreign subsidiaries translated into dollars using month-end exchange rates at September 30, 2003 is \$75.4 million. The potential loss in fair value impacting other comprehensive income resulting from a hypothetical 10% change in quoted foreign currency exchange rates amounts to \$7.5 million. At September 30, 2003 a payable balance of \$14.2 million related to intercompany transactions was outstanding on the Company's Canadian subsidiary. The potential loss from a hypothetical 10% change in quoted foreign currency exchange rates related to this balance amounts to \$1.4 million as of September 30, 2003. The Company does not use derivative financial instruments to hedge its exposure to changes in foreign currency exchange rates.

### *Revenue Variability*

The Company's revenues are variable and can be impacted by sudden unexpected changes in OEM production levels. In addition, the Company's revenues are seasonal, with the second and fourth quarters generally experiencing higher revenues than the first and third quarters. The volume of vehicles shipped during the second and fourth quarters is generally higher due to the introduction of new models, which are shipped to dealers during those periods and the higher spring and early summer sales of automobiles and light trucks. During the first and third quarters, vehicle shipments typically decline due to lower sales volume during those periods and scheduled plant shut downs. Except for the impact of rising fuel costs discussed herein, inflation has not significantly affected the Company's results of operations. Automobile manufacturers have made production cutbacks during 2003. As a result, the Company may experience a decline in vehicle deliveries during the fourth quarter.

### *Dependence on Automotive Industry*

The automotive transportation industry is dependent upon the volume of new automobiles and light trucks manufactured, imported and sold. The automotive industry is highly cyclical, and the demand for new automobiles and light trucks is directly affected by such external factors as general economic conditions in the United States, unemployment, consumer confidence, federal policies, the possibility of war, terrorist activities, and the availability of affordable new car financing. As a result, the Company's results of operations are adversely affected by cyclical downturns in the general economy or in the automotive industry and by consumer preferences in purchasing new automobiles, SUVs, and light trucks. Inventories of new vehicles in the second quarter of 2003 were significantly higher than the 2002 levels and sales of new vehicles in the second quarter of 2003 were lower than the 2002 levels. As a result, automotive manufacturers reduced new vehicle production in the third quarter of 2003 as compared to the third quarter of 2002. A significant decline in the volume of automobiles, SUVs, and light trucks manufactured as well as sold in North America, or a material change in the overall mix of vehicles manufactured, could similarly have a material adverse effect on the Company.

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### *Contractual Obligations*

The Company has certain long-term contractual obligations, including operating lease obligations and purchase and service contract commitments that are not required to be recorded in the Company's consolidated balance sheet. The Company has no material changes to this disclosure as made in its Annual Report on Form 10-K for the year ended December 31, 2002.

### *Dependence on Key Personnel*

The success of the Company is dependent upon its senior management team, as well as its ability to attract and retain qualified personnel. The Company's credit facility provides that the facility may be terminated in the event Hugh E. Sawyer ceases to be involved in the day-to-day operation of the Company, unless a successor reasonably acceptable to the lenders is appointed within 90 days of his cessation of involvement with the Company. There is no assurance that the Company will be able to retain its existing senior management or to attract additional qualified personnel.

### **Critical Accounting Policies**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make decisions based upon estimates, assumptions, and factors it considers as relevant to the circumstances. Such decisions include the selection of applicable accounting principles and the use of judgment in their application, the results of which impact reported amounts and disclosures. Changes in future economic conditions or other business circumstances may affect the outcomes of management's estimates and assumptions. Accordingly, actual results could differ from those anticipated.

The Company's critical accounting policies include the following:

**CLAIMS AND INSURANCE RESERVES** Reserves for self-insured workers' compensation, automobile, and general liability losses are subject to management's evaluation of the nature and severity of claims and actuarially determined estimates of future claims development based on historical trends adjusted for current industry trends. The Company receives third-party actuarial valuations to assist in the determination of its claims and insurance reserves. The actuarial estimates for self-insured workers' compensation and automobile liability are discounted using management's estimate of weighted risk free interest rates for each claim year to their present values. The claims and insurance reserves are adjusted periodically as such claims mature to reflect changes in actuarial estimates based on actual experience.

**ACCOUNTS RECEIVABLE VALUATION RESERVES** Substantially all revenue is derived from transporting new automobiles and light trucks from manufacturing plants, ports, auctions, and railway distribution points to automobile dealerships. Revenue is recorded when the vehicles are delivered to the dealerships. The Company makes significant estimates to determine the collectibility of its accounts receivable on the balance sheet. Estimates include assessments of the potential for customer billing adjustments based on the timing of delivery, the accuracy of pricing, as well as evaluation of the historical aging of customer accounts. In addition, estimates include periodic evaluations of the credit worthiness of customers including the impact of market and economic conditions on their viability to satisfy amounts owed to the Company.

**ACCOUNTING FOR INCOME TAXES** As part of the process of preparing the Company's consolidated financial statements the Company is required to estimate income taxes in each of the jurisdictions in which the Company operates. This process involves estimating actual current tax exposure, together with assessing temporary differences resulting from differing treatment of items, such as depreciation expense, for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included within the Company's consolidated balance sheet. The Company must then assess the likelihood that the deferred tax assets will be recovered from future taxable income and to the extent the Company believes that recovery is not likely, the Company must establish a valuation allowance. To the extent the Company establishes a valuation allowance or increases this allowance in a period, the Company must include an expense within the tax provision in the statements of operations.



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Significant management judgment is required in determining the Company's provision for income taxes, deferred tax assets and liabilities and any valuation allowance recorded against the net deferred tax assets. The net deferred tax asset as of September 30, 2003 was \$12.7 million net of a valuation allowance of \$7.1 million. The Company has recorded a valuation allowance of \$7.1 million as of September 30, 2003 due to uncertainties related to the Company's ability to utilize some of the deferred tax assets, primarily consisting of certain capital losses carried forward and foreign tax credits, before they expire. The valuation allowance is based on management's estimate of taxable income by jurisdiction in which the Company operates and the period over which the deferred tax assets will be recoverable. In the event that actual results differ from these estimates or the Company adjusts these estimates in future periods, the Company may need to establish an additional valuation allowance, which could materially impact the financial position and results of operations.

**PROPERTY AND EQUIPMENT** The Company operates approximately 3,800 company-owned Rigs, revenue equipment, in connection with its business. Property and equipment, including revenue equipment, are stated at cost and depreciated using the straight-line method over the estimated useful life down to estimated salvage value. The actual life, if different than estimated, could have an impact on depreciation expense in the Company's consolidated statements of operations.

**GOODWILL** Pursuant to SFAS 142, goodwill is evaluated annually for impairment, or on an interim basis if an event occurs or circumstances change that would reduce the fair value of goodwill below its carrying value. The fair value of goodwill is derived by using a discounted cash flow analysis. This analysis involves estimates and assumptions by management regarding future revenue streams and expenses. Changes to these assumptions and estimates could have a material effect on the carrying value of goodwill and result in an impairment charge in the Company's consolidated statements of operations. During 2003 the Company's goodwill increased by approximately \$3.8 million. The increase was due primarily to favorable exchange rate changes related to the Company's operating subsidiary in Canada that resulted from a strengthening of the Canadian dollar in relation to the U.S. dollar that continued during the third quarter of 2003. The Canadian dollar increased in value by approximately 16%, as compared to the U.S. dollar since the beginning of 2003.

**CAUTIONARY NOTICE REGARDING FORWARD-LOOKING STATEMENTS** This Quarterly Report on Form 10-Q contains, and from time to time the Company and its officers, directors, or employees may make other forward-looking statements, including statements regarding, among other items, (i) the Company's strategy, intentions or expectations, (ii) general industry trends, competitive conditions and customer preferences, (iii) the Company's management information systems, (iv) the Company's remanufacturing program and the disposal of certain tractor or trailers, (v) the Company's efforts to reduce costs, (vi) the adequacy of the Company's sources of cash to finance its current and future operations, (vii) the effects of the new Teamster agreements in the U.S. and in Canada, (viii) the capital expenditures of the Company in 2003, (ix) the ability of the Company to comply with the financial covenants set forth in the Credit Facility, and (x) resolution of litigation and renegotiation of split-dollar life insurance agreements without material adverse effect on the Company. This notice is intended to take advantage of the "safe harbor" provided by the Private Securities Litigation Reform Act of 1995 with respect to such forward-looking statements. Without limiting the generality of the foregoing, the words "believe," "anticipate," "seek," "expect," "estimate," "intend," "plan," and similar expressions are used to identify such forward-looking statements. These forward-looking statements involve a number of risks and uncertainties. Among others, factors that could cause actual results to differ materially from historical results or results expressed or implied by such forward-looking statements are the following: economic recessions or downturns in new vehicle production or sales; war in the Middle East; increases in the cost and availability of fuel; the highly competitive nature of the automotive distribution industry; price competition with non-union carriers; dependence on the automotive industry; loss or reduction of revenues generated by the Company's major customers or the loss of any such customers; the variability of OEM production and seasonality of the automotive distribution industry; potential plant closings by the OEMs; the Company's highly leveraged financial position; labor disputes involving the Company or its significant customers; the dependence on key personnel who have been hired or retained by the Company; the availability of strategic acquisitions or joint venture partners; increased frequency and severity of

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work related accidents and workers' compensation claims; availability of appropriate insurance coverages; increased expenses due to layoffs of employees; changes in regulatory requirements which are applicable to the Company's business; changes in vehicle sizes and weights which may adversely impact vehicle deliveries per load; risks associated with doing business in foreign countries; and other risk factors set forth from time to time in the Company's Securities and Exchange Commission reports, including but not limited to, this Quarterly Report on Form 10-Q and the Company's Annual Report on Form 10-K for the year ended December 31, 2002. Many of these factors are beyond the Company's ability to control or predict, and readers are cautioned not to put undue reliance on such forward-looking statements. The Company disclaims any obligation to update or review any forward-looking statements contained in this Quarterly Report or in any statement referencing the risk factors and other cautionary statements set forth in this Quarterly Report.

### **Item 3. Quantitative and Qualitative Disclosures About Market Risk**

The information required under this item is provided under the caption "Disclosures about Market Risks" under Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

### **Item 4. Controls and Procedures**

(a) Evaluation of Disclosure Controls and Procedures.

The Company maintains a system of disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) designed to provide reasonable assurance as to the reliability of the financial statements and other disclosures included in this report, as well as to safeguard assets from unauthorized use or disposition. The Company's Chief Executive Officer and Chief Financial Officer evaluated the effectiveness of the Company's disclosure controls as of the end of the period covered by this Form 10-Q. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective in alerting them in a timely manner of material information required to be included in the Company's periodic Securities and Exchange Commission filings.

(b) Changes in Internal Control Over Financial Reporting.

No changes were made to the Company's internal control over financial reporting during the Company's most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## **PART II OTHER INFORMATION**

### **Item 1. Legal Proceedings**

The Company is involved in various litigation and environmental matters relating to employment practices, damages, and other matters arising from operations in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's financial position or results of operations.

Since its last quarterly filing, Allied has settled all outstanding litigation with Ryder System, Inc., which litigation was previously disclosed in company filings. The litigation arose in connection with the acquisition by the Company of Ryder Automotive Carrier Services, Inc. and RC Management Corp. from Ryder System, Inc. in September 1997, and consisted of three actions. In *Ryder Systems, Inc. v. Allied Holdings, Inc., AH Acquisition Corp. and Allied Automotive Group* (the "Ryder Action"), Ryder alleged that the Company failed to substitute itself for Ryder under an insurance policy covering third-party claims and with various state agencies

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that regulate matters such as self-insured workers' compensation. Ryder also alleged that the Company was obligated to take certain steps to transfer from Ryder to itself the ownership and administrative responsibility for two pension plans. The other two actions, *Gateway Development & Manufacturing, Inc. v. Commercial Carriers, Inc., et al.* and *Commercial Carriers, Inc. v. Gateway Development & Manufacturing, Inc., et al.* (collectively the Gateway/CCI Actions), both centered around the contention that the Company breached legal duties with respect to a failed business transaction involving Gateway Development, Ryder Truck Rental, Inc., and Ryder System.

Under terms of the settlement agreement, Ryder System has paid the Company approximately \$1.4 million, and Ryder's insurance carrier has paid the Company approximately \$1.6 million. The payment from Ryder represents the settlement of various claims and disputes that have arisen since the 1997 acquisition. The payment from Ryder's insurance carrier represents a reimbursement for amounts paid by the Company in excess of the self-insured retention for workers' compensation and automobile liability claims assumed in the acquisition of Ryder's Automotive Carrier Group. The Company and Ryder System have agreed to dismiss all litigation each party had brought against the other as part of the settlement, which has resulted in the complete dismissal of the Ryder Action. Except with respect to expenses already incurred, Ryder has agreed to indemnify Allied for all costs, including legal fees and any potential judgment against Allied, arising out of the Gateway/CCI Actions. Therefore, although the Gateway/CCI Actions remain pending, the settlement will provide Allied with indemnification from Ryder System as to exposure to future legal fees or any potential judgment against the Company.

As part of the settlement agreement, the Company has issued a letter of credit for \$3.5 million in favor of Ryder System and has agreed to increase the letter of credit by \$1 million each quarter starting in the fourth quarter 2003 through the third quarter of 2005. The letter of credit may only be drawn by Ryder System if the Company fails to pay workers' compensation and liability claims assumed by the Company in the Ryder Automotive Carrier Group acquisition. The Company has provided the letter of credit in favor of Ryder System because Ryder has issued a letter of credit to its insurance carrier relating to the workers' compensation and liability claims assumed by the Company. By September 30, 2005, and periodically thereafter, an actuarial valuation will be made to determine the remaining outstanding amount of workers' compensation and liability claims assumed by Allied, and the letter of credit issued by the Company in favor of Ryder System will be adjusted accordingly.

**Item 6. Exhibits and Reports on Form 8-K:**

**(a) Exhibit Index**

Exhibit No.	Description
31.1	Rule 13a-14(a)/15d-14(a) Certification by Hugh E. Sawyer.
31.2	Rule 13a-14(a)/15d-14(a) Certification by Daniel H. Popky.
32.1	Section 1350 Certification by Hugh E. Sawyer.
32.2	Section 1350 Certification by Daniel H. Popky.

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**(b) Reports on Form 8-K**

On July 5, 2003, Allied Holdings, Inc. filed with the Commission a Current Report on Form 8-K attaching a press release issued by it on July 30, 2003.

On September 5, 2003, Allied Holdings, Inc. filed with the Commission a Current Report on Form 8-K announcing the completion of an amendment to its senior credit facility and attaching a press release related thereto and the amended senior credit facility.

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**EXHIBIT INDEX**

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