

INGLES MARKETS INC
Form 10-Q/A
November 24, 2003

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q/A

Amendment No. 2

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

For the quarterly period ended March 29, 2003

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 0-14706.

INGLES MARKETS, INCORPORATED

(Exact name of registrant as specified in its charter)

North Carolina

56-0846267

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer
Identification No.)

P.O. Box 6676, Asheville NC

28816

(Address of principal executive offices)

(Zip Code)

(828) 669-2941

Registrant's telephone number, including area code

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o.

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

As of May 1, 2003, the Registrant had 10,499,998 shares of Class A Common Stock, \$.05 par value per share, outstanding and 12,391,966 shares of Class B Common Stock, \$.05 par value per share, outstanding.

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INGLES MARKETS, INCORPORATED

INTRODUCTORY NOTE**Form 10-Q/A for the Three and Six Months Ended March 29, 2003**

This Amendment on Form 10-Q/A is being filed to restate certain amounts (see Note J, Critical Accounting Policies, and Managements Discussion and Analysis) and to revise disclosure and presentation of the Company's Consolidated Financial Statements for the three and six-month periods ended March 29, 2003.

In light of recent interpretations of EITF 02-16, we reviewed our method of recognizing slotting fees and other vendor allowances in accordance with EITF 02-16. This review led us to revise our methodology for recognizing this consideration. Since we had previously filed the March 2003 Form 10-Q, the option of recording the impact of EITF No. 02-16 as a cumulative effect of an accounting change was not available.

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Part I. Financial Information

Item 1. Financial Statements

INGLES MARKETS, INCORPORATED AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

ASSETS

| | MARCH 29, 2003 (UNAUDITED) (Restated)* | SEPTEMBER 28, 2002 (NOTE) |
|----------------------------|---|--|
| Current Assets: | | |
| Cash | \$ 15,083,331 | \$ 46,900,305 |
| Receivables | 31,582,339 | 34,822,934 |
| Inventories | 192,237,744 | 190,399,350 |
| Other | 6,753,658 | 5,706,754 |
| | 245,657,072 | 277,829,343 |
| Property and Equipment Net | 737,295,727 | 723,219,548 |
| Other Assets | 13,332,118 | 13,342,315 |
| | \$996,284,917 | \$ 1,014,391,206 |

NOTE: The balance sheet at September 28, 2002 has been derived from the audited financial statements at that date.

* Certain amounts have been restated in conjunction with the change in interpretation of EITF 02-16. See Note J for further details. See notes to unaudited interim financial statements.

Table of Contents**INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS (CONCLUDED)****LIABILITIES AND STOCKHOLDERS' EQUITY**

| | MARCH 29, 2003 (UNAUDITED) (Restated)* | SEPTEMBER 28, 2002 (NOTE) |
|---|---|--|
| Current Liabilities: | | |
| Short-term loans and current portion of long-term debt | \$ 43,354,376 | \$ 47,307,046 |
| Accounts payable, accrued expenses and current portion of other long-term liabilities | 130,347,212 | 139,123,085 |
| Total Current Liabilities | 173,701,588 | 186,430,131 |
| Deferred Income Taxes | 34,314,578 | 36,914,578 |
| Long-Term Debt | 549,448,623 | 549,324,487 |
| Other Long-Term Liabilities | 1,855,700 | 3,163,162 |
| Total Liabilities | 759,320,489 | 775,832,358 |
| Stockholders' Equity | | |
| Preferred stock, \$.05 par value; 10,000,000 shares authorized; no shares issued | | |
| Common stocks: | | |
| Class A, \$.05 par value; 150,000,000 shares authorized; 10,451,448 shares issued and outstanding March 29, 2003; 10,189,807 shares issued and outstanding September 28, 2002 | 522,572 | 509,490 |
| Class B, \$.05 par value; 100,000,000 shares authorized; 12,391,966 shares issued and outstanding March 29, 2003; 12,597,932 shares issued and outstanding September 28, 2002 | 619,599 | 629,897 |
| Paid-in capital in excess of par value | 100,698,822 | 100,148,857 |
| Retained earnings | 135,123,435 | 137,270,604 |
| Total Stockholders' Equity | 236,964,428 | 238,558,848 |
| Total Liabilities and Stockholders' Equity | \$ 996,284,917 | \$ 1,014,391,206 |

NOTE: The balance sheet at September 28, 2002 has been derived from the audited financial statements at that date.

* Certain amounts have been restated in conjunction with the change in interpretation of EITF 02-16. See Note J for further details. See notes to unaudited interim financial statements.

Table of Contents**INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)**

| | THREE MONTHS ENDED | |
|---|----------------------------------|-------------------|
| | MARCH 29, 2003 (Restated)* | MARCH 30, 2002 |
| Net sales | \$ 489,382,957 | \$ 493,155,353 |
| Cost of goods sold | 362,177,152 | 360,679,833 |
| Gross profit | 127,205,805 | 132,475,520 |
| Operating and administrative expenses | 115,823,020 | 116,302,291 |
| Rental income, net | 2,349,080 | 2,361,910 |
| Income from operations | 13,731,865 | 18,535,139 |
| Other income, net | 1,687,356 | 481,456 |
| Income before interest and income taxes | 15,419,221 | 19,016,595 |
| Interest expense | 12,511,137 | 13,671,342 |
| Income before income taxes | 2,908,084 | 5,345,253 |
| Income taxes: | | |
| Current | 3,150,000 | 3,250,000 |
| Deferred | (2,062,000) | (1,200,000) |
| | 1,088,000 | 2,050,000 |
| Net income | \$ 1,820,084 | \$ 3,295,253 |
| Per share amounts: | | |
| Basic earnings per common share | \$ 0.08 | \$ 0.15 |
| Diluted earnings per common share | \$ 0.08 | \$ 0.14 |
| Cash dividends per common share: | | |
| Class A Common Stock | \$ 0.165 | \$ 0.165 |
| Class B Common Stock | \$ 0.150 | \$ 0.150 |

* Certain amounts have been restated in conjunction with the change in interpretation of EITF 02-16. See Note J for further details. See notes to unaudited interim financial statements.

Table of Contents**INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED)**

| | SIX MONTHS ENDED | |
|---|----------------------------------|-----------------------------------|
| | March 29, 2003 (Restated)* | March 30, 2002 (Restated)** |
| Net sales | \$ 984,499,148 | \$ 992,599,610 |
| Cost of goods sold | 727,111,948 | 732,088,811 |
| Gross profit | 257,387,200 | 260,510,799 |
| Operating and administrative expenses | 231,159,848 | 230,862,986 |
| Rental income, net | 4,500,261 | 4,756,438 |
| Income from operations | 30,727,613 | 34,404,251 |
| Other income, net | 2,348,965 | 3,157,429 |
| Income before interest and income taxes | 33,076,578 | 37,561,680 |
| Interest expense | 25,243,265 | 25,719,116 |
| Income before income taxes | 7,833,313 | 11,842,564 |
| Income taxes: | | |
| Current | 5,300,000 | 7,130,000 |
| Deferred | (2,462,000) | (2,700,000) |
| | 2,838,000 | 4,430,000 |
| Net income | \$ 4,995,313 | \$ 7,412,564 |
| Per share amounts | | |
| Basic earnings per common share | \$ 0.22 | \$ 0.33 |
| Diluted earnings per common share | \$ 0.22 | \$ 0.32 |
| Cash dividends per common share: | | |
| Class A Common Stock | \$ 0.33 | \$ 0.33 |
| Class B Common Stock | \$ 0.30 | \$ 0.30 |

* Certain amounts have been restated in conjunction with the change in interpretation of EITF 02-16. See Note J for further details.

** Certain amounts have been reclassified for the provisions of FAS 145. See Note J for further details.
See notes to unaudited interim financial statements.

Table of Contents**INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS EQUITY (UNAUDITED)**

SIX MONTHS ENDED MARCH 29, 2003 AND MARCH 30, 2002

| | CLASS A COMMON STOCK | | CLASS B COMMON STOCK | | PAID-IN CAPITAL IN EXCESS OF PAR VALUE | RETAINED EARNINGS (Restated)* | TOTAL (Restated)* |
|------------------------------------|-------------------------|-------------------|-------------------------|-------------------|---|-------------------------------------|-----------------------|
| | SHARES | AMOUNT | SHARES | AMOUNT | | | |
| Balance, September 29, 2001 | 10,005,107 | \$ 500,255 | 12,634,432 | \$ 631,722 | \$ 98,595,411 | \$ 136,772,824 | \$ 236,500,212 |
| Net income | | | | | | 7,412,564 | 7,412,564 |
| Cash dividends | | | | | | (7,098,834) | (7,098,834) |
| Exercise of stock options | 120,300 | 6,015 | | | 1,260,354 | | 1,266,369 |
| Common stock conversions | 225 | 12 | (225) | (12) | | | |
| Balance, March 30, 2002 | 10,125,632 | \$ 506,282 | 12,634,207 | \$ 631,710 | \$ 99,855,765 | \$ 137,086,554 | \$ 238,080,311 |
| Balance, September 28, 2002 | 10,189,807 | \$ 509,490 | 12,597,932 | \$ 629,897 | \$ 100,148,857 | \$ 137,270,604 | \$ 238,558,848 |
| Net income | | | | | | 4,995,313 | 4,995,313 |
| Cash dividends | | | | | | (7,142,482) | (7,142,482) |
| Exercise of stock options | 55,675 | 2,784 | | | 549,965 | | 552,749 |
| Common stock conversions | 205,966 | 10,298 | (205,966) | (10,298) | | | |
| Balance, March 29, 2003 | 10,451,448 | \$ 522,572 | 12,391,966 | \$ 619,599 | \$ 100,698,822 | \$ 135,123,435 | \$ 236,964,428 |

* Certain amounts have been restated in conjunction with the change in interpretation of EITF 02-16. See Note J for further details. See notes to unaudited interim financial statements.

Table of Contents**INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED)**

| | SIX MONTHS ENDED | |
|---|----------------------------------|----------------------|
| | MARCH 29, 2003 (Restated)* | MARCH 30, 2002 |
| Cash Flows from Operating Activities: | | |
| Net income | \$ 4,995,313 | \$ 7,412,564 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization expense | 25,114,325 | 23,952,015 |
| Amortization of deferred gain on sale/leasebacks | (423,591) | (423,590) |
| Gains on disposals of property and equipment | (1,137,596) | (1,720,868) |
| Receipt of advance payments on purchases contracts | 750,000 | 2,587,576 |
| Recognition of advance payments on purchases contracts | (1,739,669) | (1,684,624) |
| Decrease in deferred income taxes | (2,462,000) | (2,700,000) |
| Decrease (increase) in receivables | 3,240,595 | (2,305,508) |
| (Increase) decrease in inventory | (1,838,394) | 5,936,639 |
| (Increase) decrease in other assets | (1,762,955) | 1,850,506 |
| Decrease in accounts payable and accrued expenses | (10,718,740) | (9,625,350) |
| Net Cash Provided by Operating Activities | 14,017,288 | 23,279,360 |
| Cash Flows from Investing Activities: | | |
| Proceeds from sales of property and equipment | 1,585,991 | 6,997,671 |
| Capital expenditures | (36,977,049) | (15,419,323) |
| Net Cash Used by Investing Activities | (35,391,058) | (8,421,652) |
| Cash Flows from Financing Activities: | | |
| Proceeds from issuance of long-term debt and advances on lines of credit | 20,565,000 | 272,280,684 |
| Debt issuance costs | (24,937) | (9,685,354) |
| Principal payments on long-term debt | (24,393,534) | (195,623,810) |
| Proceeds from exercise of stock options | 552,749 | 1,266,369 |
| Dividends paid | (7,142,482) | (7,098,834) |
| Net Cash (Used) Provided by Financing Activities | (10,443,204) | 61,139,055 |
| Net (Decrease) Increase in Cash | (31,816,974) | 75,996,763 |
| Cash at beginning of period | 46,900,305 | 12,434,897 |
| Cash at End of Period | \$ 15,083,331 | \$ 88,431,660 |

* Certain amounts have been restated in conjunction with the change in interpretation of EITF 02-16. See Note J for further details. See notes to unaudited interim financial statements.

Table of Contents**INGLES MARKETS, INCORPORATED AND SUBSIDIARIES****NOTES TO UNAUDITED INTERIM FINANCIAL STATEMENTS**

Six Months Ended March 29, 2003 and March 30, 2002

A. BASIS OF PREPARATION

In the opinion of management, the accompanying unaudited interim financial statements contain all adjustments necessary to present fairly the Company's financial position as of March 29, 2003, and the results of operations, changes in stockholders' equity and cash flows for the three-month and six-month periods ended March 29, 2003 and March 30, 2002. The adjustments made are of a normal recurring nature. Certain information and footnote disclosures normally included in the annual financial statements prepared in accordance with accounting principles generally accepted in the United States have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission for Form 10-Q. It is suggested that these unaudited interim financial statements be read in conjunction with the audited financial statements and the notes thereto included in the Annual Report on Form 10-K for the year ended September 28, 2002 filed by the Company under the Securities Exchange Act of 1934 on December 10, 2002.

The results of operations for the three-month and six-month periods ended March 29, 2003 are not necessarily indicative of the results to be expected for the full fiscal year.

Certain amounts for the three-month and six-month periods ended March 30, 2002 have been reclassified for comparative purposes.

B. ALLOWANCE FOR DOUBTFUL ACCOUNTS

Receivables are presented net of an allowance for doubtful accounts of \$565,854 and \$479,113 at March 29, 2003 and September 28, 2002, respectively.

C. ACCOUNTS PAYABLE, ACCRUED EXPENSES AND CURRENT PORTION OF OTHER LONG-TERM LIABILITIES

Accounts payable, accrued expenses and current portion of other long-term liabilities consist of the following:

| | March 29, 2003 | September 28, 2002 |
|--|---------------------------|-------------------------------|
| Accounts payable-trade | \$ 78,551,868 | \$ 82,651,435 |
| Property, payroll, and other taxes payable | 10,370,475 | 12,362,475 |
| Salaries, wages and bonuses payable | 10,169,902 | 11,985,095 |
| Self-insurance reserves | 7,088,230 | 6,565,623 |
| Interest | 9,619,053 | 9,569,420 |
| Other | 14,547,684 | 15,989,037 |
| | \$ 130,347,212 | \$ 139,123,085 |

Self-insurance reserves are established for workers' compensation and employee group medical and dental benefits based on claims filed and estimates of claims incurred but not reported. The Company is insured for covered costs in excess of \$350,000 per occurrence for workers' compensation and \$175,000 per covered person for medical care benefits for a policy year. Employee insurance expense, including workers' compensation and medical care benefits, net of employee contributions, totaled \$5.0 million and \$5.4 million for the three-month periods ended March 29, 2003 and March 30, 2002, respectively.

For the six-month periods ended March 29, 2003 and March 30, 2002, employee insurance expense, net of employee contributions, totaled \$9.7 million and \$10.5 million, respectively.

D. LONG-TERM DEBT

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On December 11, 2001 the Company closed an offering of \$250 million principal amount of senior subordinated notes due in 2011. The notes bear an annual interest rate of 8-7/8% and were issued at a discount to yield 9%. A portion of the proceeds was used to repay \$170.0 million in existing indebtedness.

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In conjunction with the issuance of the notes, the Company renegotiated its lines of credit, extending the maturity dates and increasing available lines of credit from \$130 million to \$145 million. Of the \$145 million of committed lines of credit, \$130 million matures in October 2004 and \$15 million matures in October 2003.

During the six months ended March 29, 2003, the Company obtained \$20.6 million in net advances on lines of credit at interest rates less than the prime rate. The proceeds of the loans were used to fund capital expenditures and for general corporate purposes.

E. DIVIDENDS

The Company paid cash dividends of \$.165 for each share of Class A Common Stock and \$.15 for each share of Class B Common Stock on January 15, 2003 and October 9, 2002 to stockholders of record on January 6, 2003 and October 1, 2002, respectively.

F. SUPPLEMENTARY CASH FLOW INFORMATION

Cash paid for interest and taxes is as follows:

| | Six Months Ended | |
|--------------------------------------|---------------------------|---------------------------|
| | March 29, 2003 | March 30, 2002 |
| Interest (net of amount capitalized) | \$25,193,632 | \$20,698,551 |
| Income taxes | \$ 6,165,973 | \$ 6,574,328 |

G. EARNINGS PER COMMON SHARE

The following tables set forth the computation of basic and diluted earnings per share for the three-month periods indicated:

| | Three Months Ended | |
|---|---------------------------|---------------------------|
| | March 29, 2003 | March 30, 2002 |
| BASIC: | | |
| Net income | \$ 1,820,084 | \$ 3,295,253 |
| Weighted average number of common shares outstanding | 22,827,745 | 22,694,779 |
| Basic earnings per common share | \$.08 | \$.15 |
| DILUTED: | | |
| Net income | \$ 1,820,084 | \$ 3,295,253 |
| Weighted average number of common shares and common stock equivalent shares outstanding | 23,034,349 | 23,071,127 |
| Diluted earnings per common share item | \$.08 | \$.14 |

The following table sets forth the computation of basic and diluted earnings per share for the six-month periods indicated:

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| | Six Months Ended | |
|---|---------------------|-------------------|
| | March 29, 2003 | March 30, 2002 |
| BASIC: | | |
| Net income | \$ 4,995,313 | \$ 7,412,564 |
| Weighted average number of common shares outstanding | 22,835,580 | 22,670,015 |
| Basic earnings per common share | \$.22 | \$.33 |
| DILUTED: | | |
| Net income | \$ 4,995,313 | \$ 7,412,564 |
| Weighted average number of common shares and common stock equivalent shares outstanding | 23,095,578 | 23,089,541 |
| Diluted earnings per common share | \$.22 | \$.32 |

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The Company operates three lines of business: retail grocery sales, shopping center rentals, and a fluid dairy processing plant. All of the Company's operations are domestic. Information about the Company's operations by lines of business (in thousands) is as follows:

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|-------------------|-------------------|--------------------|
| | March 29, 2003 | March 30, 2002 | March 29, 2003 | March 30, 2002 |
| Revenues from unaffiliated customers: | | | | |
| Grocery sales | \$466,057 | \$470,408 | \$938,627 | \$ 946,339 |
| Shopping center rentals | 4,208 | 4,442 | 7,909 | 8,441 |
| Fluid dairy | 23,326 | 22,748 | 45,872 | 46,261 |
| Total revenues from unaffiliated customers | \$493,591 | \$497,598 | \$992,408 | \$1,001,041 |
| Income from operations: | | | | |
| Grocery sales | \$ 8,677 | \$ 13,277 | \$ 20,745 | \$ 23,991 |
| Shopping center rentals | 2,349 | 2,362 | 4,500 | 4,756 |
| Fluid dairy | 2,706 | 2,896 | 5,483 | 5,657 |
| Total income from operations | \$ 13,732 | \$ 18,535 | \$ 30,728 | \$ 34,404 |

| | March 29, 2003 | September 28, 2002 |
|-------------------------|-------------------|-----------------------|
| Assets: | | |
| Grocery sales | \$844,795 | \$ 860,583 |
| Shopping center rentals | 123,060 | 124,965 |
| Fluid dairy | 28,430 | 28,843 |
| Total assets | \$996,285 | \$1,014,391 |

Revenue from shopping center rentals is reported on the rental income, net line of the income statements. The other revenues comprise the net sales reported.

For the three months ended March 29, 2003 and March 30, 2002, respectively, the fluid dairy segment had \$11.3 and \$11.0 million in sales to the grocery sales segment. The fluid dairy segment had \$22.7 and \$22.3 million in sales to the grocery sales segment in the six-month periods ended March 29, 2003 and March 30, 2002, respectively. These sales have been eliminated in consolidation and are excluded from the amounts in the table above.

I. ACCOUNTING FOR STOCK-BASED COMPENSATION

In December 2002, the FASB issued Statement No. 148, Accounting for Stock-Based Compensation Transition and Disclosure (FAS 148). FAS 148 amends FASB Statement No. 123, Accounting for Stock-Based Compensation (FAS123), to provide alternative methods of transition to the fair value method of accounting for stock-based employee compensation. In addition, FAS 148 amends the disclosure provisions of FAS 123 to require disclosure of the effects of an entity's accounting policy with respect to stock-based employee compensation on reported net income and earnings per share in annual and interim financial statements. FAS 148 does not amend FAS 123 to require companies to account for their employee stock-based awards using the fair value method. However, the disclosure provisions are required for all companies with stock-based employee compensation, regardless of whether they utilize the fair value method of accounting described in FAS 123 or the intrinsic value

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method described in APB Opinion No. 25, Accounting for Stock Issued to Employees. FAS 148 is effective for fiscal years ending after December 15, 2002 and early application is permitted. Interim pro forma disclosures are required for interim periods beginning after December 15, 2002. The Company adopted FAS 148 beginning with the March 29, 2003 quarter.

The Company reports under the provisions of Statement of Financial Accounting Standards No. 123, Accounting for Stock-Based Compensation (FAS 123). FAS 123 establishes financial accounting and reporting standards for stock-based compensation plans. As permitted by FAS 123, the Company elected to account for stock-based compensation awards in accordance with Accounting Principles Board Opinion No. 25. In accordance with FAS 123, the fair value of each option grant was determined by using the Black-Scholes option-pricing model.

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Had compensation cost for the Company's plans been determined based on the fair value at the grant date for such awards consistent with the provisions of FAS 123, the Company's earnings and earnings per share, basic and diluted, would have been reduced to the pro forma amounts indicated below:

| | Three Months Ended | | Six Months Ended | |
|--|--------------------|-------------------|-------------------|-------------------|
| | March 29, 2003 | March 30, 2002 | March 29, 2003 | March 30, 2002 |
| BASIC | | | | |
| Net income | \$1,820,084 | \$3,295,253 | \$4,995,313 | \$7,412,564 |
| Net income, pro forma | \$1,654,104 | \$3,054,002 | \$4,627,061 | \$6,881,336 |
| Basic earnings per common share | \$ 0.08 | \$ 0.15 | \$ 0.22 | \$ 0.33 |
| Basic earnings per common share, pro forma | \$ 0.07 | \$ 0.13 | \$ 0.20 | \$ 0.30 |
| DILUTED | | | | |
| Diluted earnings | \$1,820,084 | \$3,295,253 | \$4,995,313 | \$7,412,564 |
| Diluted earnings, pro forma | \$1,654,104 | \$3,054,002 | \$4,627,061 | \$6,881,336 |
| Diluted earnings per common share | \$ 0.08 | \$ 0.14 | \$ 0.22 | \$ 0.32 |
| Diluted earnings per common share, pro forma | \$ 0.07 | \$ 0.13 | \$ 0.20 | \$ 0.30 |

No compensation expense has been recognized under Opinion 25 in the three and six month periods ended March 29, 2003 and March 30, 2002. The pro forma impact of these options is not likely to be representative of the effects on reported net income for future years.

J. NEW ACCOUNTING PRONOUNCEMENTS

In August 2001, the FASB issued Statement No. 143 *Accounting for Asset Retirement Obligations* that provides accounting guidance for the costs of retiring long-lived assets and is effective for fiscal years beginning after June 15, 2002. The Company adopted this statement at the beginning of fiscal year 2003. Adoption of the statement did not have any impact on the Company's financial statements.

In October 2001, the FASB issued Statement No. 144 *Accounting for the Impairment or Disposal of Long-Lived Assets* (FAS 144). FAS 144 provides accounting guidance for financial accounting and reporting for the impairment or disposal of long-lived assets. The statement supercedes FASB Statement No. 121, *Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of* (FAS 121). It also supercedes the accounting and reporting provisions of APB Opinion No. 30 *Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions* related to the disposal of a segment of a business. FAS 144 is effective for fiscal years beginning after December 15, 2001. The Company adopted this statement at the beginning of fiscal year 2003. Adoption of the statement did not have any impact on the Company's financial statements.

In April 2002, the FASB issued Statement No. 145, *Modifications to Reporting of Extinguishments of Debt and Accounting for Certain Capital Lease Modifications and Technical Corrections* (FAS 145). FAS 145 requires gains and losses on extinguishments of debt to be classified as income or loss from continuing operations rather than as extraordinary items as previously required under FASB Statement No. 4. Extraordinary treatment is required for certain extinguishments as provided in APB Opinion No. 30. FAS 145 also amends FASB Statement No. 13 to require certain modifications to capital leases be treated as sale-leaseback transactions and modifies the accounting for sub-leases when the original lessee remains a secondary obligor (or guarantor). In the December 2002 quarter, the Company adopted FAS 145. Costs of \$0.7 million incurred with the early retirement of the \$170.0 million in debt have been reclassified in the March 2002 six-month period from an extraordinary item to interest expense. The reclassification has no effect on total basic or diluted earnings per share but eliminates the need to classify a \$0.02 per share loss in the March 2002 six-month period as an extraordinary item.

EITF (Emerging Issues Task Force) Issue No. 02-16, *Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor*, became effective as to the Company on December 29, 2002. This issue addresses the appropriate accounting for consideration received from a vendor. Due to system constraints and the nature of certain allowances, it is sometimes not practicable to apply allowances to the item cost of inventory. As a result of this new guidance and these constraints, the Company has adopted a new policy for recognizing vendor allowances, including slotting fees. The Company recognizes these allowances as a reduction to inventory and ultimately to cost of goods sold when the related products are sold, for transactions executed subsequent to December 29, 2002. Under the Company's previous accounting policy for vendor allowances including slotting fees, these credits

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were recognized as a reduction to cost of goods sold as soon as the amount was contractually established and collection was probable. In connection with the implementation of this new accounting policy, the Company applied the provisions of EITF No. 02-16 prospectively which resulted in deferring recognition of \$2.6 million of allowances, before a tax benefit of approximately \$1.0 million, in the second quarter of 2003. This charge was recorded in the Company's Condensed Consolidated Statement of Income using the prospective method and reflects an adjustment of the Company's inventory balance.

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

Overview

Ingles, a leading supermarket chain in the Southeast, operates 200 supermarkets in Georgia (83), North Carolina (60), South Carolina (33), Tennessee (21), Virginia (2) and Alabama (1). The Company locates its supermarkets primarily in suburban areas, small towns and rural communities. Ingles supermarkets offer customers a wide variety of nationally advertised food products, including grocery, meat and dairy products, produce, frozen foods and other perishables and non-food products, including health and beauty care products and general merchandise, as well as quality private label items. In addition, the Company focuses on selling high-growth, high-margin products to its customers through the development of book sections, media centers, floral departments, bakery departments and prepared foods including delicatessen sections. The Company recently began adding fuel centers and pharmacies at select store locations. As of March 29, 2003, the Company operates 21 in-store pharmacies and 16 fuel centers.

Ingles also operates two other lines of business, fluid dairy processing and shopping center rentals. The fluid dairy processing segment sells approximately 33% of its products to the retail grocery segment and approximately 67% of its products to third parties. Real estate ownership (including the shopping center rental segment) is an important component of the Company's operations, providing both operational and economic benefit.

Critical Accounting Policies

Critical accounting policies are those accounting policies that management believes are important to the portrayal of Ingles' financial condition and results of operations, and require management's most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

Self-Insurance

The Company is self-insured for workers' compensation and group medical and dental benefits. Risks and uncertainties are associated with self-insurance; however, the Company has limited its exposure by maintaining excess liability coverages. Self-insurance reserves are established based on claims filed and estimates of claims incurred but not reported. The estimates are based on data provided by the respective claims administrators. The majority of the Company's properties are self-insured for casualty losses and business interruption; however, liability coverage is maintained.

Asset Impairments

Beginning in fiscal 2003, the Company accounts for the impairment of long-lived assets in accordance with Statement of Financial Accounting Standards No. 144. For assets to be held and used, the Company tests for impairment using undiscounted cash flows and calculates the amount of impairment using discounted cash flows. For assets held for sale, impairment is recognized based on the excess of remaining book value over expected recovery value. The recovery value is the fair value as determined by independent quotes or expected sales prices developed by internal specialists. Estimates of future cash flows and expected sales prices are judgments based upon the Company's experience and knowledge of local operations and cash flows that are projected for several years into the future. These estimates can fluctuate significantly due to changes in real estate market conditions, the economic environment, capital spending decisions and inflation. Adoption of Statement No. 144 had no impact on results of operations or financial position.

Closed Store Accrual

For properties to be closed that are under long-term lease agreements, the present value of any remaining liability under the lease, discounted using risk-free rates and net of expected sublease recovery, is recognized as a liability and expensed. If the real estate and

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leasing markets change, sublease recovery could vary significantly from the recoveries originally assumed, resulting in a material change in the Company's recorded liability.

Vendor Allowances

The Company receives funds for a variety of merchandising activities from the many vendors whose products the Company buys for resale in its stores. These incentives and allowances include volume or purchase based incentives, advertising allowances, slotting fees, and promotional discounts. The purpose of these incentives and allowances is generally to help defray the costs incurred by the Company for stocking, advertising, promoting and selling the vendor's products. Whenever possible, vendor discounts and allowances that relate to our buying and merchandising activities are recorded as a component of item cost inventory and recognized in merchandise costs when the item is sold. Due to system constraints and the nature of certain allowances, it is sometimes not practicable to apply allowances to the item cost of inventory. In those instances, the allowances are applied as a reduction of merchandise costs using a rational and systematic methodology, which results in the recognition of these incentives when the initial purchase of the related merchandise is sold. Amounts that represent a reimbursement of specific identifiable incremental costs, such as advertising, are recorded as a reduction to the related expense in the period that the related expense is incurred.

Results of Operations

Ingles operates on a 52 or 53-week fiscal year ending on the last Saturday in September. There are 13 and 26 weeks of operations included in the unaudited condensed consolidated statements of income for the three and six-month periods ended March 29, 2003 and March 30, 2002. Comparable store sales are defined as sales by grocery stores in operation for the entire duration of the previous and current fiscal years. Replacement stores and major and minor remodels are included in the comparable store sales calculation. For the three and six-month periods ended March 29, 2003 and March 30, 2002, comparable store sales include 197 stores.

A replacement store is a new store that is opened to replace an existing nearby store that is closed. A major remodel entails substantial remodeling of an existing store and may include additional retail square footage. A minor remodel includes repainting, remodeling and updating the lighting and equipment throughout an existing store.

The following table sets forth, for the periods indicated, selected financial information as a percentage of net sales. For information regarding the various segments of the business, see Note H "Lines of Business" to the Unaudited Consolidated Financial Statements.

| | Three Months Ended | | Six Months Ended | |
|---|--------------------|-------------------|-------------------|-------------------|
| | March 29, 2003 | March 30, 2002 | March 29, 2003 | March 30, 2002 |
| Net sales | 100.0% | 100.0% | 100.0% | 100.0% |
| Gross profit | 26.0% | 26.9% | 26.1% | 26.3% |
| Operating and administrative expenses | 23.7% | 23.6% | 23.5% | 23.3% |
| Rental income, net | 0.5% | 0.5% | 0.5% | 0.5% |
| Other income, net | 0.4% | 0.1% | 0.2% | 0.3% |
| Income before interest and income taxes | 3.2% | 3.9% | 3.3% | 3.8% |
| Interest expense | 2.6% | 2.8% | 2.5% | 2.6% |
| Income before income taxes | 0.6% | 1.1% | 0.8% | 1.2% |
| Income taxes | 0.2% | 0.4% | 0.3% | 0.5% |
| Net income | 0.4% | 0.7% | 0.5% | 0.7% |

Three Months Ended March 29, 2003 Compared to the Three Months Ended March 30, 2002

Net Sales. Sales comparisons for the three and six-month periods were affected by the timing of the Easter holiday. In fiscal 2002, Easter fell on the day following the end of the March quarter, therefore Easter related sales were included in the March three and six-month periods of fiscal 2002. Easter related sales will be included in the third quarter of fiscal 2003.

Net sales for the March 2003 quarter decreased 0.8% to \$489.4 million from \$493.2 million for the same quarter last year. Comparable store sales for the same period decreased \$6 million or 1.3%. Excluding the effect of Easter, comparable store sales decreased \$1.8 million or 0.4% for the March 2003 quarter compared to the March 2002 quarter. Weak economic conditions in the Company's operating area contributed to the

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decline in comparable store sales. Ingles operated 200 stores at the end of the March 2003 quarter and 201 stores at the end of the March 2002 quarter.

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Gross Profit. Gross profit for the three-month period ended March 29, 2003, decreased 4.0% to \$127.2 million, or 26.0% of sales, compared to \$132.5 million, or 26.9% of sales, for the three-month period ended March 30, 2002. The Company had previously recognized certain vendor allowances, principally slotting fees, as a reduction to cost of goods sold as soon as the amount was contractually established and collection was probable. Under EITF 02-16, the Company has changed its policy to include these allowances as a reduction in inventory value. Adoption of this policy in the March 2003 quarter resulted in a one time non-cash charge to cost of goods sold of \$2.6 million, or 2.0 % of the 4.0 % decrease in gross profit. The remaining 2.0% reduction was due to weak economic conditions resulting in more conservative consumer spending and more aggressive price promotion. The higher margin deli, bakery and meat departments were affected the most by the conservative spending patterns.

Operating and Administrative Expenses. Operating and administrative expenses decreased 0.4% to \$115.8 million for the three months ended March 29, 2003, from \$116.3 million for the three months ended March 30, 2002. As a percentage of sales, operating and administrative expenses were 23.7% and 23.6% for the three months ended March 29, 2003 and March 30, 2002, respectively. A variety of factors contributed to the increase, as a percentage of sales.

A breakdown of the major increases (decreases) in operating and administrative expenses, expressed as a percentage of sales, is as follows:

| | |
|-------------------------------|--------|
| Depreciation and amortization | 0.1% |
| Rent expense | 0.1% |
| Utilities | 0.1% |
| Advertising | (0.2)% |

Fixed operating costs such as depreciation and amortization, rent expense and utilities were higher as a percentage of sales, due to the lower sales volume. In addition, utility costs rose due to a combination of a colder winter and higher fuel costs. Advertising expense declined due to cutbacks made in the advertising budget.

Rental Income, Net. Rental income, net decreased \$0.1 million to \$2.3 million for the March 2003 quarter from \$2.4 million for the March 2002 quarter. The decrease consists of gross rental income increases of \$0.1 million and operating cost increases of \$0.2 million.

Income from Operations. Income from operations decreased 25.9 % to \$13.7 million or 2.8% of sales in the March 2003 quarter compared to \$18.5 million, or 3.8% of sales in the March 2002 quarter. The decrease is principally attributable to the decreased gross profit.

Other Income, Net. Other income, net increased \$1.2 million to \$1.7 million for the three-month period ended March 29, 2003 from \$0.5 million for the three-month period ended March 30, 2002. The increase is principally due to the inclusion in the March 2003 quarter of a gain of \$1.1 million from the sale of a shopping center in which the Company no longer operated a store.

Income Before Interest & Income Taxes. Income before interest and income taxes decreased \$3.6 million to \$15.4 million, during the March 2003 quarter compared to \$19.0 million during the March 2002 quarter. Income before interest and income taxes, as a percentage of sales, was 3.2% and 3.9% for the March 2003 quarter and the March 2002 quarter, respectively.

Interest Expense. Interest expense decreased \$1.2 million for the three-month period ended March 29, 2003 to \$12.5 million from \$13.7 million for the three-month period ended March 30, 2002 principally due to a decrease in aggregate debt of \$33.4 million from March 2002 to March 2003.

Income Taxes. Income tax expense as a percentage of pre-tax income decreased to 37.4% in the March 2003 quarter compared to 38.4% in the March 2002 quarter.

Net Income. Net income decreased 44.8% for the three-month period ended March 29, 2003 to \$1.8 million compared to \$3.3 million for the three-month period ended March 30, 2002. Net income, as a percentage of sales, was 0.4% for the March 2003 quarter and 0.7% for the March 2002 quarter. Diluted earnings per share were \$.08 and \$.14 for the March 2003 and March 2002 quarters, respectively. Basic earnings per share were \$.08 for the March 2003 quarter and \$.15 for the March 2002 quarter. The one time charge from adoption of EITF 02-16 resulted in a reduction of net income of \$1.6 million, or \$.07 per diluted share.

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Six Months Ended March 29, 2003 Compared to the Six Months Ended March 30, 2002

Net Sales. As mentioned in the three-month discussion, sales comparisons for the six-month periods were affected by the timing of the Easter holiday. Net sales for the six months ended March 29, 2003 decreased 0.8% to \$984.5 million, compared to \$992.6 million for the six months ended March 30, 2002. Comparable store sales decreased \$8.0 million or 0.9% for such period. Adjusted for the difference in timing of the Easter holiday, comparable store sales decreased \$3.6 million or 0.4% for the 2003 six-month period compared to the March 2002 six-month period. Weak economic conditions in the Company's operating area contributed to the decline in comparable store sales.

Gross Profit. Gross profit for the six months ended March 29, 2003 decreased 1.2% to \$257.4 million compared to \$260.5 million, for the six months ended March 30, 2002. As a percent of sales, gross profit decreased slightly to 26.1% for the six months ended March 29, 2003 from 26.3% for the six months ended March 30, 2002. The Company had previously recognized certain vendor allowances, principally slotting fees as a reduction to cost of goods sold as soon as the amount was contractually established and collection was probable. Under EITF 02-16, the Company has changed its policy to including these allowances as a reduction in inventory value. Adoption of this policy in the March 2003 six-month period resulted in a one time non-cash charge to cost of goods sold of \$2.6 million, or 1.0% of the 1.2% decrease in gross profit.

Operating and Administrative Expenses. Operating and administrative expenses increased 0.1% to \$231.2 million for the six months ended March 29, 2003, from \$230.9 million for the six months ended March 30, 2002. As a percentage of sales, operating and administrative expenses increased to 23.5% for the March 2003 six-month period from 23.3% for the same period last year.

A breakdown of the major increases (decreases) in operating and administrative expenses, expressed as a percentage of sales, is as follows:

| | |
|-------------------------------|--------|
| Rent expense | 0.1% |
| Depreciation and amortization | 0.1% |
| Utilities | 0.1% |
| Advertising | (0.1)% |
| Insurance | (0.1)% |

As mentioned in the three-month discussion, fixed operating costs such as rent expense, depreciation and amortization and utilities were higher as a percentage of sales, due to the lower sales volume. Advertising expense declined due to cutbacks made in the advertising budget. Comprehensive changes made in April 2002 to the Company's medical plan curbed the growth of insurance costs, as a percentage of sales.

Rental Income, Net. Rental income, net decreased \$0.3 million to \$4.5 million in the March 2003 six-month period from \$4.8 million in the March 2002 comparable period. Gross rental income remained virtually unchanged, while shopping center expenses (primarily depreciation) increased \$0.3 million.

Income from Operations. Income from operations decreased 10.7% to \$30.7 million or 3.1% of sales in the March 2003 six-month period compared to \$34.4 million, or 3.5% of sales in the March 2002 six-month period.

Other Income, Net. Other income, net decreased \$0.8 million for the March 2003 six-month period over the comparable period in fiscal 2002. The March 2003 six-month period included a gain of \$1.1 million from the sale of a shopping center in which the company no longer operated a store, while the March 2002 six-month period, included \$1.8 million in gains from the sale of three tracts of land, all adjacent to store properties.

Interest Expense. Interest expense decreased \$0.5 million to \$25.2 million for the six months ended March 29, 2003 from \$25.7 million for the six months ended March 30, 2002, due primarily to the decrease in debt mentioned in the three-month discussion. During the first quarter of 2003, the balance of the proceeds from the December 2001 issuance of \$250 million of 8 7/8% Senior Unsecured Subordinated Notes (Notes) was used to fund current maturities and capital expenditures.

Costs of \$0.7 million associated with the early retirement of debt incurred during the March 2002 six-month period have been reclassified in the March 2002 six-month period from an extraordinary item to interest expense in compliance with FASB Statement No. 145.

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Income Taxes. Income tax expense as a percentage of pre-tax income decreased to 36.2% in the March 2003 six-month period compared to 37.4% in the March 2002 six-month period.

Net Income. Net income for the March 2003 six-month period was \$5.0 million, or 0.5% of sales, compared to \$7.4 million, or 0.7% of sales, for the March 2002 six-month period. Basic earnings per common share were \$.22 and \$.33 for the March 2003 and March 2002 six-month period, respectively. Diluted earnings per common share were \$.22 for the March 2003 six-month period compared to \$.32 for the March 2002 six-month period. The one time charge from adoption of EITF 02-16 resulted in a reduction of net income of \$1.6 million, or \$.07 per diluted share.

Liquidity and Capital Resources

Capital Expenditures

The Company believes that a key to its ability to continue to develop a loyal customer base is providing conveniently located, clean and modern stores which provide customers with good service and a broad selection of competitively priced products. As such, the Company has invested and will continue to invest significant amounts of capital toward the modernization of its store base. The Company's modernization program includes the opening of new stores, the completion of major remodels and expansion of selected existing stores, the relocation of selected existing stores to larger, more convenient locations and the completion of minor remodeling of its remaining existing stores.

Capital expenditures totaled \$37.0 million for the six-month period ended March 29, 2003, including the opening of three new stores, the completion of one major remodel/expansion and three minor remodels and the purchase of one shopping center in which the Company was a tenant. Capital expenditures also included the costs of upgrading and replacing store equipment, technology investments, the purchase of future store sites, capital expenditures related to the Company's distribution operation and its milk processing plant, and expenditures for stores to open later in fiscal 2003 and in fiscal 2004.

Ingles' capital expenditure plans for fiscal 2003 include investments of approximately \$70 million. For the balance of fiscal 2003, the Company plans to open one new store, replace one existing store and complete one major remodel/expansion. Expenditures will also include investments in stores expected to open in fiscal 2004 as well as technology improvements, upgrading and replacing existing store equipment and warehouse and transportation equipment and improvements to the Company's milk processing plant.

While capital expenditures for the fiscal year are expected to be of a level consistent with the Company's past practice, management expects that the number of projects pursued during each fiscal year will decline in the future to some degree, possibly stabilizing at a smaller number of projects per year. This decline in number is a result of an increase in the average size of each company store. The dollar value of such projects should remain stable or continue to increase.

The Company does not generally enter into commitments for capital expenditures other than on a store-by-store basis at the time it begins construction on a new store or begins a major or minor remodeling project. The Company generally engages in major remodeling and new store development on not more than three or four locations at a time. Therefore, the dollar amounts of any commitments for capital expenditures are generally immaterial to the Company's financial position and when compared to aggregate capital expenditures in each fiscal year. The vast majority of the Company's capital expenditures each fiscal year is discretionary. The Company makes expenditure decisions from time to time based on available financing and other market conditions.

Liquidity

The Company had net cash from operations of \$14.0 million in the March 2003 six-month period.

Cash used by investing activities totaled \$35.4 million comprised primarily of \$37.0 million of capital expenditures during the period, partially offset by \$1.6 million of proceeds from the sale of assets.

The Company has generally funded its capital expenditures with cash provided from operations and borrowings under lines of credit. The lines of credit are later refinanced with secured long-term debt. During the March 2003 six-month period, the Company's financing activities used \$10.4 million in cash. Proceeds from long-term debt totaled \$20.6 million, comprised of advances under long-term lines of credit, while repayments of long-term debt were \$24.4 million. Dividends paid totaled \$7.1 million.

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At March 29, 2003, the Company had lines of credit with seven banks totaling \$145.0 million, of which \$124.6 million were unused. Of the \$145.0 million of committed lines of credit, \$130.0 million matures in October 2004 and \$15.0 million matures in October 2003. The lines provide the Company with various interest rate options generally at rates less than prime. The Company is not required to maintain compensating balances in connection with these lines of credit. The Company was in compliance with all financial covenants related to these lines of credit at March 29, 2003.

The Company's principal sources of liquidity are expected to be cash flow from operations, borrowings under its lines of credit and long-term financing. As of March 29, 2003, the Company had unencumbered real property and equipment with a net book value of approximately \$312.0 million. The Company believes, based on its current results of operations and financial condition, that its financial resources, including existing bank lines of credit, short- and long-term financing expected to be available to it and internally generated funds, will be sufficient to meet planned capital expenditures and working capital requirements for the foreseeable future, including any debt service requirements of additional borrowings. However, there can be no assurance that any such sources of financing will be available to the Company on acceptable terms, or at all.

The supermarket business is a highly competitive business with numerous competitors. There is increasing competition for food business from non-traditional retailers such as discount stores, drug stores, club stores and super centers, as well as from restaurants as families eat out more often. The Company currently expects moderate sales growth to continue in the upcoming fiscal year as stores that are new or expanded mature and promotional efforts to drive sales are successful. It also currently expects sales of higher margin products to continue to increase due to the expansion of the perishable departments in stores that are new or remodeled.

However, it is possible that, in the future, the Company's results of operations and financial condition will be different from that described in this report or from that currently expected by the Company based on a number of intangible factors. These factors may include, among others, increased competition, changing regional and national economic conditions, adverse climatic conditions affecting food production and delivery and changing demographics as well as the additional factors discussed below under *Forward Looking Statements*. It is also possible, for such reasons, that the results of operations from the new, expanded, remodeled and/or replacement stores will not meet or exceed the results of operations from existing stores that are described in this report.

Quarterly Cash Dividends

Since December 27, 1993, the Company has paid regular quarterly cash dividends of \$.165 (sixteen and one-half cents) per share on its Class A Common Stock and \$.15 (fifteen cents) per share on its Class B Common Stock for an annual rate of \$.66 and \$.60 per share, respectively.

The Company expects to continue paying regular cash dividends on a quarterly basis. However, the Board of Directors periodically reconsiders the declaration of dividends. The Company pays these dividends at the discretion of the Board of Directors and the continuation of these payments, the amount of such dividends, and the form in which the dividends are paid (cash or stock) depends upon the results of operations, the financial condition of the Company and other factors which the Board of Directors deems relevant. In addition, certain loan agreements containing provisions outlining minimum tangible net worth requirements, restrict the ability of the Company to pay additional dividends to approximately \$30.3 million based on tangible net worth at March 29, 2003. Further, the Company is prevented from paying dividends at any time that it is in default under the indenture governing the Notes. In addition, the terms of the indenture may restrict the ability of the Company to pay additional dividends based on certain financial parameters.

Impact of Inflation

Inflation in food prices during the first six months of fiscal 2003 was slightly lower than the overall increase in the Consumer Price Index, while inflation in food prices in fiscal 2002 was slightly higher than the overall increase in the Consumer Price Index. One of the Company's significant costs is labor, which increases with inflation.

New Accounting Pronouncements

In August 2001, the FASB issued Statement No. 143 *Accounting for Asset Retirement Obligations* that provides accounting guidance for the costs of retiring long-lived assets and is effective for fiscal years beginning after June 15, 2002. The Company adopted this statement at the beginning of fiscal year 2003. Adoption of the statement did not have any impact on the Company's financial statements.

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EITF (Emerging Issues Task Force) Issue No. 02-16, Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor, became effective as to the Company on December 29, 2002. This issue addresses the appropriate accounting for consideration received from a vendor. Due to system constraints and the nature of certain allowances, it is sometimes not practicable to apply allowances to the item cost of inventory. As a result of this new guidance and these constraints, the Company has adopted a new policy for recognizing vendor allowances, including slotting fees. The Company recognizes these allowances as a reduction to inventory and ultimately to cost of goods sold when the related products are sold, for transactions executed subsequent to December 29, 2002. Under the previous accounting policy for vendor allowances including slotting fees, these credits were recognized as a reduction to cost of goods sold as soon as the amount was contractually established and collection was probable. In connection with the implementation of this new accounting policy, the Company applied the provisions of EITF No. 02-16 prospectively which resulted in deferring recognition of \$2.6 million of allowances, before a tax benefit of approximately \$1.0 million, in the second quarter of 2003. This charge was recorded in the Company's Condensed Consolidated Statement of Income using the prospective method and reflects an adjustment of the Company's inventory balance.

Forward Looking Statements

This Quarterly Report contains certain forward-looking statements within the meaning of Section 21E of the Securities Exchange Act of 1934. The words expect, anticipate, intend, plan, believe, seek and similar expressions are intended to identify forward-looking statements. When forward-looking statements and the related assumptions are made in good faith and reflect our current judgment regarding the direction of our business, actual results will almost always vary, sometimes materially, from any estimates, predictions, projections, assumptions or other future performance suggested herein. Such statements are based upon a number of assumptions and estimates which are inherently subject to significant risks and uncertainties many of which are beyond our control. Some of these assumptions inevitably will not materialize, and unanticipated events will occur which will affect our results. Some important factors (but not necessarily all factors) that affect our revenues, growth strategies, future profitability and operating results, or that otherwise could cause actual results to differ materially from those expressed in or implied by any forward-looking statement, include business and economic conditions generally in the Company's operating area; the Company's ability to successfully implement its expansion and operating strategies and to manage rapid expansion; pricing pressures, the opening of competitors stores in the Company's markets and other competitive factors; the Company's ability to reduce costs and achieve improvements in operating results; the availability and terms of financing; increases in labor and utility costs; success or failure in the ownership and development of real estate; and changes in the laws and government regulations applicable to the Company.

Consequently, actual events affecting the Company and the impact of such events on the Company's operations may vary significantly from those described in this report or contemplated or implied by statements in this report.

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Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

On December 11, 2001 the Company closed the offering of the Notes. The Notes bear interest at a rate of 8-7/8% and were issued at a discount to yield 9%. There have been no material changes in the market interest rates subsequent to September 28, 2002.

Item 4. CONTROLS AND PROCEDURES

As of March 29, 2003, the end of the period covered by this report, an evaluation was performed under the supervision and with the participation of Ingles management, including Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of Ingles disclosure controls and procedures, as such term is defined under Rule 13a-15(e) promulgated under the Securities Exchange Act of 1934, as amended (the Exchange Act). Based on that evaluation, Ingles management, including the Chief Executive Officer and Chief Financial Officer, concluded that, as of the end of the period covered by this report, Ingles disclosure controls and procedures were effective at ensuring that required information will be disclosed on a timely basis in Ingles reports filed under the Exchange Act. No changes in Ingles internal control over financial reporting have occurred during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, Ingles internal control over financial reporting.

Part II. Other Information.

Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

The Annual Meeting of Stockholders of Ingles Markets, Incorporated was held Tuesday, February 11, 2003. The only matter submitted to a vote of the stockholders at this meeting was the election of nine directors to serve until the 2004 Annual Meeting of Stockholders.

Charles L. Gaither, Jr., John O. Pollard, and J. Alton Wingate were elected by the holders of Class A Common Stock by the following votes: (a) Mr. Gaither: 8,825,689 votes for, 252,200 votes withheld, 0 abstentions and 0 broker nonvotes; (b) Mr. Pollard: 8,855,488 votes for, 222,401 withheld, 0 abstentions and 0 broker nonvotes; (c) Mr. Wingate: 8,861,287 votes for, 216,602 votes withheld, 0 abstentions and 0 broker nonvotes. Robert P. Ingle, Anthony S. Federico, Robert P. Ingle, II, Charles E. Russell, Laura Ingle Sharp and Brenda S. Tudor were each elected by the holders of Class B Common Stock by the following vote: 12,219,621 votes for, 0 votes withheld, 0 abstentions and 0 broker nonvotes.

Item 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits.

- 1) Exhibit 31.1 Rule 13a-14(a) Certificate
- 2) Exhibit 31.2 Rule 13a-14(a) Certificate
- 3) Exhibit 32.1 Certification Pursuant to 18 U.S.C. Section 1350
- 4) Exhibit 32.2 Certification Pursuant to 18 U.S.C. Section 1350

(b) Reports on Form 8-K. There were no reports on Form 8-K filed by the Company during the quarter ended March 29, 2003.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this Amendment No. 2 to its Form 10-Q to be signed on its behalf by the undersigned thereunto duly authorized.

INGLES MARKETS, INCORPORATED

Date: November 24, 2003

/s/ Robert P. Ingle

Robert P. Ingle
Chairman of the Board and Chief Executive Officer

Date: November 24, 2003

/s/ Brenda S. Tudor

Brenda S. Tudor
Vice President-Finance and Chief Financial Officer