SOUTHERN ENERGY HOMES, INC.
Annual Report to Shareholders
January 2, 2004

Southern Energy Homes, Inc. is not an SEC reporting company.
Please see the cautionary discussion on page 3, "An Important Note About this Report."

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FORWARD LOOKING STATEMENTS: This Annual Report includes forward looking statements. Investors are cautioned that such statements inherently involve risks and uncertainties which could cause actual results to differ materially from those in any forward looking statements, including without limitation: availability of financing for prospective purchasers of the Company's homes and availability of floor plan financing for dealers; availability and pricing of raw materials; the ultimate financial and operational effects of new plant investment being undertaken and discontinued operations; general economic conditions; the cyclical and seasonal nature of housing markets; competitive pricing pressures at both the wholesale and retail levels; changes in market demand; the impact of cost reduction programs and other management initiatives; the Company's contingent repurchase liabilities with respect to dealer financing and retail buyer financing; the adequacy of accruals for workers' compensation claims and insurance costs; concentration of the Company's business in certain regional markets; adverse weather conditions that reduce retail sales; the possibility of plant shutdowns from weather or other causes; availability of labor for the Company to meet operating requirements; the highly competitive nature of the manufactured housing industry; federal, state and local regulation of the Company's business; the Company's reliance on independent dealers; and other risks indicated from time to time in the Company's quarterly and annual reports to its shareholders and other public statements. Southern Energy Homes is not responsible for updating the information contained in this annual report beyond the published date.

Southern Energy Homes, Inc. is not an SEC reporting company.
Please see the cautionary discussion on page 3, "An Important Note About this Report."

An Important Note About This Report

Effective as of January 15, 2004, Southern Energy Homes, Inc. no longer has a class of securities registered pursuant to Section 12 of the Securities Exchange Act of 1934 (the "Act"), and the Company is no longer subject to the reporting requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934. Accordingly, this Annual Report is *not* filed with the Securities and Exchange Commission, is not available on the SEC's EDGAR system, and it does *not* purport to meet the requirements for companies that are subject to the Act's reporting requirements. The Company does intend in this Annual Report and other reports to provide accurate, high quality financial and other information that is in many ways consistent with the kind of information it has provided in the past, but shareholders and other interested persons are ***cautioned*** that this information is not and cannot be deemed the substantial equivalent of the information required of reporting companies under the Act.

This Annual Report and other periodic reports to shareholders are available on the Company's website, www.SEhomes.com , and at www.pinksheets.com. Interested persons may also request copies directly from the Company; please direct requests and inquiries to Chief Financial Officer, Southern Energy Homes, Inc., 144 Corporate Way, Addison, Alabama 35540, telephone (256) 747-8589.

Business

General

Southern Energy Homes, Inc. (the "Company") is engaged in the production and sale of manufactured homes, and the operation of three component supply divisions. The Company produces manufactured homes sold primarily in the southeastern and south central United States. The Company operates five home manufacturing facilities (four in Alabama and one in Texas) to produce homes sold in 18 states. The Company's homes are currently marketed under four brand names by 223 independent dealers at 531 independent dealer locations and 2 company-owned retail centers.

The Company manufactures homes that are designed as primary residences ready for immediate occupancy. The homes, most of which are customized at the Company's factories to the home buyer's specifications, are constructed by the Company in one or more sections and transported by independent trucking companies to dealer locations.

The Company's homes range in size from 672 to 3,268 square feet and sell at retail prices ranging from $20,000 to $108,000, excluding land. The Company believes that its willingness to customize floor plans and design features to match homebuyer preferences is the principal factor which differentiates it from most of its competitors.

At the end of fiscal 1998, the Company had substantial retail sales operations, consisting of 33 retail centers in seven states. As industry conditions began to weaken during fiscal 1999, however, the Company responded, among other ways, by closing or selling retail centers that did not meet profit objectives. That process continued through the next three years, culminating in the decision during fiscal 2002 to close most of the remaining retail centers and focus on the Company's core manufacturing business. In fiscal 2002, eleven retail centers were closed, and by the end of 2003, the Company had closed all but two of the retail centers that were formerly part of its retail segment. These retail centers had been negatively affected by weak market conditions, including excess retail capacity in the industry and restrictive retail financing conditions, principally as a result of the withdrawal of several lenders from the market (see "Discontinued Operations" below). The decision to close the retail centers was based primarily on management's evaluation of recent operating results and future prospects.

The component supply segment sells various supply products to the Company's manufacturing segment and to third-party customers.

The manufactured housing market is highly cyclical and seasonal and is affected by the same economic

factors which have an impact on the broader housing market. Historically, most sectors of the home building industry have been affected by, among other things, changes in general economic conditions, levels of consumer confidence, employment and income, housing demand, availability of financing and interest rate levels.

Continuing Operations

Manufactured Homes - Industry Overview

A manufactured home is a single-family house that is constructed in accordance with HUD construction and safety standards or to local building code entirely in a factory environment rather than at the home site. There are two basic categories of manufactured housing: single-section and multi-section. The manufactured housing industry grew significantly from 1991 to 1998, but has retrenched since then. According to the Manufactured Housing Institute (MHI), domestic shipments increased from 170,713 homes in calendar 1991 to 372,843 homes in calendar 1998, before declining to 130,937 in calendar 2003 We believe that the growth during the 1990s resulted from the increased availability of financing and also in large part from increasing consumer acceptance of and preference for manufactured housing.

Today's manufactured homes offer customers quality similar to many site-built homes at a more affordable price. Manufactured homes are constructed in a factory environment, utilizing assembly line techniques, which allows for volume purchases of materials and components and more efficient use of labor. The quality of manufactured homes has increased significantly over the past 20 years, as producers generally build with the same materials as site-built homes. In addition, many features associated with site-built homes are included in manufactured homes, such as central heating, name brand appliances, carpeting, cabinets, walk-in closets, vaulted ceilings, wall coverings and porches. Also, optional features include such amenities as fireplaces, wet bars and spa tubs, as well as retailer-installed options such as central air conditioning, garages and furniture packages.

As acceptance of manufactured housing has increased among higher-income buyers and financing for single-section homes has become more scarce, demand has shifted toward larger, multi-section homes, which accounted for 80% of industry shipments in calendar 2003, up from 47 percent in calendar 1991 according to MHI data.

The manufactured housing industry is cyclical, and is affected by general economic conditions and consumer confidence. For the last five years, the industry has been burdened by excess manufacturing and retailing capacity, high retailer inventories, competition from repossessed units being resold at greatly distressed prices and a slowing of retail sales. This imbalance between capacity and inventories on one hand and retail demand on the other has largely been caused by the reversal of lenient credit practices, which artificially stimulated demand during most of the 1990s, until they were replaced by the current more restrictive lending criteria for manufactured home buyers. Rapid overexpansion of retail distribution networks and retailers' optimistic expectations of future business prospects also contributed to the imbalance throughout the 1990's.

With respect to the retail financing of manufactured housing, interest rates are generally higher and the terms of loans shorter than for site-built homes. In addition, some lenders have stopped extending loans to finance the purchase of manufactured homes, including three national lenders that exited the business since the last half of fiscal 2002. This has had the effect of making financing for manufactured homes even more expensive and more difficult to obtain relative to financing for site-built homes.

Retail financing was a significant factor in the expansion of the industry, particularly toward the latter part of the 1990s growth cycle, when competitive retail lenders employed relatively liberal underwriting standards to capture more business. Although these liberal underwriting practices were a major catalyst in fueling higher sales volume through 1998, the number of sub-standard consumer loans originated during this time frame gave rise to an abnormally high rate of defaults and repossessions as loan portfolios have matured in the last four calendar years. In turn, retail lenders have responded by sharply curtailing the availability of financing to retail customers and elevating underwriting standards to more restrictive levels. At the same time, manufacturers have found themselves competing for the sale of new homes with resellers of these repossessed homes. Due to the difficult financing environment for chattel financing nationwide, the industry has been trending toward more "land and home" type

financing. Chattel financing is personal property financing secured only by the home and not by the underlying land on which the home is sited. On the other hand, "land and home" financing is real property financing secured by the home and by the underlying land on which the home is sited.

Industry manufacturing and retail capacity have been significantly reduced since 2000 in response to the financing environment and the related inventory imbalance. More than half of the retail lending capacity available in 2000 has exited the business and has not been replaced by other significant sources. We expect that weak market conditions will continue until the availability of financing improves. However, the recent announcement in February 2004 in the Wall Street Journal that Fannie Mae and eight lender partners, including Washington Mutual Inc. and General Motors Corp.'s GMAC unit, will provide low-cost financing for manufactured homes requiring down payments as low as five percent of the home price is expected to enhance demand.

Manufactured Homes - Our Operations

The Company produces a variety of single- and multi-section homes under four brand names. The homes are manufactured in sections that are transported to their destination and the finished homes may consist of one or more sections. Multi-section products are joined at the destination by the dealer or its contractor. The Company initially concentrated on the medium to higher priced segments of the manufactured housing market. Over the past several years, the product line has been broadened to include lower priced homes that sell at retail for less than $25,000. Although each manufacturing facility is an operating segment, they are aggregated into one segment for reporting purposes because they produce similar products using similar production techniques and they sell their products to the same class of customer. In addition, they are subject to the same regulatory environment and the economic characteristics (measured in terms of profitability) are similar. The four manufacturing divisions of the Company are listed below with the type, size, and retail price of the homes that each currently produces:

Division	Type	Square Feet	Retail Price Range
Southern Energy	Multi-section	1,421 - 3,268	$38,900 - $108,000
Southern Estates	Single and multi-section	1 ,216 - 2,432	30,000 - 70,000
Southern Homes	Single and multi-section	672 - 2,450	20,000 - 65,000
Southern Texas	Single and multi-section	688 - 2,432	20,000 - 65,000

The Company’s manufacturing division accounted for 94.2%, 91.1% and 89.3% of the Company’s net revenues for the fiscal years ended January 2, 2004, January 3, 2003 and December 28, 2001, respectively.

The Company held a 4.0% share of the single-section manufactured housing market in calendar 2003, up from 3.6% in 2002, as measured by shipments to retailers reported by the Manufactured Housing Institute. Single-section shipments represented 29.1% of our manufactured housing unit shipment in fiscal 2003 versus 31.4 % in 2002 and 32.3% in 2001. Our single-section homes are designed for the affordable housing market, which includes first-time, retiree and value-oriented buyers. We held a 2.4% share of the multi-section manufactured housing market in calendar 2003, up from 2.2% in 2002, as measured by shipments to retailers reported by the Manufactured Housing Institute. Multi-section shipments represented approximately 70.9% of our manufactured housing unit shipments in fiscal 2003, versus 68.6% in 2002 and 67.7% in 2001.

The Company’s product development and engineering personnel design homes in consultation with divisional management, sales representatives and dealers. They also evaluate new materials and construction techniques in a continuous program of product development and enhancement. With the use of computer aided design technology, the Company has developed engineering systems that permit customization of homes to meet the individual needs of prospective buyers. These systems allow the Company to make modifications such as increasing the length of a living room, moving a partition, changing the size and location of a window or installing custom cabinets without significant impact upon manufacturing productivity.

Each home contains two to five bedrooms, a living room, dining room, kitchen and one to three bathrooms, and features a heating system, a stove and oven, refrigerator, carpeting and draperies. The Company has traditionally focused on designing manufactured homes with features that make them comparable to site-built homes, including stone fireplaces and vaulted ceilings, thus broadening the base of potential customers. In addition

to offering the consumer optional features such as finished sheet rock, dishwashers, oak cabinets and furniture packages as well as a wide range of colors, moldings and finishes, the Company generally offers extensive customization of floor plan designs to meet specific customer preferences.

Retail - Industry Overview

The manufactured housing retail industry is highly fragmented, with approximately 4,500 retail sales centers. Most manufactured housing retailers are independently owned private companies operating a single sales center. Until 1997, the Company and most other manufacturers, with the exception of a few vertically integrated entities, marketed their manufactured homes exclusively through independent retailers. At that time, however, certain manufactured housing producers began to acquire retailers with the objective of exercising greater control over retail distribution and upgrading marketing and merchandising practices, including brand name development. Additionally, some financial consolidators and residential developers entered the manufactured housing business by acquiring retailers.

One factor leading to the industry imbalance between retail inventories and consumer demand has been the large number of retailers, each of which must maintain adequate inventory at its location to appeal to potential customers. Although the number of retail stores in the industry has decreased significantly, we anticipate that a further reduction will likely be necessary to help restore balance between the level of overall retailer inventories and the level of consumer demand for which financing is available.

Retail - Our Operations

The Company began its retail operations in November 1996 by acquiring a group of retail companies operating in Alabama and Mississippi. During fiscal 1997, the Company expanded its retail operations by acquiring another retail company with seven locations in South Carolina, and during 1998, the Company added another 15 retail centers through acquisitions. However, beginning in fiscal 1999, the industry began to weaken and in 2000 the Company began to close unprofitable retail centers. During the latter part of fiscal 2002, the Company made the decision to close most of its remaining retail centers, and completed the closure of eleven centers by the end of December 2002. At January 2, 2004, the Company had 2 retail sales centers in Alabama. Each of the remaining two sales centers maintains a separate sales force. The Company's two continuing retail centers accounted for 3%, 7% and 8% of the Company's net revenues for the fiscal years ended January 2, 2004, January 3, 2003 and December 28, 2001, respectively (also see "Discontinued Operations" below).

Component Supply

The Company presently operates three component supply divisions. Classic Panel Designs supplies laminated and other interior wall panels. Wind-Mar Supply provides windows, doors and countertops. Trimmasters produces wood molding and trim finishing, and is a provider of wood components and dining furniture. These divisions sell products both to the Company's own manufactured housing segment and to third-party customers. The Company's component supply division accounted for 3%, 2% and 2% of the Company's net revenues for the fiscal years ended January 2, 2004, January 3, 2003 and December 28, 2001, respectively.

Home Manufacturing Operations

The Company's homes are currently manufactured by four operating divisions using assembly line techniques at five facilities; two manufacturing facilities are located in Addison, Alabama, and one is located in each of Double Springs, Alabama, Lynn, Alabama and Fort Worth, Texas.

The Company's manufacturing facilities operate on a one shift per day, five days per week basis. The Company believes that these facilities have the capacity to produce a total of approximately 225 floor sections per week with minimal labor additions. The Company plans to continue operating on a single shift per day basis. During the fiscal year ended January 2, 2004, the Company produced an average of 122 floor sections per week. This represented a 12% decrease in floor section production from an average of 138 floor sections per week in the fiscal year ended January 3, 2003. In the fiscal year ended December 28, 2001, the Company produced an average

of 147 floor sections per week. The following table sets forth the total floor sections and homes sold as well as the number of home manufacturing facilities operated by the Company for the periods indicated:

	Fiscal Year Ended		
	January 2, 2004	January 3, 2003	December 28, 2001
Homes	3,606	4,203	4,411
Floor sections	6,347	7,334	7,620
Home Manufacturing facilities	5	5	5

Each division operates as a separate strategic unit that is directed by a general manager and has its own sales force. The general manager, production managers and supervisory personnel of each division have an incentive compensation system which is directly tied to the operating profit of the division. In addition, production personnel of each division have a productivity, turnover, labor efficiency and injury incentive compensation system. The Company believes that these compensation systems help to focus efforts on curtailing waste and inefficiencies in the production process, keep qualified associates and maintain a safe workplace, and represent a divergence from standard industry practices, which are typically designed to reward personnel on production volume criteria.

The extent of customization of the home performed by the Company varies to a significant degree with the price of the home. In the higher price range of the market, the home buyer is often less sensitive to the price increase that is associated with significant design modifications that might be desired. However, the Company's experience in producing a customized home on a cost-effective basis has allowed the Company to offer customized homes in all price ranges.

The principal materials used in the production of the Company's homes include steel, aluminum, wood products, gypsum wallboard, fiberglass, insulation, carpet, vinyl floor covering, fasteners and hardware items, appliances, electrical items, windows and doors. These materials and components are readily available and are purchased by the Company from numerous sources. No supplier accounted for more than 4% of the Company's purchases during each of the past three fiscal years. The Company believes that the size of its purchases allows it to obtain favorable volume discounts. The Company's expenses can be significantly affected by the availability and pricing of raw materials. Sudden increases in demand for construction materials can greatly increase the costs of materials. While in the past the Company has been able to pass along a significant portion of increased material costs, more recently the Company has had difficulties in passing on the increased costs due to competitive conditions.

Because the cost of transporting a manufactured home is significant, substantially all of the Company's homes are sold to dealers within a 600 mile radius of a manufacturing facility. The Company arranges, at the dealer's expense, for the transportation of finished homes to dealer locations using independent trucking companies. Customary sales terms are cash-on-delivery or guaranteed payment from a floor plan financing source. Dealers or other independent installers are responsible for placing the home on site, making utility hook-ups and providing and installing certain trim items.

Substantially all production is initiated against specific orders. The Company's backlog of orders for manufactured homes as of March 1, 2004 was $0.9 million as compared with $0.7 million at March 1, 2003. Dealer orders are subject to cancellation prior to commencement of production for a variety of reasons, and the Company does not consider its backlog to be firm orders. In addition, because the industry operates in an environment where order lead times are extremely short, the Company does not view backlog at any point in time to be indicative of the level of the Company's future revenues.

Sales Network

At January 2, 2004, the Company sold manufactured homes through approximately 233 independent dealers at approximately 531 independent dealer locations and through 2 company-owned retail centers in 18 states, principally in the southeastern and south-central United States.

Each of the Company's four home manufacturing divisions maintains a separate sales force. At January 2, 2004, a total of 23 salespersons maintained personal contact with the Company's independent dealers. The Company markets its homes through product promotions tailored to specific dealer needs. In addition, the Company advertises in local media and participates in regional manufactured housing shows.

The Company strives to achieve solid working relationships with its independent dealers, because we believe this is an important factor in the effective distribution of our products. In order to promote dealer loyalty and to assist dealers in penetrating retail markets, only one independent dealer within a given local market may distribute homes manufactured by a division of the Company. The Company does not have exclusive marketing agreements with its independent dealers. The Company believes its relations with its independent dealers are good and the Company has experienced relatively low turnover in its established independent dealers in the past three years.

The following table shows the percentage of net revenues accounted for by the largest single dealer and the ten largest dealers for each of the past three fiscal years:

	Percentage of Net Revenues		
	Fiscal year ended January 2, 2004	Fiscal year ended January 3, 2003	Fiscal year ended December 28, 2001
Largest dealer	6.5 %	3.8 %	5.3 %
Ten largest dealers	33.8 %	31.3 %	26.7 %

Buyers of manufactured homes typically shop at a number of retail locations prior to purchasing a home. The Company believes that it provides most of its dealers with a marketing advantage because of the dealer's ability to represent that our homes can be customized to meet the individual preferences of the customer.

Warranty, Quality Control and Service

The Company endeavors to adhere to strict quality standards and continuously refines its production procedures. In addition, in accordance with the construction codes promulgated by the Department of Housing and Urban Development ("HUD"), an independent HUD-approved, third-party inspector inspects each manufactured home for compliance during construction at our manufacturing facilities. See "Regulation."

The Company provides initial home buyers with a HUD-mandated, one-year limited warranty against manufacturing defects in the home's construction. In addition, there are often direct warranties that are provided by the manufacturers of components and appliances.

The Company has experienced quality assurance personnel at each of its manufacturing facilities to provide on-site service to dealers and home buyers. The Company continuously works to enhance its quality assurance systems, placing high emphasis on improving the value and appeal of the Company's homes and reducing consumer warranty claims.

Independent Dealer Financing

Substantially all of the Company's independent dealers finance their purchases through "floor plan" arrangements under which a financial institution provides the dealer with a loan for the purchase price of the home and maintains a security interest in the home as collateral. In connection with a floor plan arrangement, the financial institution which provides the independent dealer financing customarily requires the Company to enter into a separate repurchase agreement with the financial institution, under which the Company is obligated, upon default by the independent dealer, to repurchase the home at the Company's original invoice price less cost of all damaged/missing items and less curtailments, plus certain administrative and shipping expenses. Repurchases were $1.5 million, $2.0 million and $4.2 million for the years ended 2003, 2002, and 2001 respectively. Losses on homes

repurchased under these agreements were $0.3 million, $0.5 million and $0.9 million in 2003, 2002 and 2001, respectively. At January 2, 2004, the Company's contingent repurchase liability under floor plan financing arrangements through independent dealers was approximately $39.2 million. At January 2, 2004 the Company had accrued reserves of $0.3 million for potential losses on repurchases; actual losses may differ from the Company's estimates. While homes that have been repurchased by the Company under floor-plan financing arrangements are usually sold to other dealers, no assurance can be given that the Company will be able to sell to other dealers homes that it may be obligated to repurchase in the future under such floor-plan financing arrangements or that the Company will not suffer more losses with respect to, and as a consequence of, those arrangements than we have accrued in our financial statements. No dealer accounted for more than 6.5% of the Company's net revenues in any of the past three fiscal years. (see "Sales Network") and the Company does not view any single independent dealer as being a material customer. The Company also finances substantially its entire retail inventory through funds generated from operations.

Competition

The manufactured housing industry is highly competitive at both the manufacturing and retail levels, with competition based upon numerous factors, including total price to the dealer, customization to homeowners' preferences, product features, quality, warranty repair service and the terms of dealer and retail customer financing. The Company has many competitors, ranging from very large, experienced and well financed companies to small and specialized manufacturers. There are numerous firms producing manufactured homes in the southeastern and south central United States, many of which are in direct competition with us. In addition, certain of the Company's competitors provide retail customers with financing from captive finance subsidiaries.

Manufactured homes also compete with other forms of housing, including site-built and prefabricated homes. Historically, manufactured housing has had a price advantage over these other forms of housing. That advantage has deteriorated, however, as the credit market, at both the retail and wholesale level, of the manufactured housing industry has continued to tighten, while interest rates for site-built houses are at historic lows, thus increasing the competitive pressures on manufactured housing.

The capital requirements for entry as a producer in the manufactured housing industry are relatively small. However, the Company believes that the qualifications for obtaining inventory financing, which are based upon the financial strength of the manufacturer and each of its dealers, have recently become more difficult to meet due to the departure of financial institutions from the market and dealers requiring principal and curtailment payments from the manufacturers.

The Company believes that its willingness to customize floor plans and design features to match customer preferences is the principal factor which differentiates it from most of its competitors in the manufactured housing industry.

Regulation

The Company's manufactured homes are subject to a number of federal, state and local laws. Construction of manufactured housing is governed by the National Manufactured Housing Construction and Safety Standards Act of 1974 ("1974 Act"). In 1976, HUD issued regulations under this Act establishing comprehensive national construction standards. The HUD regulations cover all aspects of manufactured home construction, including structural integrity, fire safety, wind loads, thermal protection, plumbing and electrical. Such regulations preempt conflicting state and local regulations. The Company's manufacturing facilities and the plans and specifications of its manufactured homes have been approved by a HUD-designated inspection agency. An independent, HUD-approved third-party inspector checks each of the Company's manufactured homes for compliance during at least one phase of construction. In 1994, HUD amended manufactured home construction safety standards to improve the wind force resistance of manufactured homes sold for occupancy in coastal areas prone to hurricanes. Failure to comply with the HUD regulations could expose the Company to a wide variety of sanctions, including closing the Company's plants. The Company believes its manufactured homes meet or surpass all present HUD requirements.

Manufactured, modular and site-built homes are all built with particleboard, paneling and other products

that contain formaldehyde resins. Since February 1985, HUD has regulated the allowable concentration of formaldehyde in certain products used in manufactured homes and required manufacturers to warn purchasers concerning formaldehyde associated risks. The Company currently uses materials in its manufactured homes that meet HUD standards for formaldehyde emissions and that otherwise comply with HUD regulations in this regard. In addition, certain components of manufactured homes are subject to regulation by the Consumer Product Safety Commission ("CPSC") which is empowered to ban the use of component materials believed to be hazardous to health and to require the manufacturer to repair defects in components of its homes. The CPSC, the Environmental Protection Agency and other governmental agencies are evaluating the effects of formaldehyde. In February 1983, the Federal Trade Commission adopted regulations requiring disclosure of manufactured home's insulation specifications.

The Company's manufactured homes are also subject to local zoning and housing regulations. A number of states require manufactured home producers to post bonds to ensure the satisfaction of consumer warranty claims. A number of states have adopted procedures governing the installation of manufactured homes. Utility connections are subject to state and local regulation, and must be complied with by the dealer or other person installing the home.

The Company is subject to the Magnuson-Moss Warranty Federal Trade Commission Improvement Act, which regulates the descriptions of warranties on products. The description and substance of the Company's warranties are also subject to a variety of state laws and regulations.

Employees

As of January 2, 2004, the Company employed 1,144 full-time employees involved in the following functional areas: manufacturing, 975; sales, 26; field service, 32; administration and clerical, 88; and management, 23. Our manufacturing operations primarily require semi-skilled labor. We have the ability to adjust personnel levels depending upon with seasonal changes in production requirements.

None of the Company's employees are represented by a collective bargaining agreement. The Company believes that it has a good relationship with its employees, and it has never experienced any work stoppage.

Executive Officers

Information concerning the Executive Officers of the Company is as follows. Executive Officers are elected annually by and serve at the pleasure of the Board of Directors.

Wendell L. Batchelor (age 61) is the Founder and Chairman of the Company and a Director since the Company's incorporation in 1982. Mr. Batchelor was Chief Executive Officer of the Company from 1982 until May 2002 and President of the Company from 1982 to 1999. From 1971 to 1982, Mr. Batchelor was General Manager of Shiloh Homes, a division of Winston Industries. Mr. Batchelor was Sales Manager of Marietta Homes, a division of Winston Industries, from 1968 to 1971 and from 1966 to 1968, he was a Sales Representative for Madrid Homes. Mr. Batchelor has served in the past as Chairman of the Alabama Manufacturer's Housing Institute.

Keith O. Holdbrooks (age 43) was elected as the Company's Chief Executive Officer in May of 2002 by the Company's Board of Directors and has served as the Company's President since June 1999 and Chief Operating Officer since August 1996. From 1991 to 1996, Mr. Holdbrooks served as General Manager for Southern Homes, a division of the Company, and from 1989 to 1991 Sales Manager for Southern Homes. From 1985 to 1989 he was a sales representative for the Company's Southern Lifestyle division .

James L. Stariha (age 42) joined the Company as its Chief Financial Officer in January of 2003. From 1999 to 2002, Mr. Stariha was Vice President of Finance of BISYS Document Solutions, a subsidiary of the BISYS Group, Inc., and from 1996 to 1999 was Executive Vice President and Chief Financial Officer of Healthcare Technology Delivery, Inc. From 1983 to 1996 Mr. Stariha served in a variety of financial, marketing, and manufacturing positions with Square D Company.

Dan Batchelor (age 51) serves as the Company's General Counsel and Executive Vice President. Mr. Batchelor practiced commercial and tort litigation and business law for almost twenty years before joining the Company in 1998. Mr. Batchelor received his B.A. from the University of Virginia in 1974; J.D. from Cumberland School of Law of Samford University in 1978; and LL.M. from the University of Miami School of Law in 1979. He is admitted to practice in Alabama, Georgia and Florida and various federal jurisdictions.

Discontinued Operations

Retail Operations

As industry conditions began to weaken during fiscal 1999, the Company began to close or sell retail centers that did not meet profit objectives. That process continued, based on a case-by-case determination, through the next three years, with fourteen of the 33 centers open at the end of fiscal 1998 having been closed by the end of fiscal 2001. During the latter part of fiscal 2002, management made the determination to close most of the fifteen retail centers then remaining and essentially withdraw from any further significant retail presence. In fiscal 2002, eleven retail centers were closed, and by the end of 2003, the Company had completed the closure of all but two of the retail centers that were formerly part of its retail segment. Five of these eleven centers were in Alabama, three were in South Carolina, two in Tennessee and one in Kentucky. The decision to close the retail centers was based primarily on management's evaluation of recent operating results and future prospects. The retail centers that were closed had been negatively affected by weak market conditions, including excess retail capacity in the industry, as well as restrictive retail financing conditions, principally as a result of the withdrawal of several lenders from the market. The decision to close the retail centers was based primarily on management's evaluation of recent operating results and future prospects of those centers, and was also part of a strategic decision to concentrate the Company's resources on the primary manufacturing operations.

Consumer Financing

Home buyers normally secure financing from third-party lenders such as banks or independent finance companies. The availability and cost of financing is important to the Company's sales. Starting in late 1999, financing started to become more restrictive and some lenders began to exit the market. During the period January 1996 through February 1997, the Company originated and serviced consumer loans through a wholly-owned subsidiary, Wenco Finance, Inc. ("Wenco Finance"), for homes manufactured by the Company, in order to provide home buyers with an additional source of financing. Later the Company provided retail financing through Wenco 21, a joint venture between the Company and 21st Mortgage Corporation. After the formation of Wenco 21, Wenco Finance conducted minimal loan origination operations. As part of its decision to redirect the Company's efforts to its core manufacturing operations, the Company sold the Wenco Finance business in late 2002, and no longer offers financing to retail customers.

Available Information

Prior to January 15, 2004, the Company's common stock was registered pursuant to Section 12(b) of the Securities Exchange Act, and the Company was subject to the reporting requirements of the Act. For periods ending prior to January 15, 2004, Forms 10-K, 10-Q and 8-K and other reports required under the Act are available through the SEC EDGAR system.

Following the Company's voluntary deregistration on January 15, 2004, the Company's duty to file reports with the SEC was automatically suspended. The Company plans, however, to continue providing quarterly financial information and audited annual financial statements to shareholders, as well as other reports from time to time as circumstances warrant. The Company makes this information available free of charge through its website (www.sehomes.com), and interested persons may also request copies of information directly from the Company; please direct requests and inquiries to Chief Financial Officer, Southern Energy Homes, Inc., 144 Corporate Way, Addison, Alabama 35540, telephone (256) 747-8589.

Please also note the explanation and cautionary discussion at the beginning of this report, "An Important Note About this Report."

Properties

The Company currently operates five home manufacturing facilities (four in Alabama and one in Texas) and three component supply facilities (all in Alabama), as follows:

Unit	Building Location	Square Feet	Leased or Owned
Manufacturing			
Southern Energy	Addison, AL	72,000	Owned
Southern Estates	Addison, AL	62,500	Owned
Southern Homes			
Plant #1	Double Springs, AL	60,000	Owned
Plant #4	Lynn, AL	90,000	Owned
Southern Energy Homes of Texas	Fort Worth, TX	98,300	Owned
Component Supply			
Classic Panel	Hartselle, AL	24,000	Owned
Wind-Mar Supply	Addison, AL	22,000	Owned
Trimmasters	Haleyville, AL	50,000	Leased

The Company considers its manufacturing facilities to be adequate for its present needs. Additional information concerning production capacity and extent of utilization is discussed under "Home Manufacturing Operations" in the business section of this Report.

The Company currently operates 2 retail sales centers both in Alabama.

The Company owns its corporate headquarters building located in Addison, Alabama consisting of approximately 15,400 square feet of office space.

Legal Proceedings

The Company is a party to various legal proceedings incidental to its business. The Company typically provides a one-year warranty on new manufactured homes. The majority of these legal proceedings are claims related to warranty on manufactured homes or employment issues such as workers' compensation claims. Management believes that adequate reserves are maintained for such claims. In the opinion of management, after consultation with legal counsel, the ultimate liability, if any, with respect to these proceedings will not materially affect the financial position or results of operations of the Company; however, the ultimate resolution of these matters, which could occur within one year, could result in losses in excess of the amounts reserved.

Submission to a Vote of Security Holders

No matters were submitted to a vote of the stockholders of the Company during the fourth quarter of fiscal year 2003

Market for the Company's Common Stock, Related Stockholder Matters and Company Purchases of Equity Securities

Record Holders

As of March 18, 2004, there were approximately 104 record holders of the Company's common stock. This number does not include those stockholders holding stock in "nominee" or "street" name.

Stock Price Performance

The following table represents the high and low bid price for each quarter of the last two fiscal years of the Company's common stock.

	2003 Bid Price Range		2002 Bid Price Range	
	High	Low	High	Low
First Quarter	$1.49	$1.15	$2.75	$2.25
Second Quarter	1.90	1.18	2.65	2.01
Third Quarter	2.50	1.82	2.41	1.25
Fourth Quarter	2.99	2.11	1.75	1.04

During the periods shown above, the Company's stock was listed on the NASDAQ National Market System, and the information above is as reported by NASDAQ. Shortly after the end of fiscal 2003 (effective January 15, 2004), the Company voluntarily deregistered its stock with the SEC and consequently the stock was no longer eligible for NASDAQ listing. The Company was eligible to deregister because it has fewer than 300 shareholders of record.

On January 16, 2004, the Company's stock began trading in the over-the-counter market through the Pink Sheets Electronic Quotation Service. Pink Sheet quotes are available over the internet at www.pinksheets.com as well as through other services.

Dividends

It is the Company's current policy to retain any future earnings to finance the continuing development of its business and not to pay dividends. The Company has not paid any dividends since the initial public offering of its stock in 1992.

Common Stock Repurchase Plan

The Company announced on December 15, 2003 that the board of directors adopted a plan to repurchase up to $4 million in a common stock repurchase program. Shares purchased under the program will be held in treasury and used to fund employee benefit plans and for general corporate purposes, including the possibility of future acquisitions, though none are presently contemplated. The repurchase authorization does not specify a maximum number of shares that may be purchased, a specific length of time for the repurchases, nor any price limitations. The Company expects the repurchase to be funded by available cash. Under the authorization, the Company may periodically repurchase shares on the open market at prevailing market prices or in privately negotiated transactions.

During the fiscal quarter ended January 2, 2004, the Company did not make any purchases of its shares, under the repurchase program or otherwise.

Selected Financial Data

Five-Year Selected Financial Data
Southern Energy Homes, Inc. and Subsidiaries
(Dollars in thousands, except share and per share data)

	Year Ended				
	January 2, 2004	January 3, 2003	December 28, 2001	December 29, 2000	December 31, 1999
Operating Data					
Net revenues	$126,357	$138,514	$129,105	$156,347	$233,012
Gross profit	20,420	25,628	26,682	26,552	43,188
Selling, general and administrative expenses	20,696	24,914	25,360	32,862	36,175
Amortization of intangibles (1)	37	53	299	425	320
Impairment charges (2)	-	-	2,240	5,818	7,073
Operating income (loss) from continuing operations	(313)	661	(1,217)	(12,553)	(380)
Interest expense	481	593	893	1,464	1,058
Interest income	91	41	112	234	130
Income tax benefit	(387)	(800)	-	(325)	(1,020)
Income (loss) from continuing operations	(316)	909	(1,998)	(13,458)	(288)
Loss from discontinued operations	(502)	(8,550)	(3,074)	(3,654)	(1,305)
Net loss	(818)	(7,641)	(5,072)	(17,112)	(1,593)
Net income (loss) from continuing operations per share (Basic and diluted)	$ (0.03)	$ 0.07	$(0.17)	$(1.11)	$(0.02)
Net income (loss) per share (Basic and diluted)	$(0.07)	$(0.63)	$(0.42)	$(1.41)	$(0.13)
Weighted average shares outstanding (basic and diluted)	12,140,541	12,133,865	12,133,298	12,132,990	12,176,705
Balance Sheet Data					
Total assets	$49,244	$51,728	$73,659	$96,571	$122,014
Short-term debt	-	32	10,677	10,964	28,049
Long-term debt	-	-	-	-	2,464
Stockholders' equity	38,153	38,960	46,601	51,672	68,784

The financial information for the periods above has been restated to reflect the reclassification of the 2002 retail center closings and the consumer finance segment as discontinued operations.

(1) On December 29, 2001, the Company adopted FASB Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, which eliminates amortization of goodwill and requires an annual impairment test. Goodwill amortized in 2001, 2000 and 1999 was $0.2 million, $0.4 million and $0.2 million, respectively.

(2) During 2001, the Company recorded a pre-tax charge of $1.6 million associated with the impairment of intangible assets related to certain of the Company's retail centers and a pre-tax charge of $602,000 related to impairment of a joint venture. During 2000, the Company recorded a pre-tax charge of $6.0 million associated with the impairment of intangible assets and exit costs related to certain of the Company's retail centers. During 1999, the Company recorded pre-tax charges of $7.1 million associated with the closing of its manufacturing facility in North Carolina and three retail centers, one in Kentucky and two in South Carolina.

RESULTS OF OPERATIONS

OVERVIEW

The Company continues to face a difficult competitive environment resulting from increased price competition and reduced profits that adversely affected the entire industry during the past five years.

Fiscal 2003 saw further credit tightening and declines in overall economic conditions that have compounded the situation, resulting in a significant reduction in the availability of financing, at both the wholesale and retail levels, and increasing repossession inventories. However, the recent announcement b the Federal National Mortgage Association and lender partners to provide low-cost financing for manufactured homes is expected to improve demand for our products. Management believes Southern Energy is in an excellent position to take advantage of new demand due to our recent investments in our plants, our strong financial position and improved market share. However, pricing of our products will likely remain a factor requiring close attention, especially in light of significant increases in raw material costs during the fourth quarter of this year.

We made a number of changes during 2003 that improved our financial position, reduced operating costs and broadened our product offerings. Our cash position improved over the prior year. We reduced overhead resulting in selling, general and administrative expenses declining in both absolute dollars and as a percentage of sales. We also reconfigured our manufacturing facilities to improve work flow and added the Southern Estates housing division that expanded our sales into a new market niche.

Our new product line, Southern Estates, which produced its first home in August, 2003, is intended to fill a product gap by including the most popular options with less customization. To provide manufacturing capacity for the new product line, the Company reconfigured certain of its manufacturing operations by combining production of the Lifestyle line into the Southern Energy plant. In addition, the Company is investing $1.5 million to expand the Southern Energy plant into adjacent facilities. The expanded space will be used for improving efficiencies in finishing operations on the Company's higher end homes.

Year Ended January 2, 2004 as Compared with Year Ended January 3, 2003

Net Revenues

Total net revenues (consisting of gross revenues less volume discounts, dealer interest, returns, and allowances) for the year ended January 2, 2004 from continuing operations were $126.4 million, which represented a decline of 8.7% from 2002 net revenues of $138.5 million from continuing operations.

Net revenues from the manufactured home segment were $121.1 million (including intersegment revenues of $2.1 million) for the year ended January 2, 2004 as compared with $132.9 million (including intersegment revenues of $6.7 million) for the prior year period, a decrease of $11.8 million, or 8.8%. Total homes shipped in the year ended January 2, 2004 were 3,606, down 14.2% from the number of homes shipped in the prior year period. The decrease in homes sold was attributable to an overall industry decline in the Company's market areas. According to MHI published industry sources, industry units shipped in our market area declined 26.2% in 2003 from the prior year. The Company's market share in units shipped, however, rose from 3.8% in 2002 to 4.4% in 2003. The average wholesale price per home in 2003 was $31,891, as compared with $30,012 in 2002, an increase of 6.3%.

Net revenues from the retail sales segment from continuing operations were $4.1 million for the year ended January 2, 2004 as compared with $9.2 million for the prior year period, a decrease of $5.1 million, or 55.4%. The decline in retail revenue reflects both the continuing tighter consumer financing as well as other general economic factors. The number of total homes (new and used) sold by the retail segment from continuing operations in the year ended January 2, 2004 was 69, down 72% from the number of homes sold in the prior year period. The average retail price per new home in 2003 was $55,918 as compared with $47,977 in 2002, an increase of 16.6%.

Net revenues from the component supply segment were $24.7 million (including intersegment revenues of $21.5 million) for the year ended January 2, 2004, as compared with $24.6 million (including intersegment revenues of $21.8 million) for the prior year period.

Operating facts

	Fiscal years ended	
	January 2, 2004	January 3, 2003
Company owned retail centers (continuing operations)	2	3
Retail units sold:		
New Single-section	7	21
New Multi-section	41	137
Used homes	21	88
Total	69	246
Wholesale units sold:		
External customers	3,549	4,030
Intercompany	57	173
	3,606	4,203
Total homes sold	3,675	4,449
Average sales prices - retail (new)	$55,918	$47,977
Average sales price – wholesale	$31,891	$30,012
Floor sections produced	6,347	7,334

Gross Profit

Gross profit consists of net revenues less the cost of sales, which includes labor, materials and overhead. Gross profit for the year ended January 2, 2004 from continuing operations was $20.4 million, or 16.2% of net revenues, as compared with $25.6 million, or 18.5% of net revenues, in the prior year period. This decline in the gross profit percentage was attributable primarily to higher labor costs, higher material prices, and higher warranty expenses offset slightly by higher sales prices.

Selling, General and Administrative Expenses

Selling, general and administrative expenses include primarily sales commissions, advertising expenses, freight costs, salaries for support personnel, administrative compensation, insurance costs, and professional fees. Selling, general and administrative expenses from continuing operations were $20.7 million, or 16.4% of net revenues, during the year ended January 2, 2004, as compared with $24.9 million, or 18.0% of net revenues, for the same period of the prior year. The decrease in selling, general and administrative expenses as a percentage of sales was attributable to the following factors: lower dealer interest payments, lower administrative salaries and lower legal expenses, offset slightly by higher insurance expenses.

Interest Expense

Interest expense for the year ended January 2, 2004 from continuing operations was $0.5 million as compared with $0.6 million for the year ended January 3, 2003.

Income Taxes

Income taxes are provided for based on the tax effect of revenue and expense transactions included in the

determination of pre-tax book income. Because the Company has operated at a loss in recent fiscal years, management believes that under the provisions of SFAS 109, it is not appropriate to record income tax benefits on current losses in excess of anticipated refunds of taxes previously paid. As a result, the Company has established valuation allowances against the net deferred tax benefits related to net operating loss carry forwards and other net deductible temporary differences between financial and taxable income. The valuation allowance may be reversed in future years if the Company returns to profitability.

At January 2, 2004, the Company had a federal net operating loss carry forward of approximately $2.9 million that expires in 2023. State net operating loss carryforwards amounting to approximately $20.9 million are available to offset future taxable income in Alabama and Texas and they expire at various dates in 2006 through 2023. The tax loss generated in 2002 for federal income tax purposes was carried back under the temporary 5 year net operating loss carry back rules applicable to 2002. Accordingly, the Company filed a carryback refund claim and received a federal income tax refund of $5.3 million in 2003 with respect to the 2002 net operating loss. The difference between the actual (as filed) refund received in 2003 and the estimated refundable tax recorded in our balance sheet at the end of fiscal 2002 is reflected in the 2003 tax benefit.

Year Ended January 3, 2003 as Compared with Year Ended December 28, 2001

Net Revenues

Total net revenues (consisting of gross revenues less volume discounts, dealer interest, returns, and allowances) for the year ended January 3, 2003 from continuing operations were $138.5 million, which represented an increase of 7.3% from 2001 revenues of $129.1 million from continuing operations.

Net revenues from the manufactured home segment were $132.9 million (including intersegment revenues of $6.7 million) for the year ended January 3, 2003 as compared with $133.6 million (including intersegment revenues of $18.4 million) for the prior year period, a decrease of $0.7 million, or 0.6%. Total homes shipped in the year ended January 3, 2003 were 4,203, down 4.7% from the number of homes shipped in the prior year period. The decrease in homes sold was attributable to an overall industry decline in the Company's core market areas and increased competition within these market areas. The average wholesale price per home in 2002 was $30,012, as compared with $28,826 in 2001, an increase of 4.1%.

Net revenues from the retail sales segment from continuing operations were $9.2 million for the year ended January 3, 2003 as compared with $10.5 million for the prior year period, a decrease of $1.3 million, or 12%. The decline in retail revenue reflects both tighter consumer financing and other general economic factors. The number of total homes (new and used) sold by the retail segment from continuing operations in the year ended January 3, 2003 was 246, down 19.6% from the number of homes sold in the prior year period. The average retail price per new home in 2002 was $47,977 as compared with $46,593 in 2001, an increase of 3.0%.

Net revenues from the component supply segment were $24.6 million (including intersegment revenues of $21.8 million) for the year ended January 3, 2003, as compared with $23.3 million (including intersegment revenues of $20.3 million) for the prior year period, an increase of $1.3 million, or 5.5%.

Gross Profit

Gross profit consists of net revenues less the cost of sales, which includes labor, materials and overhead. Gross profit for the year ended January 3, 2003 from continuing operations was $25.6 million, or 18.5% of net revenues, as compared with $26.7 million, or 20.7% of net revenues, in the prior year period. This decline in the gross profit percentage was attributable primarily to higher labor costs and material prices, offset slightly by higher sales prices and lower warranty expenses.

Selling, General and Administrative Expenses

Selling, general and administrative expenses include primarily sales commissions, advertising expenses, freight

costs, salaries for support personnel, administrative compensation, insurance costs, and professional fees. Selling, general and administrative expenses from continuing operations were $24.9 million, or 18.0% of net revenues, during the year ended January 3, 2003, as compared with $25.4 million, or 19.6% of net revenues, for the same period of the prior year. The decrease in selling, general and administrative expenses as a percentage of sales was attributable to the following factors: lower dealer interest payments and lower administrative salaries, offset slightly by higher insurance expenses.

Interest Expense

Interest expense for the year ended January 3, 2003 from continuing operations was $0.6 million as compared with $0.9 million for the year ended December 28, 2001. The decline in interest expense in the current year was a result of lower interest rates, 5.7% compared to 7.6%, through the Company's line of credit and lower average borrowings.

Income Taxes

During the fiscal year ended January 3, 2003, in which the Company recognized significant losses from the closing of retail centers and the sale of the Wenco Finance loan portfolio, the Company recorded a $4.5 million current tax benefit from discontinued operations. The Company filed a federal carryback refund claim in the second quarter of fiscal 2003. Recorded income tax benefits for the year-end January 3, 2003 from continued operations was $0.8 million compared to no income tax benefit from continuing operations recorded for the year ended December 28, 2001. In fiscal 2001, the Company established valuation allowances against the tax benefits of substantially all net operating loss carry forwards and deductible temporary differences between financial and taxable income. The tax benefit otherwise applicable to the 2001 net operating losses was completely offset by the valuation allowance for deferred tax assets.

Contractual Obligations and Commercial Commitments

The Company has various contractual obligations and commercial commitments arising from operations. These obligations and commitments are more fully described in this Annual Report under various headings in "Management's Discussion and Analysis" as well as in the notes to the audited financial statements. The following table lists the aggregate maturities of various classes of obligations and amounts of commitments payable or expiring by time frames indicated as of January 2, 2004 (in millions):

Contractual Obligations:	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Operating Leases	$ 0.1	$ 0.1	$ -	$ -	$ -
Other Commercial Commitments (1):					
Letters of Credit	$ 0.7	$ 0.7	$ -	$ -	$ -

(1) Excludes commitments described below

Substantially all of the Company's independent dealers finance their purchases through "floor plan" arrangements under which a financial institution provides the dealer with a loan for the purchase price of the home and maintains a security interest in the home as collateral. In connection with a floor plan arrangement, the financial institution that provides the independent dealer financing customarily requires the Company to enter into a separate repurchase agreement with the financial institution, under which the Company is obligated, upon default by the independent dealer, to repurchase the homes at the Company's original invoice price less cost of all damaged/missing items and less certain curtailments, plus certain administrative and shipping expenses. Repurchases were $1.5 million, $2.0 million and $4.2 million for the years ended 2003, 2002, and 2001, respectively. Losses on homes repurchased under these agreements were $0.3 million, $0.5 million and $0.9 million for the years ended 2003, 2002, and 2001, respectively. At January 2, 2004, the Company had a reserve of $250,000 for future repurchase losses, related to these floor plan arrangements. At January 2, 2004, the Company's contingent repurchase liability under floor plan financing arrangements through independent dealers was approximately $39.2 million.

The Company is also obligated under the revenue sharing agreement to repurchase homes that were financed by Wenco 21 LLC, upon repossession, for 50% to 65% of the outstanding loan balance, approximately $11.6 million

maximum commitment at January 2, 2004. At January 2, 2004, the Company had a reserve of $330,000 for future repurchase losses. Losses on homes repurchased under this obligation were not significant in fiscal 2003, 2002 and 2001.

Joint Ventures

The Company owns interests in four joint ventures. Ownership interests range from 33% to 39%. These joint ventures have total assets of $11.2 million and total liabilities of $4.7. Because the Company is a limited partner or has an interest in a limited liability company, the Company's exposure to loss is generally limited to its investments and advances and any commitments to fund operations of the investees. The Company and certain of its equity partners have guaranteed certain debt for companies in which the Company owns various equity interests. The guarantees are limited to various percentages of the outstanding debt. At January 2, 2004, $2.9 million was outstanding under the various guarantees, of which the Company had guaranteed $1.0 million. One of the companies has lease purchase agreements with third parties to sell a facility financed by debt that the Company has guaranteed. The Company expects the proceeds from the exercise of the purchase option to be used to pay off the debt and to be released from the guaranty upon payoff in 2004.

LIQUIDITY AND CAPITAL RESOURCES

Since its organization, the Company has financed its operations primarily with cash generated from a combination of operations, stock offerings and borrowings.

During the year ended January 2, 2004, net cash provided by operating activities of continuing operations was approximately $4.2 million. Net loss from continuing operations for the year was $0.3 million, which included non-cash charges for amortization expenses of $0.4 million and depreciation expense of $2.1 million, as well as non-cash income from the equity in earnings of joint ventures of $0.3 million. Cash provided by operating activities also included income tax refunds of $4.2 million and decreased accounts receivable of $0.9 million and other receivables of $0.6 million, partially offset by increased inventories of $0.8 million, increased prepayments and other of $0.7 million, decreased accounts payable and accruals of $1.6 million. In addition to cash provided by operating activities, other significant items affecting cash flows from continuing operations included capital expenditures of $1.8 million, net cash received from joint ventures of $0.2 million, and proceeds from the sale of property, plant and equipment of $0.2 million.

In accordance with the Company's current revolving credit facility, the Company applies all cash receipts to reduce the line of credit. At January 2, 2004 the balance of the revolving credit facility was zero and the Company's net working capital from continuing operations was $14.6 million, including $10.2 million in cash and cash equivalents, as compared with a working capital of $13.2 million at January 3, 2003, including $7.0 million in cash and cash equivalents. The increase in net working capital was primarily attributable to an increase in cash and cash equivalents of $3.2 million, a decrease in accounts payable and accrued liabilities of $1.6 million, an increase in inventories of $0.8 million and increase in prepayments and other of $0.7 million, partially offset by decreases in refundable income taxes of $4.2 million, accounts receivable of $0.9 million and other receivables of $0.6 million.

For the year ended January 2, 2004, net cash flow from discontinued operations was $0.6 million, principally from the sale of retail inventory and other assets, offset by a net loss from discontinued operations of $0.5 million, which included a reserve for losses on repossessions of $0.3 million.

During the year ended January 3, 2003, net cash provided by continuing operations was approximately $0.8 million. Net income from continuing operations for the year was $0.9 million. Included in net income were the following non-cash charges: amortization expenses of $0.4 million, provision for doubtful accounts of $0.2 million and depreciation expense of $2.2 million. Cash provided by operating activities also reflected decreased accounts receivable of $1.2 million, decreased inventories of $0.9 million, and an increase in accounts payable of $0.4 million, which were offset by an increase in refundable income taxes of $3.8 million and a decrease in accrued liabilities of $1.4 million. In addition to cash provided by operating activities, other significant items affecting cash flows from continuing operations included capital expenditures of $2.0 million, proceeds from the sale of property,

plant and equipment of $0.8 million, net repayments of notes payable of $10.6 million, and net cash from joint ventures of $0.9 million.

At January 3, 2003 the balance of the revolving credit facility was zero and the Company's net working capital from continuing operations was $13.2 million, including $7.0 million in cash and cash equivalents, as compared with a negative working capital of $6.6 million at December 28, 2001, including $0.3 million in cash and cash equivalents. The increase in net working capital was primarily attributable to an increase in cash and cash equivalents of $6.7 million, an increase in refundable income taxes and other assets of $3.8 million, a decrease in accrued liabilities of $1.4 million and a decrease in notes payable of $10.6 million, partially offset by a decrease in accounts receivable of $1.2 million, a decrease in inventories of $0.9 million, and an increase in accounts payable of $0.4 million.

During the year ended January 3, 2003, the Company's net cash flow from discontinued operations was $16.7 million. The sale of the Wenco loan portfolio for $6.1 million and sale of inventory and other assets from the closure of eleven retail centers were the main contributing factors to the increase in cash flow, offset by a net loss from discontinued operations of $8.6 million.

At January 2, 2004 the Company had a $10 million secured line of credit, which matures on March 8, 2005 and bears interest at the prime rate plus 1%, which amounted to 5% at January 2, 2004. At January 2, 2004 the Company's availability on the line of credit (based on an asset base limitation) was $8 million. The Company's ability to draw upon this line of credit is dependent upon its continued compliance with certain financial ratios and covenants. The Company had no outstanding borrowings at January 2, 2004 and January 3, 2003, respectively.

Capital Expenditures

As of January 2, 2004, the Company does not currently plan to make material capital expenditures during the next twelve months. However, if business conditions change, the Company could increase its capital expenditures plans for 2004.

Critical Accounting Estimates

The Company uses accounting policies that it believes are appropriate to accurately and fairly report its results of operations and financial position, and it applies those accounting policies in a consistent manner. The preparation of the Company's financial statements in conformity with generally accepted accounting principles requires that the Company's management make estimates and assumptions that may affect the reported amounts of assets, liabilities, revenues and expenses. These estimates and assumptions are based on historical and other factors believed to be reasonable under the circumstances. The Company evaluates these estimates and assumptions on an ongoing basis. Actual results can and frequently will differ from these estimates. It is possible that materially different amounts would be reported under different conditions or using different methods or assumptions.

The Company believes that the following accounting policies are the most critical ones used in the preparation of its financial statements, because these are the ones that involve the most significant judgments and estimates about the effect of matters that are inherently uncertain.

Product Warranties

The Company warrants its products against certain manufacturing defects for a period of one year commencing at the time of retail sale, and the estimated cost of such warranties is accrued at the time of sale to the independent dealer. The Company's estimates are derived from two main elements: the historical average cost of servicing warranties, and the number of units under warranty, which includes homes in retailer inventories and homes purchased by consumers still within the warranty period. Many factors can cause the actual warranty cost in any period to vary from average historical cost. In addition, the time when a unit is sold at retail affects the average warranty cost estimate in a given time period, both because of the fluctuations in historical average per unit warranty cost over time, and the fact that warranty costs are higher earlier in the warranty period and lower nearer the end of the warranty period. Warranty costs represent a significant expense to the Company, and therefore significant changes in the above factors could have an adverse effect on the Company's financial performance.

Volume Incentives Payable

Volume incentive payments to independent dealers who retail the Company's products are accounted for as a reduction to gross sales, and are estimated and accrued when sales of products are made to the dealers. Volume incentive reserves are recorded based on the annualized purchases of independent dealers who purchase the minimum qualifying amount of product from the Company. The potential amount of the payment is accrued by the Company at the time of the sale to the dealer, based upon estimates derived from the historical payout rates. Actual payout rates fluctuate based on dealer compliance and performance, which is affected by a number of variables, including general economic conditions and the quality of individual dealers and their respective sales organizations. Volume incentive costs represent a significant expense to the Company, and therefore significant changes in the above factors could have an adverse effect on the Company's financial performance.

Litigation

The Company is a party to various legal proceedings incidental to its business. The majority of these legal proceedings are claims related to warranties on manufactured homes or employment issues. Establishing reserves for such claims requires subjective judgments, on an ongoing, case-by-case basis, that take into account all the known circumstances at any point in time. The Company relies largely upon consultation with legal counsel to assist it in making estimates of the likely ultimate cost of these matters. Though litigation reserve estimates include as a component the average historical cost of successful defense or other processing of nonmeritorious claims, legal proceedings and their ultimate resolution are of course largely outside the Company's control and often bear no relationship to historical experience, legal merit, or any other factual analysis or any analytic method. The Company attempts to minimize the inherent unpredictability of the reserve estimates by continuous review and updating, but there is no way to eliminate the risk that the ultimate resolution of these matters could result in losses in excess of the amounts reserved.

Workers Compensation Claims

The Company is partially self-insured for workers compensation claims. The Company purchases insurance coverage for all workers compensation claims in excess of stated limits, currently $350,000 per occurrence. Amounts are accrued currently for the estimated costs of claims incurred, including related expenses. Accrual of liabilities for unsettled claims requires that the Company estimate its ultimate liability for medical costs, lost wages and legal and related expenses. These estimates are primarily based on actuarial information and third-party consultants who provide assessments of medical impairments and related economic consequences. Periodic adjustments to the reserves are made as events occur that indicate changes are necessary. Nonetheless, there is no assurance that the amounts accrued will not vary from the ultimate amounts incurred upon final disposition of all outstanding claims.

Repurchase Obligations

Substantially all of the Company's independent dealers finance their purchases through "floor plan" arrangements under which a financial institution provides the dealer with a loan for the purchase price of the home and maintains a security interest in the home as collateral. In connection with a floor plan arrangement, the financial institution that provides the independent dealer financing customarily requires the Company to enter into a separate repurchase agreement with the financial institution, under which the Company is obligated, upon default by the independent dealer, to repurchase the homes at the Company's original invoice price less the cost of all damaged/missing items and less certain curtailments, plus certain administrative and shipping expenses. Potential losses under repurchase obligations are a function of the difference between the repurchase price and the estimated net resale value of the homes. Estimated losses under repurchase agreements are accrued based on the historical number of homes repurchased, the cost of such repurchases and the historical losses incurred, as well as the current inventory levels held by independent dealers. The Company also takes into consideration known risks associated with independent dealers. Significant changes in these factors could have a material adverse impact on future operating results.

The Company also has contingent repurchase obligations under the terms of the revenue sharing agreement with 21st Mortgage Corporation by which 21st Mortgage and the Company will share equally in the profits and losses derived from the loans that comprised the Wenco 21, LLC portfolio (the details of which are discussed in note 7 to the financial statements). The Company estimates the possible future repurchase losses arising from these obligations based upon historical losses incurred, the cost of such repurchases and the historical losses incurred, as well as the current loan balances in the portfolio. Significant changes in these factors could have a material adverse impact on

future operating results.

Inflation

The Company believes that the relatively moderate rate of inflation over the past few years has not had a significant impact on its sales or profitability. Although there can be no assurance that the Company will be able to do so in the future, the Company has in the past been able to pass on most of the increases in its costs by increasing selling prices. There is no assurance that we will be able to continue increasing our selling prices in the future.

Quantitative and Qualitative Disclosures Regarding Market Risk

Historically the Company has not entered into derivatives contracts to either hedge existing risk or for speculative purposes. The Company also does not and has not entered into contracts involving derivative financial instruments or derivative commodity instruments. To the extent that "financial instruments" may be deemed to include trade accounts receivable, loans and structured notes, the Company does not utilize derivative instruments to manage such risks. The Company's principal credit agreement bears a floating interest rate of 1.0% over prime. Accordingly, the Company is subject to market risk associated with changes in interest rates. At January 2, 2004, nothing was outstanding under the credit agreement. With respect to accounts receivable, most of the Company's sales of manufactured homes are pre-sold, such that orders exist before construction begins. When manufactured homes are sold to dealers as inventory, such homes are generally paid from availability under the dealer's floor plan financing arrangement. In the typical case, funds are wired to the Company from the dealer's floor plan lender within 21 days of delivery to the dealer's lot. Management thus does not perceive that the Company is subject to a material market risk with respect to its non-interest bearing accounts receivable.

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Consolidated Financial Statements and Notes to Consolidated Financial Statements

Consolidated Balance Sheets
Southern Energy Homes, Inc. and Subsidiaries

	January 2, 2004	January 3, 2003
Assets		
Current Assets:		
Cash and cash equivalents	$ 10,174,000	$ 6,960,000
Accounts receivable, less allowance for doubtful accounts of $362,000 and $323,000, respectively	4,682,000	5,504,000
Other receivables	1,526,000	1,236,000
Inventories	8,098,000	7,280,000
Refundable income taxes	-	4,191,000
Prepayments and other	1,215,000	483,000
Current assets of discontinued operations	51,000	800,000
	25,746,000	26,454,000
Property, plant, and equipment:		
Property, plant and equipment, at cost	33,127,000	31,636,000
Less accumulated depreciation and amortization	(17,204,000)	(15,613,000)
	15,923,000	16,023,000
Intangibles and other non-current assets:		
Goodwill, net	3,305,000	3,305,000
Investment in joint ventures	3,694,000	4,300,000
Other assets	526,000	958,000
Non-current assets of discontinued operations	50,000	688,000
	7,575,000	9,251,000
	$ 49,244,000	$ 51,728,000
Liabilities and Stockholders' Equity		
Current liabilities:		
Notes payable	$ -	$ 32,000
Accounts payable	1,120,000	1,662,000
Volume incentive payable	2,035,000	3,204,000
Accrued payroll related expenses	1,410,000	1,713,000
Accrued workers' compensation	1,454,000	1,886,000
Accrued warranty	2,312,000	2,143,000
Accrued other	2,758,000	1,808,000
Current liabilities of discontinued operations	2,000	320,000
	11,091,000	12,768,000
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Preferred stock, $.0001 par value, 1,000,000 shares authorized, none outstanding	-	-
Common stock, $.0001 par value, 40,000,000 shares authorized, 12,143,865 and 12,133,865 shares issued and outstanding at January 2, 2004 and at January 3, 2003, respectively	1,000	1,000
Capital in excess of par	8,341,000	8,330,000
Retained earnings	29,811,000	30,629,000
	38,153,000	38,960,000
	$49,244,000	$51,728,000

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

Consolidated Statements of Operations
Southern Energy Homes, Inc. and Subsidiaries

	Year Ended		
	January 2, 2004	January 3, 2003	December 28, 2001
	(52 Weeks)	(53 Weeks)	(52 Weeks)
Net revenues	$126,357,000	$138,514,000	$129,105,000
Cost of sales	105,937,000	112,886,000	102,423,000
Gross profit	20,420,000	25,628,000	26,682,000
Operating expenses:			
Selling, general and administrative	20,696,000	24,914,000	25,360,000
Amortization of intangibles	37,000	53,000	299,000
Impairment and other charges (Note 9)	-	-	2,240,000
	20,733,000	24,967,000	27,899,000
Operating income (loss) from continuing operations	(313,000)	661,000	(1,217,000)
Interest expense (including amortization of debt issue costs)	(481,000)	(593,000)	(893,000)
Interest income	91,000	41,000	112,000
Income (loss) from continuing operations before income taxes	(703,000)	109,000	(1,998,000)
Benefit for income taxes	387,000	800,000	-
Income (loss) from continuing operations	(316,000)	909,000	(1,998,000)
Loss from discontinued operations, net of tax benefit of $4.5 million for the fiscal year ended January 3, 2003	(502,000)	(8,550,000)	(3,074,000)
Net loss	$(818,000)	$(7,641,000)	$(5,072,000)
Per share data:			
Basic and diluted net income (loss) per share:			
Income (loss) from continuing operations	$ (0.03)	$ 0.07	$ (0.17)
Loss from discontinued operations	(0.04)	(0.70)	(0.25)
Net loss	$ (0.07)	$ (0.63)	$ (0.42)
Weighted average number of common shares outstanding:			
Basic and diluted	12,140,541	12,133,865	12,133,298

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

Consolidated Statements of Stockholders' Equity
Southern Energy Homes, Inc. and Subsidiaries

	Common Stock		Capital in Excess	Retained	
	Shares	Amount	of Par	Earnings	Total
Balance, December 29, 2000	12,132,990	$1,000	$8,329,000	$43,342,000	$51,672,000
Exercise of stock options	875	-	1,000	-	1,000
Net loss	-	-	-	(5,072,000)	(5,072,000)
Balance, December 28, 2001	12,133,865	1,000	8,330,000	38,270,000	46,601,000
Net loss	-	-	-	(7,641,000)	(7,641,000)
Balance, January 3, 2003	12,133,865	1,000	8,330,000	30,629,000	38,960,000
Exercise of stock options	10,000	-	11,000	-	11,000
Net loss	-	-	-	(818,000)	(818,000)
Balance, January 2, 2004	12,143,865	$1,000	$8,341,000	$29,811,000	$38,153,000

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

Consolidated Statements of Cash Flows
Southern Energy Homes, Inc. and Subsidiaries

	Year Ended		
	January 2, 2004	January 3, 2003	December 28, 2001
	(52 Weeks)	(53 Weeks)	(52 Weeks)
Cash flows from operating activities:			
Income (loss) from continuing operations	$ (316,000)	$ 909,000	$(1,998,000)
Adjustments to reconcile income (loss) from continuing operations to net cash provided by operating activities:			
Equity in earnings of joint ventures	(333,000)	(329,000)	(365,000)
Non-cash impairment charges (Note 9)	-	-	2,240,000
Depreciation of property, plant and equipment	2,147,000	2,240,000	2,327,000
(Gain) loss on sale of property, plant and equipment	(151,000)	(44,000)	351,000
Amortization of debt issuance costs	354,000	370,000	290,000
Amortization of intangibles	37,000	53,000	299,000
Provision for doubtful accounts receivable	(39,000)	163,000	(8,000)
Change in assets and liabilities:			-
Accounts receivable	862,000	1,214,000	884,000
Other receivables	603,000	264,000	(48,000)
Inventories	(818,000)	886,000	5,414,000
Prepayments and other	(663,000)	(89,000)	6,497,000
Refundable income taxes	4,191,000	(3,842,000)	-
Accounts payable	(823,000)	390,000	111,000
Accrued liabilities	(813,000)	(1,354,000)	(1,304,000)
Net cash provided by operating activities	4,238,000	831,000	14,690,000
Cash flows from investing activities:			
Capital expenditures	(1,795,000)	(2,023,000)	(1,072,000)
Investments in joint ventures	(128,000)	(549,000)	(146,000)
Proceeds from sale of joint venture	-	1,250,000	-
Distributions from joint ventures	175,000	235,000	371,000
Proceeds from sale of property, plant and equipment	179,000	823,000	1,155,000
Net cash (used in) provided by investing activities	(1,569,000)	(264,000)	308,000
Cash flows from financing activities:			
Net repayments on notes payable	(32,000)	(10,645,000)	(12,170,000)
Payment of debt issuance costs	-	(29,000)	(1,002,000)
Proceeds from exercise of stock options	11,000	-	1,000
Net cash used in financing activities	(21,000)	(10,674,000)	(13,171,000)
Net increase (decrease) in cash and cash equivalents from continuing operations	2,648,000	(10,107,000)	1,827,000
Net cash provided by (used in) discontinued Operations	566,000	16,739,000	(7,544,000)
Net increase (decrease) in cash and cash equivalents	3,214,000	6,632,000	(5,717,000)
Cash and cash equivalents at beginning of year	6,960,000	328,000	6,045,000
Cash and cash equivalents at end of year	$10,174,000	$6,960,000	$ 328,000
Supplemental cash flow information:			
Cash paid for interest	$ 481,000	$ 612,000	$ 1,947,000
Tax refunds received, net of payments	$ 5,248,000	$ 1,377,000	$ 5,135,000

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

Notes to Consolidated Financial Statements

Southern Energy Homes, Inc. and Subsidiaries

1. The Company and Basis of Presentation

Southern Energy Homes, Inc. (the "Company") has three reportable segments: manufacturing, retail and component supply. The Company produces manufactured homes, primarily on a custom basis, for wholesale to dealers located primarily in the southeastern and south-central regions of the United States. Retail sales are concentrated in the southeastern United States. The component supply segment sells various supply products to the Company's manufacturing segment and to third-party customers.

The Company is on a 52/53-week year with the fiscal year ending on the Friday closest to the last day of December. The 2003 fiscal year included 52 weeks, the 2002 fiscal year included 53 weeks and the 2001 fiscal year included 52 weeks.

The Company's business is seasonal and cyclical with the potential for significant fluctuations in earnings being affected by factors impacting the broader housing market, including the availability and cost of customer financing and changes in the cost of construction materials.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Discontinued Operations

The Company closed a retail center in South Carolina in the second quarter of 2003. The closure of this retail center was not material to the financial results of the Company.

In 2002, the Company closed eleven retail centers that were formerly part of the retail segment. These retail centers had been negatively affected by weak market conditions and restrictive retail financing conditions, principally as a result of the withdrawal of several lenders from the market. The decision to close the retail centers was based primarily on management’s evaluation of recent operating results and future prospects. These centers were sold or closed by the end of December 2002.

The Company also sold its consumer financing segment, principally consisting of the Wenco loan portfolio, in December 2002. The Wenco loan portfolio had a book value of approximately $11.8 million. The loan portfolio was sold for $6.1 million in a cash transaction. The decision to sell the loan portfolio was prompted by management's strategic plan to eliminate unprofitable business lines and thereby allow the Company to focus on its core manufacturing business.

As required by FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* ("SFAS 144"), the operating results and disposal of the eleven retail centers and the Wenco loan portfolio, which were previously reported in the retail and consumer financing segments, have been classified in discontinued operations for all prior periods presented herein. The Company recognized a $0.5 million loss on discontinued operations in the year ended January 2, 2004 which included a reserve of $0.3 million for losses on repurchase obligations. The Company recognized a $13.1 million loss ($8.6 million net of tax benefit) on discontinued operations in the year ended January 3, 2003, which included $2.7 million of operating losses during the year, $3.6 million to write-down the carrying value of unsold homes in retail inventory, $1.1 million for leasehold, severance, termination of leases and other related costs and the $5.7 million loss on sale of the Wenco loan portfolio. As required by SFAS 144, any further operating losses, as well as adjustments to exit costs accruals (if any), will be reported in discontinued operations as incurred, or when circumstances warrant revisions of the related accounts. Historical operating results of the discontinued operations were as follows for the years ended:

	January 2, 2004	January 3, 2003	December 28, 2001
Net revenues	$ 1,533,000	$ 16,836,000	$ 27,888,000

Loss from operations	(502,000)	(2,662,000)	(3,074,000)
Disposal loss	-	(10,388,000)	-
Net loss before tax	$ (502,000)	$ (13,050,000)	$ (3,074,000)

As of January 2, 2004, the remaining assets and liabilities of the discontinued operations are reflected in the consolidated balance sheets as current or non-current based on the original classification of these accounts, net of any necessary valuation allowances. Although we believe we have appropriately reduced the carrying value of the assets to their estimated recoverable amounts, net of disposal cost where appropriate, actual results could be different and the difference will be reported in discontinued operations in future periods.

Net assets of the discontinued operations are as follows:

	January 2, 2004	January 3, 2003
Current Assets:		
Inventories	$ 51,000	$ 675,000
Prepayments and other	-	125,000
Total current assets:	51,000	800,000
Non –Current Assets:		
Installment contracts receivable	-	342,000
Property, plant and equipment	50,000	344,000
Other assets	-	2,000
Total non -current assets:	50,000	688,000
Current liabilities	(2,000)	(320,000)
Net assets of discontinued operations	$ 99,000	$ 1,168,000

There are no material contingent liabilities, including environmental liabilities or litigation, related to the closed retail centers or the consumer finance business discontinued in 2002.

3. Summary of Significant Accounting Policies

Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. All significant intercompany transactions have been eliminated in the consolidated financial statements.

Investments in Joint Ventures

The Company accounts for its investments of 50% or less in joint ventures, where it does not have the ability to control, on the equity basis of accounting. Therefore, the Company's share of income or loss is recorded as equity income or loss from its ventures in the accompanying consolidated statements of operations (see Note 5).

Impairment is recognized when facts and circumstances indicate that the carrying value of an investment is not likely to be recoverable from cash distributions and proceeds from sale or liquidation of the investee. No public market exists for any of the Company's equity investees.

Cash and Cash Equivalents

For purposes of reporting cash flows, the Company considers cash and cash equivalents to include cash on hand and highly liquid debt instruments and investments purchased with an original maturity of three months or less.

Advertising Costs

Advertising costs are expensed as incurred and totaled $1.2 million, $1.6 million and $1.5 million for 2003, 2002 and 2001, respectively.

Inventories

Inventories are valued at first-in, first-out ("FIFO") cost, which is not in excess of market. An analysis of inventories

(excluding those reported in discontinued operations) follows:

	January 2, 2004	January 3, 2003
Raw materials	$ 4,564,000	$ 3,725,000
Work in progress	703,000	570,000
Finished goods	2,831,000	2,985,000
	$ 8,098,000	$ 7,280,000

Property, Plant and Equipment

Property, plant and equipment are recorded at cost. Depreciation is computed on the straight-line, accelerated cost recovery system or modified accelerated cost recovery system methods over the estimated service lives of depreciable assets (5-39 years for buildings and improvements, 3-10 years for machinery and equipment, 5-10 years for office and computer equipment, and 7-10 years for leasehold improvements, which is the lesser of the lease term or the asset's useful life). Cost of property, plant and equipment (excluding those reported in discontinued operations) is as follows:

	January 2, 2004	January 3, 2003
Land	$ 403,000	$ 403,000
Buildings and improvements	15,877,000	13,900,000
Machinery and equipment	9,767,000	9,715,000
Office and computer equipment	4,657,000	4,665,000
Leasehold improvements	1,430,000	1,302,000
Construction-in-progress	993,000	1,651,000
	$33,127,000	$31,636,000

Maintenance and repairs are charged to expense as incurred; expenditures for renewals and betterments are capitalized. When assets are retired or otherwise disposed of, the property, plant and equipment accounts are relieved of cost and accumulated depreciation and any resulting gain or loss is credited or charged to income.

Goodwill

On December 29, 2001, the Company adopted FASB Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, which eliminates amortization of goodwill and requires an annual impairment test. SFAS No. 142 requires that impairment be tested at the reporting unit level, using a two-step approach. The first step determines if goodwill is impaired by comparing the fair value of the reporting unit as a whole to the book value. If a deficiency exists, the second step measures the amount of the impairment loss as the difference between the implied fair value of goodwill and its carrying value.

The following table presents the impact of SFAS No. 142 on net loss and net loss per share had the standard been in effect for the fiscal year ended December 28, 2001:

	2001
Reported net loss	$(5,072,000)
Pro forma adjustments	
Amortization of goodwill	248,000
Adjusted net loss	$(4,824,000)
Reported net loss per share	$(0.42)
Adjusted net loss per share	$(0.40)

As of January 2, 2004 and January 3, 2003, the carrying value of goodwill was $3.3 million (which is net of accumulated depreciation of $2.7 million) and of which $2.8 million relates to the manufacturing segment, $0.3 million relates to the supply segment, and the remainder $0.2 million relates to all other segments. None of the Company's goodwill was impaired in 2002 or 2003. In 2001, a portion of goodwill related to the Company's retail segment was impaired (see Note 9).

Long-Lived Assets

The Company continually evaluates whether events and circumstances have occurred that indicate that the remaining balance of long-lived assets to be held and used in the operations of the Company may be impaired and not be recoverable. In performing this evaluation, the Company uses an estimate of the related cash flows expected to result from the use of the asset and its eventual disposition. When this evaluation indicates the asset has been impaired, the Company will measure such impairment based on the asset's fair value and the amount of such impairment is charged to earnings (see Note 9).

Repurchase Agreements

Substantially all of the Company's independent dealers finance their purchases through "floor plan" arrangements under which a financial institution provides the dealer with a loan for the purchase price of the home and maintains a security interest in the home as collateral. In connection with a floor plan arrangement, the financial institution that provides the independent dealer financing customarily requires the Company to enter into a separate repurchase agreement with the financial institution, under which the Company is obligated, upon default by the independent dealer, to repurchase the homes at the Company's original invoice price less cost of all damaged/missing items and less certain curtailments, plus certain administrative and shipping expenses. The Company estimates and records a reserve for probable losses on dealer repurchases based on historical loss experience and the outstanding principal amount of floor plan financing.

Effective August 31, 2003, Wenco 21, LLC, a joint venture in which we held a 50% interest, was liquidated with the assets and liabilities of Wenco 21, LLC being transferred into a book entry reserve account held by 21st Mortgage Corporation, the other joint venture partner. In exchange for its pro rata distribution of the liquidated assets and liabilities, the Company received an interest (in the form of a revenue sharing agreement) in specified assets and liabilities that were transferred to 21st Mortgage Corporation. Under the terms of the revenue sharing agreement, the Company and 21st Mortgage Corporation will share equally in the profits and losses derived from the loans that comprised the Wenco 21, LLC portfolio. The Company is also obligated under the revenue sharing agreement to repurchase homes that were financed by Wenco 21 LLC, upon repossession, for 50% to 65% of the outstanding loan balance. At January 2, 2004, the Company had a reserve of $330,000 for future repurchase losses. The Company's contingent repurchase obligation under this commitment is approximately $11.6 million. At January 2, 2004, the Company has included approximately $1.0 million classified in other receivables in the consolidated balance sheet associated with this interest (in the form of a revenue sharing agreement) in specified assets and liabilities. At January 2, 2004, the carrying amount of loans in the Wenco 21 portfolio included in the reserve account was approximately $19.9 million. These loans collateralize approximately $19.1 million of the reserve account's obligations. The Company currently adjusts the carrying value of this investment for any income or losses incurred by the portfolio through earnings and its maximum exposure to loss as a result of its continuing involvement with the loan portfolio, assuming that 100% of the loans and underlying collateral becomes worthless, is approximately $12.6 million.

Computer Software Costs

The Company capitalizes external direct costs of materials and services, payroll and payroll-related costs for employees directly associated with developing or obtaining computer software. Capitalized costs of computer software developed or obtained for internal use are amortized on a straight-line basis over five years.

Volume Incentive Payable

The Company provides rebates to dealers based upon a predetermined formula applied to the volume of homes sold to the dealer during the year. Such rebates (reflected as a reduction of gross revenues) are recorded at the time sales to independent dealers are recognized.

Product Warranties

The Company warrants its products against certain manufacturing defects for a period of one year commencing at the time of retail sale. The estimated cost of such warranties is accrued at the time of sale to the independent dealer based on historical warranty costs incurred. Periodic adjustments to the accrual are made when events occur which indicate changes are necessary.

Litigation

The Company is a party to various legal proceedings incidental to its business. The Company typically provides a one-year warranty on new manufactured homes. The majority of these legal proceedings are claims related to warranty on manufactured homes or employment issues such as workers' compensation claims. Management believes that adequate reserves are maintained for such claims. In the opinion of management, after consultation with legal counsel, the ultimate liability, if any, with respect to these proceedings will not materially affect the financial position or results of operations of the Company; however, the ultimate resolution of these matters, which could occur within one year, could result in losses in excess of the amounts reserved.

Insurance Arrangements

The Company is partially self-insured for workers' compensation and health insurance claims. The Company purchases insurance coverage for all workers' compensation claims in excess of $350,000 per occurrence, and for all health-care claims in excess of $75,000 per occurrence (with an annual aggregate stop-loss limit of approximately $4.4 million for all claims). Amounts are accrued currently for the estimated costs of claims incurred, including related expenses. Management considers accrued liabilities for unsettled claims to be adequate; however, there is no assurance that the amounts accrued will not vary from the ultimate amounts incurred upon final disposition of all outstanding claims. As a result, periodic adjustments to the reserves will be made as events occur which indicate changes are necessary.

Fair Value of Financial Instruments

The carrying value of the Company's cash equivalents, accounts receivable, accounts payable, accrued expenses and notes payable approximates fair value because of the short-term nature of these instruments.

Revenue Recognition

The Company manufactures its homes pursuant to dealer orders, and sales to independent dealers and related transit costs are recognized upon delivery of the home to its dealers. Almost all of the Company's sales to its independent dealers are under floor-plan financing arrangements. Under these floor-plan financing arrangements, the Company bills the dealers upon delivery of the home and at the same time transfers title. Consistent with these arrangements, the Company typically does not allow independent dealers to cancel a purchase after manufacture by the Company has commenced. The Company carries insurance which covers possible damage to a home while on the Company's premises prior to shipment. During shipment, independent trucking companies transporting the Company's homes carry insurance to cover any damages that may occur.

Prior to the fourth quarter of 2001, the Company recorded retail home sales when customers signed installment contracts for the purchase of manufactured homes, the Company received the appropriate down payment, construction of the home was complete, and the home buyer had inspected and accepted the home. Effective with the beginning of the fourth quarter of 2001, the Company revised its criteria for recognizing revenue from retail operations to require that the buyers' purchases be fully funded, in addition to meeting all other purchase criteria previously required by the Company. The effect of the change in the Company's revenue recognition criteria was not material to the results of operations in 2001.

Stock-Based Compensation

Under fixed stock option plans, stock options may be granted to employees and directors at exercise prices that are equal to, less than, or greater than the fair market value of the Company's stock on the date of grant.

The Company accounts for all forms of stock compensation granted to directors and employees under APB Opinion No. 25, *Accounting for Stock Issued to Employees.* No compensation cost is recognized for options that are issued with exercise prices that equal or exceed the fair market value of the Company's common stock on the date of grant. Had compensation expense for the Company's stock options been determined under SFAS No. 123, *Accounting for Stock-Based Compensation*, the Company's net loss and net loss per share would have been as follows:

	2003	2002	2001
Net loss - as reported	$ (818,000)	$ (7,641,000)	$ (5,072,000)
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards	(234,000)	(191,000)	(350,000)
Net loss -pro forma	$ (1,052,000)	$ (7,832,000)	$ (5,422,000)
As reported - net loss per share	$(0.07)	$(0.63)	$(0.42)
Pro forma- net loss per share	$(0.09)	$(0.65)	$(0.45)

Shipping Fees and Costs

Shipping revenues are included as a component of net revenues. Total shipping costs, which were included in selling, general and administrative expenses were $6.1 million, $6.8 million and $7.2 million, during 2003, 2002 and 2001, respectively.

Dealer Interest Payments

The Company has agreements with certain independent dealers to reimburse them for their interest costs incurred in connection with floor-plan financing. Payments related to these agreements are treated as customer incentives and are classified as a reduction of revenues in the accompanying consolidated statements of operations. For the years ended January 2, 2004, January 3, 2003, and December 28, 2001, such incentives amounted to $649,000, $827,000 and $954,000, respectively.

Recent Accounting Pronouncements

In June 2001, the FASB issued SFAS 143, *Accounting for Asset Retirement Obligations.* SFAS 143 addresses financial accounting and reporting for obligations associated with the retirement of tangible long-lived assets and the associated asset retirement costs. It applies to legal obligations associated with the retirement of long-lived assets that result from the acquisition, construction, development and/or the normal operation of a long-lived asset, except for certain obligations of lessees. SFAS 143 is effective for financial statements issued for fiscal years beginning after June 15, 2002. The adoption of SFAS 143 did not have any impact in 2003 on the Company's financial position, results of operations or cash flows.

In January 2003, the FASB issued Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51* (FIN 46). In December 2003, the FASB modified FIN 46 to make certain technical corrections and address certain implementation issues that had arisen. FIN 46 addresses whether business enterprises must consolidate the financial statements of entities known as "variable interest entities". A variable interest entity is defined by FIN 46 to be a business entity that has one or both of the following characteristics: (1) the equity investment at risk is not sufficient to permit the entity to finance its activities without additional support from other parties, which is provided through other interests that will absorb some or all of the expected losses of the entity; and (2) the equity investors lack one or more of the following essential characteristics of a controlling financial interest: (a) direct or indirect ability to make decisions about the entity's activities through voting rights or similar rights, (b) the obligation to absorb the expected losses of the entity if they occur, which makes it possible for the entity to finance its activities, or (c) the right to receive the expected residual returns of the entity if they occur, which is the compensation for risk of absorbing expected losses. FIN 46 does not require consolidation by transferors to qualifying special purpose entities. For non-public companies with an interest in an entity that is subject to the interpretation and that is created after December 31, 2003, this interpretation is effective immediately. A non public enterprise must apply this interpretation to all entities that are subject to this interpretation by the beginning of the first annual period beginning after December 15, 2004. FIN 46 did not have an impact on the Company's financial position, results of operations or cash flows.

In July 2002, the FASB issued SFAS 146, *Accounting for Costs Associated with Exit or Disposal Activities.* SFAS 146 addresses the recognition, measurement and reporting of costs that are associated with exit and disposal activities, including restructuring activities that were previously accounted for pursuant to the guidance set forth in EITF No 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity*. SFAS 146 revises the accounting for certain lease termination costs and employee termination benefits, which are generally recognized in connection with restructuring activities. Adoption of this standard as of January 4, 2003 had no impact on the Company's financial position, results of operations or cash flows for the fiscal year ended January 2, 2004.

In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an Interpretation of FASB Statements No. 5, 57, and 107 and Rescission of FASB Interpretation No. 32* ("FIN 45"). FIN 45 clarifies the requirements of FASB Statement No. 5, *Accounting for Contingencies*, relating to a guarantor's accounting for, and disclosure of, specified types of guarantees. FIN 45 requires that upon issuance of a guarantee, the entity (i.e., the guarantor) must recognize a liability for the fair value of the obligation it assumes under that guarantee. The disclosure provisions of FIN 45 were effective for financial statements of interim or annual periods that ended after December 15, 2002. FIN 45's provisions for initial recognition and measurement must be applied (on a prospective basis) to guarantees issued or modified after December 31, 2002, irrespective of the guarantor's fiscal year end. The guarantor's previous accounting for guarantees that were issued before the date of FIN 45's initial application may not be revised or restated to reflect the effect of the recognition and measurement provisions of FIN 45. The Company has guarantees that are subject to the disclosure provisions of FIN 45. See Note 7 "Repurchase Agreements". The adoption of the prospective recognition and measurement aspects of FIN 45 did not have a material effect on the Company's financial position, results of operations or cash flows.

In May 2003, the FASB issued SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity*. This statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. This statement requires an issuer to classify a financial instrument issued in the form of shares that are mandatorily redeemable—that embodies an unconditional obligation requiring the issuer to redeem them by transferring its assets at a specified or determinable date—as a liability. The Company has no such securities outstanding and SFAS

No. 150 had no impact upon adoption in 2003.

Prior Year Reclassifications

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

4. Earnings Per Share

At January 2, 2004, January 3, 2003, and December 28, 2001, 1,684,079, 1,448,141, and 1,222,871 outstanding options were excluded from the weighted average number of common shares, on a diluted basis, because they were antidilutive.

5. Investments in Joint Ventures

The Company owns interests in four joint ventures all of which are accounted for using the equity method. The Company owns a 39% interest in WoodPerfect, Ltd., a manufacturing joint venture, which produces rafters used in the production of homes manufactured by the Company and others. The Company also owns 33% of WoodPerfect of Texas, Inc., which manufactures rafters used in the production of manufactured homes. The Company owns a 33% interest in Hillsboro Manufacturing, Inc., which manufactures laminate wallboard. The Company owns 33% of Lamraft LLP which is a real estate holding company that leases facilities to a third party. The Company formerly owned 33% of Ridge Pointe Mfg., LLC, which manufactures cabinet doors for sale to participants in the joint venture as well as third-party customers. The Ridge Pointe Mfg., LLC interest was sold in May 2002. The Company also formerly owned a 50% interest in Wenco 21, LLC, an entity that originates installment loans for the purchase of homes manufactured by the Company and others. Wenco 21, LLC was liquidated August 31, 2003 and the Company received, in exchange for its pro rata liquidating distribution in the net assets of Wenco 21, LLC, an interest in specified assets and liabilities that were transferred to the other joint venture partner, 21st Mortgage Corporation (see note 7).

The Company's investments in and advances to unconsolidated joint ventures amounted to $3.7 million and $4.3 million at January 2, 2004 and January 3, 2003, respectively. The Company's equity in the net earnings of these ventures was $0.3 million, $0.3 million and $0.4 million for the fiscal years ended January 2, 2004, January 3, 2003 and December 28, 2001, respectively. The Company received distributions from joint venture investments of $0.2 million, $0.2 million and $0.4 million for the fiscal years ended January 2, 2004, January 3, 2003 and December 28, 2001, respectively, Retained earnings at January 2, 2004 did not include any undistributed earnings of joint ventures and at January 3, 2003, included undistributed earnings of joint ventures of $0.7 million.

Since the liquidation of Wenco 21, LLC in August 2003, the Company's only remaining significant joint venture is WoodPerfect, Ltd. A summary of the joint ventures' financial information is as follows:

	As of	
	January 2, 2004	January 3, 2003
Current Assets	$ 4,141,000	$ 5,855,000
Non current assets	3,054,000	24,787,000
Total assets	7,195,000	30,642,000
Current liabilities	1,404,000	2,470,000
Non current liabilities	-	20,674,000
Total liabilities	1,404,000	23,144,000
Members' equity	5,791,000	7,498,000
Company equity investment	3,542,000	4,419,000

The January 2, 2004 summary balance sheet data reflect WoodPerfect, Ltd. only and the January 3, 2003 summary balance sheet data include WoodPerfect, Ltd and Wenco 21, LLC.

	For the Years Ended		
	January 2, 2004	January 3, 2003	December 28, 2001
Revenues	$ 34,578,000	$ 38,874,000	$ 37,291,000
Cost of sales	30,479,000	33,506,000	32,377,000
Gross profit	4,099,000	5,368,000	4,914,000

Operating income	779,000	983,000	912,000
Net income	803,000	986,000	879,000

The above summary income statement information for the fiscal year ended January 2, 2004 reflects WoodPerfect, Ltd. only and the summary income statement information for the years ended January 3, 2003 and December 28, 2001 includes WoodPerfect, Ltd and Wenco 21, LLC.

6. Income Taxes

The provision (benefit) for income taxes for the fiscal years ended January 2, 2004, January 3, 2003 and December 28, 2001 was as follows:

	2003	2002	2001
Continuing operations:			
Current (benefit) expense:			
Federal	$(330,000)	$(751,000)	$(304,000)
State	(57,000)	(49,000)	(45,000)
	(387,000)	(800,000)	(349,000)
Deferred (benefit) expense:			
Federal	-	-	304,000
State	-	-	45,000
	-	-	349,000
Total income tax benefit - continuing operations	(387,000)	(800,000)	-
Income tax benefit - discontinued operations	-	(4,500,000)	-
Total income tax expense (benefit)	$(387,000)	$(5,300,000)	$ -

The provision (benefit) for income taxes applicable to continuing operations differed from the amounts computed by applying the federal statutory rate of 34% in fiscal year 2003, 2002 and 2001 due to the following:

	2003	2002	2001
Federal taxes (benefit) at statutory rate on income from continuing operations before income taxes	$ (239,000)	$ 37,000	$ (679,000)
Change in valuation allowance unrelated to current period net operating losses	195,000	(171,000)	701,000
State taxes (benefit), net of federal income tax effect	20,000	(382,000)	(59,000)
Actual federal and state carryback refunds received in excess of benefits previously recognized	(417,000)	-	-
Goodwill amortization and other	54,000	(284,000)	37,000
	$(387,000)	$(800,000)	$ -

The deferred tax effects of temporary differences at January 2, 2004 and January 3, 2003 are as follows:

	January 2, 2004	January 3, 2003
Deferred tax benefits:		
Warranty accrual	$ 855,000	$ 793,000
Workers' compensation accrual	539,000	698,000
Accrued expenses	593,000	988,000
Federal and State operating loss carry forwards	1,824,000	2,597,000

Other	424,000	518,000
	4,235,000	5,594,000
Deferred tax liabilities:		
Depreciation	(426,000)	(381,000)
Other	(220,000)	(271,000)
	(646,000)	(652,000)
Net deferred tax benefits	3,589,000	4,942,000
Valuation allowance	(3,589,000)	(4,942,000)
Net deferred taxes	$ -	$ -

Because the Company has operated at a loss in recent fiscal years, management believes that under the provisions of SFAS 109, it is not appropriate to record income tax benefits on current losses and other net deductible temporary differences in excess of anticipated refunds of taxes previously paid. As a result, the Company has established valuation allowances against the net deferred tax benefits related to net operating loss carry forwards and other net deductible temporary differences between financial and taxable income. The valuation allowance may be reversed in future years if the Company returns to profitability.

At January 2, 2004, the Company had a federal net operating loss carry forward of approximately $2.9 million that expires in 2023. State net operating loss carryforwards amounting to approximately $20.9 million are available to offset future taxable income in Alabama and Texas and they expire at various dates in 2006 through 2023. During 2003, the state net operating loss deferred tax assets and the related valuation allowances were adjusted to eliminate carryforwards in states where the Company or its subsidiaries no longer conduct business. The tax loss generated in 2002 for federal income tax purposes has been carried back under the temporary 5 year net operating loss carry back rules applicable to 2002. Accordingly, the Company filed a carryback refund claim in 2003 and received a federal income tax refund of $5.3 million with respect to the 2002 net operating loss.

7. Commitments and Contingencies

Repurchase Agreements

Repurchases under dealer floor plan financing arrangements were $1.5 million, $2.0 million and $4.2 million for the years ended 2003, 2002, and 2001, respectively. Losses on homes repurchased under these agreements were $0.3 million, $0.5 million and $0.9 million for the years ended 2003, 2002 and 2001, respectively. At January 2, 2004, the Company had a reserve of $250,000 for future repurchase losses. At January 2, 2004, the Company's contingent repurchase liability under floor plan financing arrangements through independent dealers was approximately $39.2 million. The Company estimates and records a reserve for probable losses on dealer repurchases based on historical loss experience and the outstanding principal amount of floor plan financing.

Effective August 31, 2003, Wenco 21, LLC, a joint venture in which we held a 50% interest, was liquidated with the assets and liabilities of Wenco 21, LLC being transferred into a book entry reserve account held by 21st Mortgage Corporation, the other joint venture partner. In exchange for its pro rata distribution of the liquidated assets and liabilities, the Company received an interest (in the form of a revenue sharing agreement) in specified assets and liabilities that were transferred to 21st Mortgage Corporation. Under the terms of the revenue sharing agreement, the Company and 21st Mortgage Corporation will share equally in the profits and losses derived from the loans that comprised the Wenco 21, LLC portfolio. The Company is also obligated under the revenue sharing agreement to repurchase homes that were financed by Wenco 21 LLC, upon repossession, for 50% to 65% of the outstanding loan balance. At January 2, 2004, the Company had a reserve of $330,000 for future repurchase losses. The Company's contingent repurchase obligation under this commitment is approximately $11.6 million. Losses on homes repurchased under this obligation were not significant in fiscal 2003, 2002 and 2001. At January 2, 2004, the Company has included approximately $1.0 million classified in other receivables in the consolidated balance sheet associated with this interest (in the form of a revenue sharing agreement) in specified assets and liabilities. At January 2, 2004, the carrying amount of loans in the Wenco 21 portfolio included in the reserve account was approximately $19.9 million. These loans collateralize approximately $19.1 million of the reserve account's obligations. The Company currently adjusts the carrying value of this investment for any income or losses incurred by the portfolio through earnings and its maximum exposure to loss as a result of its continuing involvement with the loan portfolio, assuming that 100% of the loans and underlying collateral becomes worthless, is approximately $12.6 million.

Letters of Credit

The Company has provided a letter of credit for $0.6 million to a lending institution to provide additional wholesale floor plan resources for the Company's independent dealers and $0.1 million letter of credit to an insurance company to secure a bond to do

business in a particular state.

Operating Leases

The Company leases certain manufacturing facilities and retail sales centers under operating leases. Rent expense under all leases was $0.1 million for the year ended January 2, 2004, $0.7 million for the year ended January 3, 2003, and $1.1 million for the year ended December 28, 2001. Future minimum lease payments for each of the next five years at January 2, 2004 are not material.

Litigation

For the years ended January 2, 2004 and January 3, 2003, accrued litigation reserves (in addition to normal warranty and workmen's compensation claims reserves) were $0.8 million and $0.9 million, respectively.

8. Employee Benefit Plans

The Company has employee stock options outstanding under its 1993 Stock Option Plan and 2002 Incentive Award Plan. The 1993 Plan (which has now terminated, although outstanding options granted thereunder remain exercisable) authorized a total of 1,500,000 shares of Company common stock for issuance to key employees and advisors upon exercise of options, and the 2002 Plan authorizes a total of 1,000,000 shares for issuance upon exercise of options or in the form of restricted stock awards. The Company granted options to acquire 267,000, 220,000 and 319,250 shares of common stock in 2003, 2002 and 2001, respectively. The Company has not to date made any restricted stock awards. The exercise prices of the options under both plans approximated the fair market value of the Company's common stock at the date of grant. Of the 1,500,000 shares authorized and reserved for issuance under the 1993 Plan, at January 2, 2004, a total of 1,075,079 were subject to outstanding options, of which 1,070,079 were then exercisable. No further grants will be made under the 1993 Plan. Of the 1,000,000 shares authorized and reserved for issuance under the 2002 Plan, at January 2, 2004, a total of 477,750 were subject to outstanding options, of which 132,375 were exercisable on that date, and 522,250 remained available for issuance or grant.

The Company also maintains a stock option plan which authorizes a total of 100,000 shares of Company common stock for issuance to the Company's non-employee directors. Under the plan, outside directors each year are automatically granted options to purchase 3,750 shares. In 2003, 2002, and 2001, the Company granted options to acquire 18,750, 18,750 and 22,500 shares, respectively, of common stock to its non-employee directors. All shares available for under the plan had been reserved for outstanding grants as of mid-2002. The grants in 2002 included 6,250 shares under the plan, and 12,500 shares granted directly by the board on the same terms and conditions under the plan. The grants in 2003 of 18,750 options, were also granted by the board on the same terms and conditions as under the plan, but in light of then-applicable new NASDAQ listing requirements were granted conditionally, subject to shareholder approval. Effective as of January 15, 2004, the Company is no longer subject to NASDAQ listing requirements. The exercise prices of the options approximated the fair market value of the Company's common stock on the dates of grant. At January 2, 2004, options to purchase 100,000 shares were outstanding and exercisable under the plan, and 31,250 shares were reserved for issuance upon exercise of the options granted by the board of directors on the same terms and conditions as under the plan.

The following table summarizes the changes in the number of shares under option pursuant to the plans described above:

	January 2, 2004	Weighted Average Exercise Price	January 3, 2003	Weighted Average Exercise Price	December 28, 2001	Weighted Average Exercise Price
Outstanding at beginning of year	1,448,141	$2.75	1,222,871	$3.24	928,871	$3.83
Granted	285,750	1.62	238,750	2.11	341,750	1.61
Exercised	(10,000)	1.06	-	-	(875)	1.65
Forfeited	(39,812)	3.11	(13,480)	1.64	(46,875)	3.18
Outstanding at end of year	1,684,079	2.83	1,448,141	$2.75	1,222,871	$3.24
Exercisable at end of year	1,333,704	3.11	1,212,891	$3.27	1,091,684	$3.44
Weighted average fair value of options granted during the year		$1.37		$1.70		$1.03

The following table summarizes information about stock options outstanding at January 2, 2004:

Range of Exercise Prices	Options Outstanding: Number Outstanding at January 2, 2004	Options Outstanding: Weighted-Average Remaining Contractual Life	Options Outstanding: Weighted-Average Exercise Price	Options Exercisable: Number Exercisable January 2, 2004	Options Exercisable: Weighted-Average Exercise Price
Under 2.04	887,750	7.83	$ 1.41	655,750	$ 1.33
2.05 - 2.43	229,500	7.72	2.11	111,125	2.10
2.44 - 4.52	88,800	5.54	2.47	88,800	2.47
4.53 – 5.49	11,250	5.42	4.53	11,250	4.53
5.50 – 9.49	429,279	3.52	5.50	429,279	5.50
9.49 and above	37,500	3.46	10.80	37,500	10.80
	1,684,079	5.17	$ 2.83	1,333,704	$ 3.11

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model with the following weighted average assumptions used for grants in 2003, 2002 and 2001:

	2003	2002	2001
Dividend yield	0%	0%	0%
Expected volatility	83%	72%	74%
Risk-free interest rate	3.80%	5.10%	5.09%
Expected life (years)	10	10	10

Of the options granted in 2003, 58,750 options were exercisable immediately, 160,000 shares become exercisable equally over four years and the remainder become exercisable equally over two years. Vesting of the 2002 grants is 43,750 options vesting immediately, 100,000 shares exercisable equally over four years and the remainder vesting equally over two years. Vesting of the 2001 grants is 247,500 options vesting immediately and the remainder vesting equally over two years.

The Company offers a 401(k) retirement plan to employees having completed 90 days of service, whereby eligible employees may contribute up to 20% of their annual compensation subject to limitations by the Internal Revenue Service. The Company may match up to 100% of the employee contributions as limited by the Internal Revenue Service. For the years ended January 2, 2004, January 3, 2003 and December 28, 2001, Company contributions to the plan were $67,000, $75,000 and $84,000, respectively.

9. Impairment and Other Charges

During 2001, the Company recorded an impairment charge of $1.6 million for the remaining goodwill related to its retail operations segment. The charge was required because of continued losses at the two retail centers where the goodwill was recorded. This impairment charge is reported in continuing operations in the accompanying statement of operations because under the accounting rules governing discontinued operations in 2001 (APB 30), these retail centers did not meet the criteria for classification as discontinued operations. The Company also recorded a $602,000 impairment charge related to its investment in an unprofitable joint venture.

A summary of activity in the restructuring liability accounts (including amounts reported in discontinued operations) follows:

	2003	2002	2001
Restructuring liabilities at beginning of year	$ 344,000	$ 29,000	$ 227,000
Exit costs accrued	-	832,000	-
Employee termination costs accrued	-	103,000	-
Payments charged to the liability accounts	(334,000)	(620,000)	(198,000)
Restructuring liabilities at end of year	$ 10,000	$ 344,000	$ 29,000

A substantial portion of the impairment and other charges recognized in 2001 and 2002 involved the write-down of assets and did not

require cash payments.

A summary of non-cash related components of the special charges in 2002 and 2001 follows:

	2002	2001
Impairment of facilities	$ 429,000	$ -
Impairment of intangible assets	-	1,638,000
Inventory write down	3,584,000	-
Leasehold impairments	248,000	-
Other	462,000	602,000
Total non-cash charges	$ 4,723,000	$ 2,240,000
These non-cash charges are reflected in:		
Continuing operations	$ -	$ 2,240,000
Discontinued operations	$ 4,723,000	$ -

10. Shareholder Rights Plan

On October 10, 2003, the Company adopted a shareholder rights plan and designated 40,000 of its 1,000,000 authorized shares of preferred stock as Series A Junior Participating Preferred Stock (the "Preferred Stock"). In connection with this rights plan, the Company declared a dividend of one preferred share purchase right (a "Right") for each outstanding share of common stock, payable to the stockholders of record as of November 3, 2003. Each Right entitles the holder to purchase one one-thousandth (1/1000) of a share of the Preferred Stock, which has economic terms similar to that of one share of the Company's common stock, for $25.00, subject to adjustment.

In the event that any person or group acquires 15% or more of the Company's outstanding common stock, each holder of a Right (other than the acquiring person or group) will be entitled to receive, upon payment of the exercise price, shares of common stock (or other equivalent security such as the Preferred Stock) having a market value equal to twice the exercise price, unless the Board redeems the Rights for $.001 per right or exchanges the Rights for one common share or one one-thousandth of a share of Preferred Stock.

Existing holdings of 15% or more of the Company's common shares by persons directly or indirectly will not cause the rights to be exercisable, nor entitle the holders of rights to purchase additional shares of the Company, unless such holder acquires additional shares or converts such holdings from indirect to direct beneficial ownership.

The purchase price payable and number of shares of preferred stock issuable upon exercise of the rights are subject to customary adjustments to prevent dilution. Rights do not have voting rights and the holder has no rights as a stockholder until rights are exercised. The terms of the rights may be amended by the Board in its discretion, without the consent of the holders of the rights. The rights expire on October 10, 2013 unless earlier redeemed or exchanged.

Each one-thousandth share of preferred stock purchased upon exercise of the rights has rights and preferences substantially equivalent to those of one common share and shares are not redeemable. Each share of preferred stock will be entitled to a minimum preferential quarterly dividend payment of $1 per share and an aggregate dividend of 1,000 times the dividend declared per common share. In the event of liquidation, the holders of the Preferred Stock will be entitled to a minimum preferential liquidation payment of $1,000 per share and an aggregate payment of 1,000 times the payment made per common share. Each share of preferred stock will have 1,000 votes, voting together with the common shares. In the event of any merger or exchange transaction, holders of the preferred stock will be entitled to receive 1,000 times the amount received per common share.

In connection with the rights plan, the board of directors approved change of control severance agreements with certain of its key executives, and amended outstanding stock option agreements to provide that participants will be fully and immediately vested in the event of a change in control.

11. Segment and Related Information

The Company has three reportable segments: manufacturing, retail operations and component supply. The manufacturing segment produces manufactured homes at five production facilities for sale to independent and company-owned retail centers. Although each manufacturing facility is an operating segment, they are aggregated into one segment for reporting purposes because they produce similar products using similar production techniques and they sell their products to the same class of customer. In

addition, they are subject to the same regulatory environment and their economic characteristics (measured on terms of profitability) are similar. The retail operations segment sells homes to retail customers which have been produced by the Company's manufacturing segment and various other manufacturers. The component supply segment sells various supply products to the Company's manufacturing segment and to third-party customers.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. The Company evaluates performance based on total (external and intersegment) revenues, gross profit and segment operating income. The Company accounts for intersegment sales and transfers as if the sales or transfers were to third-parties, at current market prices. The Company does not allocate income taxes to its segments. The Company's reportable segments are strategic business units that offer different products and services. They are managed separately because each business requires different operating and marketing strategies.

Revenue from segments below the quantitative thresholds are attributable to two other operating segments of the Company which include a trucking business (closed in July 2001) and a small insurance business. These segments have never met the quantitative thresholds for determining reportable segments. The Corporate segment does not generate any revenues, but does incur certain administrative expenses that are not allocated to reportable segments.

The following tables present information about segment revenues, gross profit, and operating profit or loss (dollars in thousands):

	2003	2002	2001
Revenues:			
Manufacturing	$121,145,000	$132,862,000	$ 133,640,000
Retail Operations	4,059,000	9,234,000	10,487,000
Component Supply	24,714,000	24,632,000	23,342,000
All Other	81,000	289,000	3,439,000
Eliminations for intersegment revenues:			
Manufacturing	(2,105,000)	(6,735,000)	(18,395,000)
Component Supply	(21,537,000)	(21,768,000)	(20,327,000)
All Other	-	-	(3,081,000)
Total revenues	$126,357,000	$138,514,000	$ 129,105,000
Gross profit (loss):			
Manufacturing	$ 18,002,000	$ 21,195,000	$ 21,324,000
Retail Operations	1,104,000	1,774,000	3,940,000
Component Supply	1,474,000	2,187,000	2,065,000
All Other	(265,000)	(672,000)	2,674,000
Eliminations	105,000	1,144,000	(3,321,000)
Gross profit	$ 20,420,000	$ 25,628,000	$ 26,682,000
Segment operating income (loss) before tax:			
Manufacturing	$ 2,553,000	$ 3,971,000	$ 5,027,000
Retail Operations	(517,000)	(2,474,000)	(4,592,000)
Component Supply	629,000	1,346,000	1,114,000
All Other	113,000	100,000	137,000
Eliminations	105,000	1,144,000	(240,000)
Total segment operating income	2,883,000	4,087,000	1,446,000
Income / expenses not allocated to segments:			
Corporate expenses	(3,586,000)	(3,978,000)	(3,444,000)
Tax benefit	387,000	800,000	-
Income (loss) from continuing operations	$ (316,000)	$ 909,000	$ (1,998,000)

A summary of segment assets, depreciation and amortization, and capital additions for the years ended 2003, 2002, and 2001, is as follows for continued operations:

	Segment Assets	Depreciation and Amortization	Capital Additions
2003:			
Manufacturing	$ 16,914,000	$ 916,000	$ 349,000
Retail Operations	3,434,000	87,000	227,000
Component Supply	4,216,000	162,000	625,000
Total reportable segments	24,564,000	1,165,000	1,201,000
All Other	201,000	-	-
Corporate (unallocated)	25,220,000	1,373,000	594,000
Eliminations	(842,000)	-	-
Discontinued operations	101,000	-	-
Consolidated	$ 49,244,000	$ 2,538,000	$ 1,795,000
2002:			
Manufacturing	$ 16,561,000	$ 852,000	$ 277,000
Retail Operations	4,368,000	114,000	9,000
Component Supply	3,583,000	199,000	999,000
Total reportable segments	24,512,000	1,165,000	1,285,000
All Other	9,000	-	-
Corporate (unallocated)	26,725,000	1,498,000	738,000
Eliminations	(1,006,000)	-	-
Discontinued operations	1,488,000	-	-
Consolidated	$ 51,728,000	$ 2,663,000	$ 2,023,000
2001:			
Manufacturing	$ 19,252,000	$ 925,000	$ 608,000
Retail Operations	6,748,000	238,000	68,000
Component Supply	3,601,000	234,000	2,000
Total reportable segments	29,601,000	1,397,000	678,000
All Other	48,000	2,000	-
Corporate (unallocated)	17,654,000	1,517,000	394,000
Eliminations	(3,102,000)	-	-
Discontinued operations	29,458,000	-	-
Consolidated	$ 73,659,000	$ 2,916,000	$ 1,072,000

12. Concentration of Credit Risk

Financial instruments which potentially subject the Company to concentration of credit risk, consist principally of temporary cash investments and trade receivables. The Company places its temporary cash investments with credit-worthy, high-quality financial institutions.

The Company's customer base is concentrated in the manufactured home industry. Customers are located in the southeastern and southwestern United States. The Company requires no collateral or other security to support customer receivables. An allowance for doubtful accounts has been established for potential credit losses.

13. Related Party Transactions

The Company sold homes to a development company affiliated with certain stockholders who also were executive officers of the Company. During the years ended January 2, 2004, January 3, 2003, and December 28, 2001, such sales amounted to $98,000, $42,000, and $52,000, respectively.

The Company purchased a lake house and boat from the chairman of the Company in 2003 for $230,000 to be used for corporate promotional purposes.

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14. Summary of Unaudited Quarterly Financial Data

Unaudited quarterly financial information is as follows:

	Quarter Ended				Year Ended
	April 4, 2003	July 4, 2003	October 3, 2003	January 2, 2004	January 2, 2004
Net revenues	$28,044,000	$31,102,000	$33,993,000	$33,218,000	$126,357,000
Gross profit	3,808,000	5,490,000	6,054,000	5,068,000	20,420,000
Income taxes (benefit)	-	(330,000)	(87,000)	30,000	(387,000)
Income (loss) from continuing operations	(1,547,000)	575,000	656,000	-	(316,000)
Income (loss) from discontinued operations	136,000	(229,000)	(53,000)	(356,000)	(502,000)
Net income (loss)	(1,411,000)	346,000	603,000	(356,000)	(818,000)
Income (loss) per share from:					
Continuing operations	$ (0.13)	$ 0.05	$ 0.05	$ -	$ (0.03)
Discontinued operations	0.01	(0.02)	(0.00)	(0.03)	(0.04)
Net income (loss)	$ (0.12)	$ 0.03	$ 0.05	$ (0.03)	$ (0.07)
Weighted average number of common shares outstanding	12,133,865	12,140,643	12,143,865	12,143,865	12,140,541

	Quarter Ended				Year Ended
	March 29, 2002	June 28, 2002	September 27, 2002 (1)	January 3, 2003 (1)	January 3, 2003
Net revenues	$31,105,000	$39,656,000	$34,522,000	$33,231,000	$138,514,000
Gross profit	5,718,000	7,755,000	6,969,000	5,186,000	25,628,000
Income tax benefit	-	-	-	800,000	800,000
Income (loss) from continuing operations	105,000	1,272,000	647,000	(1,115,000)	909,000
Loss from discontinued operations (2) (3)	(903,000)	(1,017,000)	(3,514,000)	(3,116,000)	(8,550,000)
Net income (loss)	(798,000)	255,000	(2,867,000)	(4,231,000)	(7,641,000)
Income (loss) per share from:					
Continuing operations	$ 0.01	$ 0.10	$ 0.05	$ (0.09)	$ 0.07
Discontinued operations	(0.07)	(0.08)	(0.29)	(0.26)	(0.70)
Net income (loss)	$ (0.06)	$ 0.02	$ (0.24)	$ (0.35)	$ (0.63)
Weighted average number of common shares outstanding	12,133,865	12,133,865	12,133,865	12,133,865	12,133,865

(1) In the third quarter of 2002 the Company made the decision to close seven retail centers and in the fourth quarter of 2002 the Company closed an additional four retail centers and sold its Wenco Finance loan portfolio.

(2) In the third quarter of 2002, the Company closed seven retail centers. The Company recognized a loss on discontinued operations in the third quarter of $3.3 million (net of a tax benefit of $1.8 million) or $0.27 per share consisting of operating losses during the quarter, a write-down of the carrying value of unsold homes in current retail inventory, severance, exit costs associated with rental commitments, and write-down of equipment and leasehold improvements.

(3) In the fourth quarter of 2002, the Company sold its Wenco loan portfolio. The Company recognized a pre-tax loss on discontinued operations in the fourth quarter from the sale of the loan portfolio of $5.7 million.

Report of Ernst & Young LLP, Independent Auditors

The Board of Directors and Shareholders
Southern Energy Homes, Inc.

We have audited the accompanying consolidated balance sheets of Southern Energy Homes, Inc. and Subsidiaries as of January 2, 2004 and January 3, 2003, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three fiscal years in the period ended January 2, 2004. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Southern Energy Homes, Inc. and Subsidiaries at January 2, 2004 and January 3, 2003, and the results of their operations and their cash flows for each of the three fiscal years in the period ended January 2, 2004, in conformity with accounting principles generally accepted in the United States.

As discussed in Note 3 to the consolidated financial statements, in fiscal 2002 the Company changed its method of accounting for goodwill.

/s/ ERNST & YOUNG LLP

Birmingham, Alabama
February 20, 2004

Statement of Management's Responsibility

Southern Energy Homes, Inc. and subsidiaries

The consolidated financial statements and related information herein were prepared by the Company and were based on accounting principles generally accepted in the United States, appropriate in the circumstances to reflect in all material respects the consolidated financial position of the Company as of January 2, 2004 and January 3, 2003, and the consolidated results of its operations and its cash flows for each of the years ended January 2, 2004 and January 3, 2003 and December 28, 2001. The financial information presented elsewhere in this Annual Report has been prepared in a manner consistent with the financial statement disclosures.

Management is responsible for the reliability and integrity of these statements. In meeting this responsibility, management maintains an accounting system and related internal controls to provide reasonable assurance that the financial records are reliable for preparing financial statements and maintaining accountability for assets. The Company's systems and controls are also designed to provide reasonable assurance that assets are safeguarded and those transactions are executed in accordance with management's authorizations and recorded properly.

The Board of Directors has appointed an Audit Committee that meets periodically with management and the independent public accountants.

Ernst & Young LLP has audited the consolidated financial statements in accordance with auditing standards generally accepted in the United States and their report appears herein.

Controls and Procedures

The Company has evaluated the effectiveness of its disclosure controls and procedures. The evaluation was performed under the supervision and with the participation of the Company's management. Based on this evaluation, management has concluded that the disclosure controls and procedures are effective in ensuring that all material information disclosed in this annual report has been communicated to them in a manner appropriate to allow timely decisions regarding disclosure. There have been no significant changes in the Company's internal controls, or in other factors that could significantly affect internal controls, including any corrective actions with regard to significant deficiencies and material weaknesses with regard to the Company's internal controls, subsequent to that evaluation.

Directors and Executive Officers of the Company

Information concerning directors is contained in the Company's proxy statement for the annual meeting of stockholders to be held on May 18, 2004.

Information concerning executive officers of the Company is contained in the text appearing under the caption "Business - Executive Officers."

Executive Compensation

Information about executive compensation is contained in the Company's proxy statement for the annual meeting of stockholders to be held on May 18, 2004, and is incorporated herein by reference.

Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information about security ownership is contained in the Company's proxy statement for the annual meeting of stockholders to be held on May 18, 2004.

Certain Relationships and Related Transactions

Information about certain relationships and transactions is contained in the Company's proxy statement for the annual meeting of stockholders to be held on May 18, 2004.

Principal Accountant Fees and Services

Information about principal accountant fees and services is contained in the Company's proxy statement for the annual meeting of stockholders to be held on May 18, 2004.