

Edgar Filing: STONEPATH GROUP INC - Form 10-Q

STONEPATH GROUP INC  
Form 10-Q  
May 10, 2004

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2004

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 001-16105

STONEPATH GROUP, INC.

-----  
(Exact name of registrant as specified in its charter)

Delaware

65-0867684

-----  
(State or other jurisdiction of  
incorporation or organization)

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

1600 Market Street, Suite 1515  
Philadelphia, PA 19103

-----  
(Address of principal executive offices) (Zip Code)  
Registrant's Telephone Number, Including Area Code: (215) 979-8370  
-----

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

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

There were 41,199,102 issued and outstanding shares of the registrant's common stock, par value \$.001 per share, at May 5, 2004.

STONEPATH GROUP, INC.

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Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

STONEPATH GROUP, INC.  
Condensed Consolidated Balance Sheets  
(UNAUDITED)

	March 31, 2004	Dece
	-----	---
Assets		
Current assets:		
Cash and cash equivalents	\$ 4,054,784	\$

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Accounts receivable, net	47,402,077	
Other current assets	4,432,223	
	-----	-----
Total current assets	55,889,084	
Goodwill and acquired intangibles, net	44,864,962	
Furniture and equipment, net	8,293,749	
Other assets	1,168,959	
Deferred taxes	1,574,000	
	-----	-----
	\$ 111,790,754	\$
	=====	=====
Liabilities and Stockholders' Equity		
Current liabilities:		
Line of credit-bank	\$ 8,623,305	\$
Accounts payable	23,506,131	
Accrued expenses	7,326,644	
Earn-out payable	1,157,738	
Capital lease obligation	796,049	
	-----	-----
Total current liabilities	41,409,867	
Capital lease obligation, net of current portion	1,225,335	
	-----	-----
Total liabilities	42,635,202	
	-----	-----
Minority interest	2,087,100	
	-----	-----
Commitments and contingencies (Note 5)		
Stockholders' equity:		
Preferred stock, \$.001 par value, 10,000,000 shares authorized; Series D Convertible, issued and outstanding: 192,807 and 310,480 shares at 2004 and 2003, respectively	193	
Common stock, \$.001 par value, 100,000,000 shares authorized; issued and outstanding: 39,943,477 and 37,449,944 shares at 2004 and 2003, respectively	39,943	
Additional paid-in capital	221,347,937	
Accumulated deficit	(154,357,361)	(
Accumulated other comprehensive income	37,740	
Deferred compensation	--	
	-----	-----
Total stockholders' equity	67,068,452	
	-----	-----
Total liabilities and stockholders' equity	\$ 111,790,754	\$
	=====	=====

See accompanying notes to unaudited consolidated financial statements.

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STONEPATH GROUP, INC.  
Consolidated Statements of Operations  
(UNAUDITED)

	Three months end ----- 2004 ----
Total revenue	\$ 60,533,707
Cost of transportation	42,809,574
	-----
Net revenue	17,724,133
Personnel costs	9,897,742
Other selling, general and administrative costs	8,057,401
Depreciation and amortization	850,836
Litigation settlement	--
	-----
Loss from operations	(1,081,846)
Other income	
Interest income (expense), net	(35,739)
Other income (expense), net	(15,508)
	-----
Income (loss) before income tax expense (benefit) and minority interest	(1,133,093)
Income tax expense (benefit)	(417,800)
	-----
Loss before minority interest	(715,293)
Minority interest	69,608
	-----
Net loss attributable to common stockholders	\$ (784,901)
	=====
Basic and diluted loss per common share	\$ (0.02)
	=====
Basic and diluted weighted average common shares outstanding	38,385,489
	=====

See accompanying notes to unaudited consolidated financial statements.

STONEPATH GROUP, INC.  
Consolidated Statements of Cash Flows  
(UNAUDITED)

Three months end  
-----

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	2004
	----
Cash flow from operating activities:	
Net loss	\$ (784,901)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:	
Deferred income taxes	121,000
Depreciation and amortization	850,836
Minority interest in income of subsidiaries	69,608
Stock-based compensation	21,174
Loss on disposal of furniture and equipment	10,450
Changes in assets and liabilities, net of effect of acquisitions:	
Accounts receivable	4,687,992
Other assets	(599,214)
Accounts payable and accrued expenses	(4,160,617)
	-----
Net cash provided by (used in) operating activities	216,328
	-----
Cash flows from investing activities:	
Purchases of furniture and equipment	(1,081,720)
Acquisition of business, net of cash acquired	(2,334,012)
Payment of earn-out	(5,465,986)
Loans made	(75,000)
	-----
Net cash used in investing activities	(8,956,718)
	-----
Cash flows from financing activities:	
Proceeds from line of credit	8,623,305
Issuance of common stock, net of costs	--
Issuance of common stock upon exercise of options and warrants	1,237,357
Principal payments on capital lease	(175,382)
	-----
Net cash provided by financing activities	9,685,280
	-----
Effect of foreign currency translation	35,743
	-----
Net increase in cash and cash equivalents	980,633
Cash and cash equivalents at beginning of period	3,074,151
	-----
Cash and cash equivalents at end of period	\$ 4,054,784
	=====
Cash paid for interest	\$ 45,256
	=====
Cash paid for income taxes	\$ 51,261
	=====
Supplemental disclosure of non-cash investing and financing activities:	
Increase in furniture and equipment and capital lease obligation	\$ 390,754
Increase in common stock from conversion of Series D preferred stock	\$ 117

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See accompanying notes to unaudited consolidated financial statements.

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### Stonepath Group, Inc. Notes to Unaudited Consolidated Financial Statements March 31, 2004

#### (1) Nature of Operations and Basis of Presentation

Stonepath Group, Inc. and subsidiaries (the "Company") is a non-asset based third-party logistics services company providing supply chain solutions on a global basis. A full range of time-definite transportation and distribution solutions is offered through the Company's Domestic Services platform, where the Company manages and arranges the movement of raw materials, supplies, components and finished goods for its customers. A full range of international logistics services including international air and ocean transportation as well as customs house brokerage services is offered through the Company's International Services platform. In addition to these core service offerings, the Company also provides a broad range of value added supply chain management services, including warehousing, order fulfillment and inventory management. The Company services a customer base of manufacturers, distributors and national retail chains.

The accompanying unaudited consolidated financial statements were prepared in accordance with generally accepted accounting principles for interim financial information. Certain information and footnote disclosures normally included in financial statements have been condensed or omitted pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the "SEC") relating to interim financial statements. These statements reflect all adjustments, consisting only of normal recurring accruals, necessary to present fairly the Company's financial position, operations and cash flows for the periods indicated. While the Company believes that the disclosures presented are adequate to make the information not misleading, these unaudited consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2003. Interim operating results are not necessarily indicative of the results for a full year because our operating results are subject to seasonal trends when measured on a quarterly basis. Our first and second quarters are likely to be weaker as compared with our other fiscal quarters, which we believe is consistent with the operating results of other supply chain service providers.

#### (2) Stock-Based Compensation

In December 2002, the Financial Accounting Standards Board issued Statement of Financial Accounting Standards ("SFAS") No. 148, "Accounting for Stock-Based Compensation - Transition and Disclosure," which amended the disclosure requirements of SFAS No. 123, "Accounting and Disclosure of Stock-Based Compensation" to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The Company accounts for its employee stock option grants by applying the intrinsic value method in accordance with Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" and related interpretations.

The table below illustrates the effect on net loss attributable to common stockholders and loss per common share as if the fair value of options granted had been recognized as compensation expense in accordance with the provisions of SFAS No. 123.

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Stonepath Group, Inc.  
Notes to Unaudited Consolidated Financial Statements  
March 31, 2004

	Three months ended March 31,	
	2004	2003
Net loss attributable to common stockholders:		
As reported	\$ (784,901)	\$ (7,305)
Add: stock-based employee compensation expense included in reported net loss, net of tax	13,367	22,618
Deduct: total stock-based compensation expense determined under fair value method for all awards, net of tax	(1,359,970)	(894,318)
	\$ (2,131,504)	\$ (879,005)
Pro forma net loss attributable to common stockholders	\$ (2,131,504)	\$ (879,005)
	=====	=====
Basic and diluted loss per common share:		
As reported	\$ (0.02)	\$ --
Pro forma	(0.06)	(0.04)

### (3) Recent Acquisitions

On February 9, 2004, the Company acquired, through its indirect wholly owned subsidiary, Stonepath Holdings (Hong Kong) Limited, a 55% interest in Shaanxi Sunshine Cargo Services International Co., Ltd. ("Shaanxi"). Shaanxi is a Class A licensed freight forwarder headquartered in Shanghai, PRC and provides a wide range of customized transportation and logistics services and supply chain solutions, including global freight forwarding, warehousing and distribution, shipping services and special freight handling. As consideration for the purchase which was effective as of March 1, 2004, the Company paid \$5,500,000 consisting of \$3,500,000 in cash and \$2,000,000 of the Company's common stock. The seller may receive additional consideration of up to an additional \$5,500,000 under an earn-out arrangement payable at the rate of \$1,100,000 per year over a period of five years based on the future financial performance of Shaanxi. The Company used funds from its credit facility with LaSalle Business Credit, Inc. for the cash payment at the closing. The common shares issued in the transaction are subject to a one year restriction on sale and are subject to a pro rata forfeiture based upon a formula that compares the actual pre-tax income of Shaanxi through December 31, 2004 with the targeted level of income of \$4,000,000 (on an annualized basis). Also, if the trading price of the Company's common stock is less than \$3.17 per share at the end of the one year restriction, the Company will issue additional shares to the seller. Because the common shares issued in connection with this transaction are subject to forfeiture, they are accounted for as additional contingent consideration. When the number of common shares to be retained by the seller is ultimately determined, such shares will be valued at their then fair value and will result in additional goodwill being recorded.

The acquisition, which significantly enhances the Company's presence in the region, was accounted for as a purchase and accordingly, the results of operations and cash flows of Shaanxi will be included in the Company's consolidated financial statements prospectively from the date of acquisition. Because the Company consolidates its foreign subsidiaries on a one month lag, such information will not be reflected in the consolidated financial statements until the second quarter of 2004. The total purchase price, including

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acquisition expenses of \$266,000, but excluding the contingent consideration, was \$3,766,000. The following table summarizes the preliminary allocation of the purchase price based on estimated fair value of the assets acquired and liabilities assumed at March 1, 2004 (in thousands):

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Stonepath Group, Inc.	
Notes to Unaudited Consolidated Financial Statements	
March 31, 2004	
Current assets	\$ 16,691
Furniture and equipment	89
Goodwill and other intangible assets	2,701
	-----
Total assets acquired	19,481
Current liabilities assumed	(14,844)
Minority interest	(871)
	-----
Net assets acquired	\$ 3,766
	=====

The following unaudited pro forma information is presented as if the acquisition of Shaanxi had occurred on December 1, 2002, using the one month lag consolidation policy:

	March 31, 2004	March 31, 2003
Revenue	\$ 80,531	\$ 51,806
Net loss	(221)	(257)
Loss per share:		
Basic and diluted	\$ (0.01)	\$ (0.01)

#### (4) Revolving Credit Facility

To ensure adequate financial flexibility, we have a \$20,000,000 revolving credit facility (the "Facility") collateralized by the accounts receivable and the other assets of the Company and its subsidiaries. The Facility requires the Company and its subsidiaries to meet certain financial objectives and maintain certain financial covenants. Advances under the Facility may be used to finance future acquisitions, capital expenditures or for other corporate purposes. We expect that the cash flow from operations of our subsidiaries will be sufficient to support the corporate overhead of the Company and some portion, if not all, of the contingent earn-out payments and other cash requirements associated with our acquisitions. Therefore, we anticipate that our primary use of the Facility will be to finance the cost of new acquisitions and to pay any portion of existing earn-out arrangements that cash flow from operations is otherwise unable to fund. At March 31, 2004 we had advances of \$1,200,000 and another \$7,400,000 in outstanding checks which have been classified as incremental borrowings. Based upon available collateral and net of \$1,200,000 in advances under the Facility, outstanding letter of credit commitments and funds reserved for off-shore investments, there was approximately \$12,200,000 available for borrowing under our Facility.

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Stonepath Group, Inc.	
Notes to Unaudited Consolidated Financial Statements	
March 31, 2004	



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### (5) Commitments and Contingencies

On May 6, 2003, we elected to settle litigation instituted on August 20, 2000 by Austost Anstalt Schaan, Balmore Funds, S.A. and Amro International, S.A. Although we believed that the plaintiffs' claims were without merit, we chose to settle the matter in order to avoid future litigation costs and to mitigate the diversion of management's attention from operations. The total settlement costs of \$750,000, paid \$400,000 in cash and \$350,000 in shares of the Company's common stock, are included in the accompanying March 31, 2003 unaudited consolidated statement of operations.

On October 12, 2000, Emergent Capital Investment Management, LLC ("Emergent") filed suit against the Company and two of its officers contending that it was misled by statements made by the defendants in connection with the offering of the Company's Series C Preferred Stock which closed in March 2000. Specifically, Emergent alleges that it is entitled to rescind the transaction because it was allegedly represented that the size of the offering would be \$20,000,000 and the Company actually raised \$50,000,000. Emergent seeks a return of its \$2,000,000 purchase price of Series C shares. In June of 2001, the Company moved for summary judgment in this case.

After the summary judgment motion was filed, Emergent filed a second action against the Company and two of its officers alleging different allegations of fraud in connection with the Series C offering. In the new complaint, Emergent alleged that oral statements and written promotional materials distributed by the Company at a meeting in connection with the Series C offering were materially inaccurate with respect to the Company's investment in Net Value, Inc., a wholly owned subsidiary of the Company. Emergent also contended that the defendants failed to disclose certain allegedly material transactions in which an officer was involved prior to his affiliation with the Company. The Company filed a motion to dismiss this new action for failure to state a claim upon which relief can be granted.

On October 2, 2001, the Court entered an order granting summary judgment to the defendants in the first case filed by Emergent and dismissing Emergent's second complaint for failure to state a claim upon which relief can be granted. The Court allowed Emergent 20 days to file a second amended complaint as to the second action only. On October 21, 2001, Emergent did file a second amended complaint in the second action. The second amended complaint did not raise any new factual allegations regarding Emergent's participation in the offering.

The Company filed a motion to dismiss Emergent's second amended complaint. On April 15, 2002, the United States District Court for the Southern District of New York entered an order granting the motion to dismiss Emergent's second amended complaint against the Company and its former officers. The Court refused to grant Emergent an additional opportunity to re-plead its claims against the defendants and a final order dismissing the matter was entered. Emergent thereafter filed a notice of appeal to the United States Court of Appeals for the Second Circuit. On September 4, 2003, the Second Circuit Court of Appeals entered an order affirming in part, vacating in part and remanding in part the matter to the District Court. The Court of Appeals affirmed the dismissal of some of the counts in the Second Amended Complaint and determined that Emergent had stated a claim on the other counts. The Company has filed an answer denying liability to Emergent and discovery on causation issues is proceeding. The Company believes that it has meritorious defenses to the plaintiff's claims and continues to vigorously defend this action.

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March 31, 2004

The Company may become involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position, results of operations or liquidity.

### (6) Stockholders' Equity

#### Common Stock

On March 6, 2003, the Company completed a private placement of 4,470,000 shares of its common stock. The transaction consisted of the sale of 4,270,000 shares at \$1.35 per share and 200,000 shares at \$1.54 per share. In connection with this transaction, the Company realized gross proceeds of \$6,072,500, paid a brokerage fee consisting of cash commissions of \$364,350, issued placement agent warrants to purchase 297,000 shares of common stock at an exercise price of \$1.49 per share, and incurred other cash expenses of \$33,677. In addition, the Company had previously paid the placement agent \$25,000 in cash and had issued them warrants to purchase 150,000 shares of common stock at an exercise price of \$1.23 per share.

In connection with the Shaanxi acquisition, the Company issued 630,915 shares of its common stock. Because these shares are subject to a pro rata forfeiture based on the financial performance of Shaanxi through December 31, 2004, such shares have not been reflected as outstanding securities in the accompanying consolidated financial statements.

#### Series D Convertible Preferred Stock

There are 192,807 shares of Series D Preferred Stock outstanding as of March 31, 2004.

Each share of the Series D Convertible Preferred Stock is convertible into ten shares of common stock of the Company. Subsequent to December 31, 2003, the holders of the Series D Convertible Preferred Stock are entitled to participate in all liquidation distributions made to the holders of the Company's common stock on an as-if converted basis. The Series D Convertible Preferred Stock carries no dividend, and, except under limited circumstances, has no voting rights except as required by law. The Series D Convertible Preferred Stock automatically converts into shares of the Company's common stock as of December 31, 2004.

During the three months ended March 31, 2004, 117,000 shares of the Company's Series D Preferred Stock were converted into 1,170,000 shares of the Company's common stock.

#### Stock Options

During the three months ended March 31, 2004, options on 2,045,200 shares were granted. The range of exercises prices on granted options was \$2.38 to \$3.75 per share and the weighted average exercise price was \$3.02 per share.

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Stonepath Group, Inc.  
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March 31, 2004

Options on 45,417 shares expired during the three months ended March 31, 2004. The range of exercise prices was \$1.30 to \$2.30 per share and the weighted

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average exercise price was \$1.66 per share.

During the three months ended March 31, 2004, options on 873,000 shares were exercised. The range of exercise prices was \$0.60 to \$1.38 per share and the weighted average exercise price was \$0.97 per share.

During the three months ended March 31, 2004, non-employees exercised warrants for the purchase of 443,833 of the Company's common stock. The exercise price of all exercised warrants was \$1.00 per share.

### (7) Earnings (Loss) per Share

Basic earnings (loss) per common share and diluted earnings (loss) per common share are presented in accordance with SFAS No. 128, "Earnings per Share." Basic earnings (loss) per common share has been computed using the weighted-average number of shares of common stock outstanding during the period. Diluted earnings (loss) per common share incorporates the incremental shares issuable upon the assumed exercise of stock options and warrants and upon the assumed conversion of the Company's preferred stock, if dilutive. For the three months ended March 31, 2004 and 2003, all stock options, stock warrants, and convertible securities were excluded because their effect was antidilutive. The total numbers of such shares excluded from diluted loss per common share are 10,821,405 and 8,666,447 at March 31, 2004 and 2003, respectively. Also, the 630,915 shares of common stock issued in connection with the Shaanxi acquisition are subject to pro rata forfeiture based upon the financial performance of Shaanxi through December 31, 2004. Accordingly, such shares have been excluded from the calculation of basic and diluted earnings (loss) per common share for the three months ended March 31, 2004.

### (8) Income Taxes

For the three months ended March 31, 2004, the Company calculated income tax expense (benefit) using estimated effective rates of 34.0% for U.S. federal income taxes, 4.9% for state income taxes and 30.0% for foreign income taxes. For the quarter ended March 31, 2003, the Company calculated income tax expense only for state and foreign components. The Company did not reflect any expense for federal income taxes in the quarter ended March 31, 2003 due to the full valuation allowance that had been established for its deferred tax assets.

The components of income tax expense (benefit) consist of the following:

	Three Months Ended March 31,	
	2004	2003
U.S. federal	\$ (448,700)	\$ --
State	(36,200)	7,400
Foreign	67,100	7,821
	\$ (417,800)	\$ 15,221
	=====	=====

### (9) Segment Information

SFAS No. 131, "Disclosures About Segments of an Enterprise and Related Information," established standards for reporting information about operating segments in financial statements. Operating segments are defined as components of an enterprise engaging in business activities about which separate financial information is available that is evaluated regularly by the chief operating decision maker or group in deciding how to allocate resources and in assessing performance. The Company identifies operating segments based on the principal service provided by the business unit. Each segment has a separate management

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structure. The accounting policies of the reportable segments are the same as described in our Annual Report on Form 10-K for the year ended December 31, 2003. Segment information, in which corporate expenses (other than the litigation settlement in 2003) have been fully allocated to the operating segments, is as follows (in thousands):

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Stonepath Group, Inc.  
Notes to Unaudited Consolidated Financial Statements  
March 31, 2004

	Three months ended March 31, 2004		
	Domestic Services	International Services	Corporate
Revenue from external customers	\$ 35,005	\$ 25,529	\$ --
Intersegment revenue	8	12	--
Revenue from significant customer	11,761	--	--
Segment operating income (loss)	(1,340)	258	--
Segment assets	51,924	57,059	4,808
Segment goodwill	23,896	12,366	--
Depreciation and amortization	658	193	--
Capital additions	414	127	931
	Three months ended March 31, 2003		
	Domestic Services	International Services	Corporate
Revenue from external customers	\$ 23,774	\$ 14,798	\$ --
Intersegment revenue	34	28	--
Revenue from significant customer	9,835	--	--
Segment operating income (loss)	262	466	(750)
Segment assets	38,539	14,056	1,809
Segment goodwill	15,309	5,002	--
Depreciation and amortization	521	69	--
Capital additions	344	37	1,353

The revenue in the table below is allocated to geographic areas based upon the location of the customer (in thousands):

	Three months ended March 31,	
	2004	2003
Total revenue:		
United States	\$53,246	\$38,123
Asia	6,071	449
North America (excluding the United States)	124	--
Europe	668	--
Other	425	--

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	-----	-----
Total	\$60,534	\$38,572
	=====	=====

The following table presents long-lived assets by geographic area:

	March 31,	
	2004	2003
	-----	-----
United States	\$7,892,979	\$4,730,653
Asia	400,770	17,385
	-----	-----
Total long-lived assets	\$8,293,749	\$4,748,038
	=====	=====

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### Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

#### Cautionary Statement For Forward-Looking Statements

This Quarterly Report on Form 10-Q includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, regarding future results, levels of activity, events, trends or plans. We have based these forward-looking statements on our current expectations and projections about such future results, levels of activity, events, trends or plans. These forward-looking statements are not guarantees and are subject to known and unknown risks, uncertainties and assumptions about us that may cause our actual results, levels of activity, events, trends or plans to be materially different from any future results, levels of activity, events, trends or plans expressed or implied by such forward-looking statements. In some cases, you can identify forward-looking statements by terminology such as "may", "will", "should", "could", "would", "expect", "plan", "anticipate", "believe", "estimate", "continue", or the negative of such terms or other similar expressions. While it is impossible to identify all of the factors that may cause our actual results, levels of activity, events, trends or plans to differ materially from those set forth in such forward-looking statements, such factors include the inherent risks associated with: (i) our ability to sustain an annual growth rate in revenues consistent with recent results, (ii) our ability to achieve targeted operating margins, (iii) our ability to identify, acquire, integrate and manage additional businesses in a manner which does not dilute our earnings per share, (iv) our ability to obtain the capital necessary to make additional acquisitions, (v) the uncertainty of future trading prices of our common stock and the impact such trading prices may have upon our ability to utilize our common stock to facilitate our fund raising efforts and associated acquisition strategy, (vi) the uncertain effect on the future trading price of our common stock associated with the possible additional issuance of securities upon the conversion or exercise of outstanding convertible securities and to satisfy existing contractual commitments, (vii) our dependence on certain large customers, (viii) our dependence upon certain key personnel, (ix) an unexpected adverse result in any legal proceeding, (x) the scarcity and competition for the operating companies we need to acquire to implement our business strategy, (xi) competition in the freight forwarding, logistics and supply chain management industry, (xii) the impact of current and future laws affecting the Company's operations, (xiii) adverse changes in general economic conditions as well as economic conditions affecting the specific industries and customers we serve,

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(xiv) regional disruptions in transportation, (xv) the risk that the actual results of recently acquired businesses are not consistent with their historical results and forward-looking guidance provided to us at the time of acquisition, and (xvi) other factors which are or may be identified from time to time in our Securities and Exchange Commission filings and other public announcements, including our most recent Annual Report on Form 10-K for the year ended December 31, 2003. Readers are cautioned not to place undue reliance on forward-looking statements, which speak only as of the date made. We undertake no obligation to publicly release the result of any revision of these forward-looking statements to reflect events or circumstances after the date they are made or to reflect the occurrence of unanticipated events.

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### OVERVIEW

We are a non-asset based third-party logistics services company providing supply chain solutions on a global basis. We offer a full range of time-definite transportation and distribution solutions through our Domestic Services platform, where we manage and arrange the movement of raw materials, supplies, components and finished goods for our customers. We offer a full range of international logistics services, including international air and ocean transportation as well as customs house brokerage services, through our International Services platform. In addition to these core service offerings, we also provide a broad range of value added supply chain management services, including warehousing, order fulfillment and inventory management solutions. We service a customer base of manufacturers, distributors and national retail chains through a network of offices in 21 major metropolitan areas in North America, Puerto Rico, ten locations in Asia and five locations in South America, using an extensive network of independent carriers and service partners strategically located around the world.

As a non-asset based provider of third-party logistics services, we seek to limit our investment in equipment, facilities and working capital through contracts and preferred provider arrangements with various transportation providers who generally provide us with favorable rates, minimum service levels, capacity assurances and priority handling status. The volume of our flow of freight enables us to negotiate attractive pricing with our transportation providers.

Our strategic objective is to build a leading global logistics services organization that integrates established operating businesses and innovative technologies. We plan to achieve this objective by broadening our network through a combination of synergistic acquisitions and the organic expansion of our existing base of operations. We are currently pursuing an aggressive acquisition strategy to enhance our position in our current markets and to acquire operations in new markets. The focus of this strategy is on acquiring businesses that have demonstrated historic levels of profitability, have a proven record of delivering high quality services, have a customer base of large and mid-sized companies and which otherwise may benefit from our long term growth strategy and status as a public company.

Our strategy has been designed to take advantage of shifting market dynamics. The third party logistics industry continues to grow as an increasing number of businesses outsource their logistics functions to more cost effectively manage and extract value from their supply chains. Also, we believe the industry is positioned for further consolidation as it remains highly fragmented, and as customers are demanding the types of sophisticated and broad-reaching service offerings that can more effectively be handled by larger, more diverse organizations. As a non-asset based provider of third party logistics services, we can focus on optimizing the transportation solution for

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our customers, rather than on our own asset utilization. Our non-asset based approach allows us to maintain a high level of operating flexibility and leverage a cost structure that is highly variable in nature.

Our acquisition strategy relies upon two primary factors: first, our ability to identify and acquire target businesses that fit within our general acquisition criteria and, second, the continued availability of capital and financing resources sufficient to complete these acquisitions. Our growth strategy relies upon a number of factors, including our ability to efficiently integrate the businesses of the companies we acquire, generate the anticipated economies of scale from the integration, and maintain the historic sales growth of the acquired businesses so as to generate continued organic growth. There are a variety of risks associated with our ability to achieve our strategic objectives, including our ability to acquire and profitably manage additional businesses, our current reliance on a small number of key customers, the risks inherent in international operations, and the intense competition in our industry for customers and for the acquisition of additional businesses. The business risks associated with these factors are identified or referred to above under our "Cautionary Statement for Forward-Looking Statements."

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Our principal source of income is derived from freight forwarding services. As a freight forwarder, we arrange for the shipment of our customers' freight from point of origin to point of destination. Generally, we quote our customers a turn key cost for the movement of their freight. Our price quote will often depend upon the customer's time-definite needs (first day through fifth day delivery), special handling needs (heavy equipment, delicate items, environmentally sensitive goods, electronic components, etc.) and the means of transport (truck, air, ocean or rail). In turn, we assume the responsibility for arranging and paying for the underlying means of transportation.

We also provide a range of other services including customs brokerage, warehousing and other services, which include customized distribution, fulfillment, and other value added supply chain services.

Total revenue represents the total dollar value of services we sell to our customers. Our cost of transportation includes direct costs of transportation, including motor carrier, air, ocean and rail services. We act principally as the service provider to add value in the execution and procurement of these services to our customers. Our net transportation revenue (gross transportation revenue less the direct cost of transportation) is the primary indicator of our ability to source, add value and resell services provided by third parties, and is considered by management to be a key performance measure. We believe that net revenue is also an important measure of economic performance. Net revenue includes transportation revenue and our fee-based activities, after giving effect to the cost of transportation. In addition, management believes measuring its operating costs as a function of net revenue provides a useful metric, as our ability to control costs as a function of net revenue directly impacts operating earnings. With respect to our services other than freight transportation, net revenue is identical to gross revenue.

A significant portion of our revenue is derived from our international operations, and the growth of those operations is an important part of our business strategy. Our current international operations are focused on the shipment of goods into and out of the United States and are dependent on the volume of international trade with the United States. Our strategic plan contemplates the growth of those operations, as well as the expansion into the transportation of goods wholly outside of the United States. The following factors could adversely affect our current international operations, as well as the growth of those operations:

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- the political and economic systems in certain international markets are less stable than in the United States;
- wars, civil unrest, acts of terrorism and other conflicts exist in certain international markets;
- export restrictions, tariffs, licenses and other trade barriers can adversely affect the international trade serviced by our international operations;
- managing distant operations with different local market conditions and practices is more difficult than managing domestic operations;
- differing technology standards in other countries present difficulties and expense in integrating our services across international markets;
- complex foreign laws and treaties can adversely affect our ability to compete; and
- our ability to repatriate funds may be limited by foreign exchange controls.

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Our operating results will be affected as acquisitions occur. Since all acquisitions are made using the purchase method of accounting for business combinations, our financial statements will only include the results of operations and cash flows of acquired companies for periods subsequent to the date of acquisition. To help facilitate the consolidation, analysis and public reporting process, our offshore operations are included within our consolidated results on a one-month lag, or more specifically, our calendar year results will include results from offshore operations for the period December 1 through November 30. As a result of the one-month lag, the earnings impact of the Shaanxi transaction will be first reflected in our consolidated results starting in April 2004.

Our GAAP based net income will also be affected by non-cash charges relating to the amortization of customer related intangible assets and other intangible assets arising from our completed acquisitions. Under applicable accounting standards, purchasers are required to allocate the total consideration in a business combination to the identified assets acquired and liabilities assumed based on their fair values at the time of acquisition. The excess of the consideration paid over the fair value of the identifiable net assets acquired is to be allocated to goodwill, which is tested at least annually for impairment. Applicable accounting standards require the Company to separately account for and value certain identifiable intangible assets based on the unique facts and circumstances of each acquisition. As a result of the Company's acquisition strategy, our net income will include material non-cash charges relating to the amortization of customer related intangible assets and other intangible assets acquired in our acquisitions. Although these charges may increase as the Company completes more acquisitions, we believe we are actually growing the value of our intangible assets (e.g., customer relationships). Thus, we believe that earnings before interest, taxes, depreciation and amortization, or EBITDA, is a useful financial measure for investors because it eliminates the effect of these non-cash costs and provides an important metric for our business. Accordingly, we employ EBITDA as a measure of our historical financial performance and as a benchmark for future guidance.

Our operating results are also subject to seasonal trends when measured on a quarterly basis. Our first and second quarters are likely to be weaker as compared with our other fiscal quarters, which we believe is consistent with the operating results of other supply chain service providers. This trend is dependent on numerous factors, including the markets in which we operate, holiday seasons, consumer demand and economic conditions. Since our revenue is largely derived from customers whose shipments are dependent upon consumer



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demand and just-in-time production schedules, the timing of our revenue is often beyond our control. Factors such as shifting demand for retail goods and/or manufacturing production delays could unexpectedly affect the timing of our revenue. As we increase the scale of our operations, seasonal trends in one area may be offset to an extent by opposite trends in another area. We cannot accurately predict the timing of these factors, nor can we accurately estimate the impact of any particular factor, and thus we can give no assurance that historical seasonal patterns will continue in future periods.

### CRITICAL ACCOUNTING POLICIES

Our accounting policies, which are in compliance with accounting principles generally accepted in the United States, require us to apply methodologies, estimates and judgments that have a significant impact on the results we report in our financial statements. In our Annual Report on Form 10-K for the year ended December 31, 2003 we have discussed those policies that we believe are critical and require the use of complex judgment in their application. Since the date of that Form 10-K, there have been no material changes to our critical accounting policies or the methodologies or assumptions applied under them.

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### RESULTS OF OPERATIONS

Quarter ended March 31, 2004 compared to quarter ended March 31, 2003

The following table summarizes our total revenue, net transportation and other revenue (in thousands):

	Quarter ended March 31,		Change	
	2004	2003	Amount	Percent
Total revenue	\$ 60,534	\$ 38,572	\$ 21,962	56.9%
Transportation revenue	\$ 55,355	\$ 35,780	\$ 19,575	54.7
Cost of transportation	42,810	26,388	16,422	62.2
Net transportation revenue	12,545	9,392	3,153	33.6
Net transportation margins	22.7%	26.2%		
Customs brokerage	2,679	1,864	815	43.7
Warehousing and other value added services	2,500	928	1,572	169.4
 Total net revenue	 \$ 17,724	 \$ 12,184	 \$ 5,540	 45.5%
Net revenue margin	29.3%	31.6%		

Total revenue was \$60.5 million in the first quarter of 2004, an increase of 56.9% over total revenue of \$38.6 million in the first quarter of

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2003. \$13.6 million or 62.1% of the increase in total revenue was attributable to organic growth with \$8.3 million or 37.9% of the increase in total revenue attributable to acquisitions. The Domestic Services platform delivered \$35.0 million in total revenue for the first quarter of 2004, an improvement of \$11.2 million and 47.1% over the same prior year period with \$8.7 million of the increase coming from same store growth and the remaining \$2.5 million in revenue growth coming from acquisitions. The International Services platform delivered \$25.5 million in total revenue for the first quarter of 2004, a year over year improvement of \$10.7 million or 72.3%, with \$4.9 million of the increase coming from same store growth and the remaining \$5.8 million improvement attributed to acquisitions.

Net transportation revenue was \$12.5 million in the first quarter of 2004, an increase of 33.6% over net transportation revenue of \$9.4 million in the first quarter of 2003. \$1.5 million, or 48.4% of the increase in net transportation revenue, was attributable to same store growth with \$1.6 million, or 51.6% of the increase, attributable to acquisitions. The Domestic Services platform delivered \$9.3 million in net transportation revenue for the first quarter of 2004, an improvement of \$1.9 million or 25.7% over the same prior year period, with \$1.3 million of the increase coming from same store growth and the remaining \$0.6 million in growth coming from acquisitions. The International Services platform delivered \$3.2 million in net transportation revenue for the first quarter of 2004, a year over year improvement of \$1.2 million or 60.0%, with \$0.2 million of the increase coming from same store growth and the remaining \$1.0 million improvement attributed to acquisitions.

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Net transportation margins decreased to 22.7% for the first quarter of 2004 from 26.2% for the first quarter of 2003. For the first quarter of 2004, net transportation margins for the Domestic Services platform declined to 28.4% from 32.2% tied primarily to one piece of low-margin business that the Company expects to discontinue by the end of the second quarter of 2004. For the International Services platform, net transportation margins declined to 14.2% from 15.5% driven primarily by general rate increases taken by the underlying asset-based carriers that we have not been able to pass along to our customers.

Net revenue was \$17.7 million in the first quarter of 2004, an increase of 45.5% over net revenue of \$12.2 million in the first quarter of 2003. \$3.5 million, or 63.6% of the increase in net revenue, was attributable to same store growth, with \$2.0 million, or 36.4% of the increase, attributable to acquisitions. The Domestic Services platform delivered \$11.5 million in net revenue for the first quarter of 2004, an improvement of \$3.3 million or 40.2% over the same prior year period with \$2.5 million of the increase coming from same store growth with the remaining \$0.8 million in growth coming from acquisitions. The International Services platform delivered \$6.2 million in net revenue for the first quarter of 2004, a year over year improvement of \$2.2 million or 55.0%, with \$1.0 million of the increase coming from same store growth and the remaining \$1.2 million improvement attributed to acquisitions.

Net revenue margins decreased to 29.3% for the first quarter of 2004 compared to 31.6% for the same prior year period. Net revenue margins at Domestic Services declined to 32.9% from 34.3% driven primary from the low margin business that will be winding down by the end of the second quarter of 2004. For the International Services platform, net transportation margins declined to 24.4% from 27.2% driven primarily by general rate increases taken by the underlying asset-based carriers that we have not been able to pass along to our customers.

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The following table compares certain consolidated statement of operations data as a percentage of our net revenue (in thousands):

	Quarter ended March 31,			
	2004		2003	
	Amount	Percent	Amount	Percent
Net revenue	\$17,724	100.0	\$12,184	100.0
Personnel costs	9,898	55.8	6,563	53.9
Other selling, general and administrative	8,057	45.5	4,303	35.3
Depreciation and amortization	851	4.8	590	4.8
Litigation settlement	--	--	750	6.2
Total operating costs	18,806	106.1	12,206	100.2
Loss from operations	(1,082)	(6.1)	(22)	(0.2)
Other income (expense), net	(51)	(0.3)	30	0.2
Income (loss) before income tax expense (benefit) and minority interest	(1,133)	(6.4)	8	--
Income tax expense (benefit)	(418)	(2.4)	15	0.1
Loss before minority interest	(715)	(4.0)	(7)	(0.1)
Minority interest	70	0.4	--	--
Net loss attributable to common stockholders	\$ (785)	(4.4)	\$ (7)	(0.1)

Personnel costs were \$9.9 million for the first quarter of 2004, an increase of 50.8% over \$6.6 million for the first quarter of 2003. \$0.8 million or 24.2% of the increase in personnel costs is attributable to incremental costs assumed as part of our acquisition program with \$2.5 million or 75.8% of the increase attributable to increased costs in the base business. Personnel costs as a percentage of net revenue increased to 55.8% in the first quarter of 2004 from 53.9% in the first quarter of 2003. This increase was driven by hiring of operations, sales and management personnel, particularly in our International Services platform. For the comparable prior year period, headcount increased by 570 to a total of 1,098 with 414 added in operations, 45 added in sales and marketing and 111 added in financial and administrative services.

Other selling, general and administrative costs were \$8.1 million for the first quarter of 2004, an increase of 87.2% over \$4.3 million for the first quarter of 2003. \$0.6 million or 15.8% of the increase is attributable to incremental costs assumed as part of our acquisition program with \$3.2 million or 84.2% of the increase attributable to increased costs of the base business. As a percentage of net revenue, other selling, general and administrative costs increased to 45.5% in the first quarter of 2004 from 35.3% in the first quarter of 2003. This increase is primarily due to spending related to facilities, equipment and technology particularly in our Domestic Services platform.

Depreciation and amortization was \$0.9 million in the first quarter of 2004, an increase of 44.2% over \$0.6 million in the first quarter of 2003. This increase is primarily due to the amortization of intangible assets acquired.

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Depreciation and amortization as a percentage of net revenue remained constant at 4.8%.

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In the first quarter of 2003, litigation settlement charges resulted from the settlement of litigation that arose prior to our transition to a logistics business. Such settlement was ultimately paid using \$400,000 in cash and \$350,000 in shares of the Company's common stock.

Loss from operations was \$1.1 million in the first quarter of 2004, as compared to breakeven results for the first quarter of 2003. Loss from operations as a percentage of net revenue was (6.1%) for the first quarter of 2004.

As a result of historical losses related to investments in early-stage technology businesses, the Company has accumulated federal net operating losses (NOLs). In the fourth quarter of 2003, we reversed \$3.0 million of the valuation allowance based on the Company's history of profitable operations for the past year and projected profitability in the near future. In addition we also recorded a deferred tax liability generated principally by the tax amortization of goodwill, which is deductible for tax purposes over a life of 15 years but is not amortized for book purposes. As a result, we recognized a non-cash net tax benefit of \$1.7 million in 2003. The Company has approximately \$17.8 million of NOLs as of December 31, 2003 to offset future federal taxable income. Due to the NOLs, the Company was only subject to certain state and foreign taxes which resulted in a tax provision of approximately \$15,000 in 2003.

Net loss attributable to common stockholders was \$0.8 million in the first quarter of 2004, compared to breakeven results in the first quarter of 2003. Basic and diluted loss per common share was \$0.02 for the first quarter of 2004 compared to \$0.00 per basic and diluted common share for the first quarter of 2003.

### FINANCIAL OUTLOOK

Based on our first quarter results and outlook for the balance of the year, we are forecasting earnings before interest, taxes, depreciation and amortization, or EBITDA, of \$11.0 million on expected total revenue of \$325.0 million and expect net income of \$5.5 million. This guidance is based on the current platform and visibility to new customers in our sales pipeline but does not include any incremental acquisitions that we might complete over the course of 2004. In general, we expect to deploy \$10.0 to \$20.0 million per year in support of our acquisition strategy which would be funded through a combination of existing cash, draws upon our credit facility, the proceeds of new financings and the value of newly issued securities. Based on our acquisition model, this could generate incremental annualized EBITDA in the range of \$4.0 to \$8.0 million. Based on the recent erosion in our stock price, however, our acquisition activity over the course of 2004 is likely to be at the low end of this range.

We believe that EBITDA is a useful financial measure for investors because it eliminates the effect of non-cash costs associated with the amortization of customer intangibles arising from the Company's acquisition strategy. A reconciliation of EBITDA to the most directly comparable GAAP measure in accordance with SEC Regulation S-K follows:

	(amounts in millions)	
	2003A	2004E
	-----	-----
Net income	\$7.1	\$ 5.5

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Interest expense/(income)	0.2	0.5
Income tax expense/(benefit)*	(1.3)	-
Depreciation and amortization	2.6	5.0
	----	----
EBITDA (Earnings before interest, taxes, depreciation and amortization)	\$8.6	\$11.0
	====	=====

\* Prior to the fourth quarter of 2003, the Company maintained a valuation allowance to offset 100% of the net deferred tax assets associated with the tax losses generated prior to the Company's move into the logistics business. In the fourth quarter of 2003, a portion of the valuation allowance was reversed, resulting in the recognition of a deferred tax asset and related nonrecurring non-cash tax benefit of \$1.7 million, resulting in an overall income tax benefit of \$1.3 million. For purposes of developing its 2004 net earnings guidance, the Company has assumed that an additional portion of the valuation allowance will be reversed in 2004 that will result in additional tax benefits to offset any tax expense for the year.

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Our revenue and net income estimates have been developed based on a number of principal assumptions including, among others: (i) our ability to sustain revenue growth rates consistent with recent results, (ii) our ability to achieve targeted operating margins, (iii) that no material economic or customer disruptions will occur, (iv) that we will not be required to repay some portion or all of the \$1.3 million received by us as a payment of pre-petition indebtedness during the bankruptcy of a material customer, (v) that we will not be caused to incur additional charges as a result of the bankruptcy of FAO, Inc., a significant customer of the recently acquired business of Regroup, (vi) that we continue to maintain existing relationships with key employees, (vii) that there is no unexpected adverse result in any legal proceeding, and (viii) that other factors which are or may be identified from time to time in our SEC filings and other public announcements, including our most recent Annual Report on Form 10-K for the year ended December 31, 2003, will not have an adverse effect on our operations. Furthermore, our estimates as to the expected financial results that may be realized from our recent acquisitions have been developed based on the historical results and forward looking guidance provided to us at the time of such each transaction. We may need to adjust our 2004 guidance if the results of operations of the acquired businesses in 2004 are inconsistent with the historical and forward-looking guidance provided to us by the sellers of those businesses. These adjustments could materially affect our 2004 estimates.

Assuming we can continue to execute on our business plan and acquisition model without any material disruptions, and identify and close transactions similar to transactions accomplished to date, it is our goal to generate \$500.0 million in annualized revenue by the end of 2006.

Notwithstanding our expectations regarding our ability to deliver these results, we can never be certain that future revenue or earnings will be achieved at any particular level. Estimates of future financial performance are forward-looking statements and are subject to uncertainty created by the risk elements otherwise identified in our Annual Report on Form 10-K for the year ended December 31, 2003 under "Risks Particular to our Business." Furthermore, even though we believe our current operations will achieve a certain level of earnings on an annual basis, our results are subject to seasonal trends.

SOURCES OF GROWTH

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Management believes that a comparison of "same store" growth is critical in the evaluation of the quality and extent of the Company's internally generated growth. This "same store" analysis isolates the financial contributions from operations that have been included in the Company's operating results for the full comparable prior year period. The table below presents "same store" comparisons for the three-month period ended March 31, 2004 (which is the measure of any increase from the same period of 2003).

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	For the three months ended March 31, 2004
Domestic	38.0%
International	33.6%

### LIQUIDITY AND CAPITAL RESOURCES

Cash and cash equivalents totaled \$4.1 million and \$3.1 million as of March 31, 2004 and December 31, 2003, respectively. Working capital totaled \$14.5 million and \$16.3 million at March 31, 2004 and December 31, 2003, respectively.

Cash provided by operating activities was \$0.2 million for the first quarter of 2004 compared to \$0.7 million used in the first quarter of 2003. This quarter on quarter improvement was driven principally by the seasonal increase in our collection of receivables.

Net cash used in investing activities during the first quarter of 2004 was \$9.0 million compared to \$4.6 million in the first quarter of 2003. Investing activities were driven principally by approximately \$5.5 million in earn-out payments made in relation to 2003 performance targets, \$2.3 million paid for acquisitions (net of cash acquired) and \$0.7 million spent in connection with the roll-out of Tech-Logis(TM), the Company's new web-based technology platform.

Net cash provided by financing activities during the first quarter of 2004 was \$9.7 million compared to \$5.7 million in the first quarter of 2003. Financing activities consisted of \$8.6 million in proceeds from the Company's line of credit and \$1.2 million from the issuance of common stock upon the exercises of options and warrants, offset by principal payments of \$0.2 million for a capital lease. We may receive proceeds in the future from the exercise of options and warrants that were outstanding as of the end of the first quarter. As of March 31, 2004, approximately 13,170,000 options and warrants were outstanding.

	Number of shares	Proceeds if exercised
Options outstanding under our Stock Option Plan	10,684,217	\$ 17,181,613
Non-Plan Options	1,046,700	2,494,250
Warrants	1,439,563	1,499,573
	-----	-----
Total	13,170,480	\$ 21,175,436
	=====	=====

To ensure that we have adequate near-term liquidity, we maintain a revolving credit facility of \$20.0 million (the "Facility") with LaSalle

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Business Credit, Inc. that is collateralized by accounts receivable and other assets of the Company and its subsidiaries. The Facility requires the Company and its subsidiaries to comply with certain financial covenants. Advances under the Facility are available to fund future acquisitions, capital expenditures or for other corporate purposes.

As of May 1, 2004 we had advances of \$9.8 million and we had eligible accounts receivable sufficient to support \$16.5 million in borrowings. The terms of our Facility are subject to certain financial covenants which may limit the amount otherwise available under the Facility. Principal among these are financial covenants that limit availability based upon measures of our cash flow, as well as a multiple of funded debt to consolidated EBITDA of our domestic operations. Under the funded debt to consolidated EBITDA covenant, our funded debt is limited to a multiple of 2.75 of our domestic EBITDA measured on a rolling four quarter basis. Based on our rolling four quarter forecast, the domestic component of our current 2004 EBITDA guidance would provide capacity of approximately \$17.0 million under our Facility. If our rolling four quarter domestic EBITDA decreases, the availability under our Facility could be negatively impacted.

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Under the terms of the Facility, we are permitted to make additional acquisitions without the lender's consent only if certain conditions are satisfied. The conditions imposed by the Facility include the following: (i) the absence of an event of default under the Facility, (ii) the company to be acquired must be in the transportation and logistics industry, (iii) the purchase price to be paid must be consistent with our historical business and acquisition model, (iv) the undrawn availability under the Facility must average \$5.0 million for the 60 days preceding the acquisition and must be at least \$5.0 million after giving effect for the acquisition, (v) the lender must be reasonably satisfied with projected financial statements we provide covering a 12 month period following the acquisition, (vi) the acquisition documents must be provided to the lender and must be consistent with the description of the transaction provided to the lender, (vii) the aggregate cash disbursed to support the purchase and operation of our foreign operations must not exceed \$11.3 million, and (viii) the number of permitted acquisitions is limited to four per year (excluding any acquisitions for which the purchase price is payable solely in stock). In the event that we were not able to satisfy the conditions of the Facility in connection with a proposed acquisition, we would have to forego the acquisition unless we either obtained the lender's consent or retired the Facility. This may limit or slow our ability to achieve the critical mass we may need to achieve our strategic objectives.

We believe that our current working capital and anticipated cash flow from operations are adequate to fund existing operations and to implement our acquisition strategy in the near term. However, our ability to finance further acquisitions is limited by the availability of additional capital. We may finance acquisitions, however, using our common stock as all or some portion of the consideration. In the event that our common stock does not attain or maintain a sufficient market value or potential acquisition candidates are otherwise unwilling to accept our securities as part of the purchase price for the sale of their businesses, we may be required to utilize more of our cash resources, if available, in order to continue our acquisition program. If we do not have sufficient cash resources through either operations or from debt facilities, our growth could be limited unless we are able to obtain such additional capital.

We have used a significant amount of our available capital to finance acquisitions. Our acquisitions are normally structured with certain amounts paid at closing, and the balance paid over a number of years in the form of earn-out

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installments which are payable based upon the future earnings of the acquired businesses. We will be required to make significant payments in the future if the earn-out installments under our various acquisitions become due. While we believe that a portion of the required payments will be generated by the acquired businesses, we may have to secure additional sources of capital to fund the remainder of the earn-out payments as they become due. This presents us with certain business risks relative to the availability of capacity under our Facility, the availability and pricing of future fund raising, as well as the potential dilution to our stockholders if the fund raising involves the sale of equity.

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Below are descriptions of material acquisitions made since 2001 including a breakdown of consideration paid at closing and future potential earn-out payments. We define "material acquisitions" as those with aggregate potential consideration of \$5.0 million or more.

On October 5, 2001, we acquired Air Plus, a group of Minneapolis-based privately held companies that provide a full range of logistics and transportation services. The transaction was valued at up to \$34.5 million, consisting of cash of \$17.5 million paid at closing and a four-year earn-out arrangement of up to \$17.0 million. In the earn-out, we agreed to pay the former Air Plus shareholders installments of \$3.0 million in 2003, \$5.0 million in 2004, \$5.0 million in 2005 and \$4.0 million in 2006, with each installment payable in full if Air Plus achieves pre-tax income of \$6.0 million in each of the years preceding the year of payment. In the event there is a shortfall in pre-tax income, the earn-out payment will be reduced on a dollar-for-dollar basis to the extent of the shortfall. Shortfalls may be carried over or carried back to the extent that pre-tax income in any other payout year exceeds the \$6.0 million level. Based upon 2003 performance, the former Air Plus shareholders received \$5.0 million on March 31, 2004. On a cumulative basis, Air Plus has generated \$12.8 million in adjusted earnings, providing its former shareholders with a total of \$8.0 million in earn-out payments and excess earnings of \$0.8 million to carryforward and apply to future earnings targets. In total, the former Air Plus shareholders have elected to receive \$7.6 million in cash with the balance paid in Company common stock.

On April 4, 2002, we acquired Stonepath Logistics International Services, Inc. ("SLIS") (f/k/a Global Transportation Services, Inc.), a Seattle-based privately held company that provides a full range of international air and ocean logistics services. The transaction was valued at up to \$12.0 million, consisting of cash of \$5.0 million paid at the closing and up to an additional \$7.0 million payable over a five year earn-out period based upon the future financial performance of SLIS. We agreed to pay the former Global shareholders a total of \$5.0 million in base earn-out payments payable in installments of \$0.8 million in 2003, \$1.0 million in 2004 through 2007 and \$0.2 million in 2008, with each installment payable in full if SLIS achieves pre-tax income of \$2.0 million in each of the years preceding the year of payment (or the pro rata portion thereof in 2002 and 2007). In the event there is a shortfall in pre-tax income, the earn-out payment will be reduced on a pro-rata basis. Shortfalls may be carried over or carried back to the extent that pre-tax income in any other payout year exceeds the \$2.0 million level. We also provided the former Global shareholders with an additional incentive to generate earnings in excess of the base \$2.0 million annual earnings target ("SLIS' tier-two earn-out"). Under SLIS' tier-two earn-out, the former Global shareholders are also entitled to receive 40% of the cumulative pre-tax earnings in excess of \$10.0 million generated during the five-year earn-out period subject to a maximum additional earn-out opportunity of \$2.0 million. SLIS would need to generate cumulative earnings of \$15.0 million over the five-year earn-out period to receive the full \$7.0 million in contingent earn-out payments. Based upon



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2003 performance, the former Global shareholders received \$1.0 million on April 1, 2004. On a cumulative basis, SLIS has generated \$9.3 million in adjusted earnings, providing its former shareholders with a total of \$1.8 million in cash earn-out payments and excess earnings of \$5.8 million to carryforward and apply to future earnings targets.

On May 30, 2002, we acquired United American, a Detroit-based privately held provider of expedited transportation services. The United American transaction provided us with a new time-definite service offering focused on the automotive industry. The transaction was valued at up to \$16.1 million, consisting of cash of \$5.1 million paid at closing and a four-year earn-out arrangement based upon the future financial performance of United American. We agreed to pay the former United American shareholder a total of \$5.0 million in base earn-out payments payable in installments of \$1.25 million in 2003 through 2006, with each installment payable in full if United American achieves pre-tax income of \$2.2 million in each of the years preceding the year of payment. In the event there is a shortfall in pre-tax income, the earn-out payment will be reduced on a dollar-for-dollar basis to the extent of the shortfall. Shortfalls may be carried over or carried back to the extent that pre-tax income in any other payout year exceeds the \$2.2 million level. The Company has also provided the former United American shareholder with an additional incentive to generate earnings in excess of the base \$2.2 million annual earnings target ("United American's tier-two earn-out"). Under United American's tier-two earn-out, the former United American shareholder is entitled to receive 50% of the cumulative pre-tax earnings generated by a certain pre-acquisition customer in excess of \$8.8 million during the four-year earn-out period subject to a maximum additional earn-out opportunity of \$6.0 million. United American would need to generate cumulative earnings of \$20.8 million over the four-year earn-out period to receive the full \$11.0 million in contingent earn-out payments. Based upon 2003 performance, the former United American shareholder received \$0.2 million on April 1, 2004. On a cumulative basis, United American has generated \$2.4 million in adjusted earnings, providing its former shareholder with a total of \$0.5 million in cash earn-out payments and a cumulative earnings shortfall of \$2.0 million. In future years, earnings in excess of the \$2.2 million target would first be applied against the \$2.0 million shortfall.

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On June 20, 2003, through our indirect wholly owned subsidiary, Stonepath Logistics Government Services, we acquired the business of Regroup, a Virginia limited liability company. The Regroup transaction enhanced our presence in the Washington, D.C. market and provided a platform to focus on the logistics needs of U.S. government agencies and contractors. The transaction was valued at up to \$27.2 million, consisting of cash of \$3.7 million and \$1.0 million of Company stock paid at closing, and a five-year earn-out arrangement. The Company agreed to pay the members of Regroup a total of \$10.0 million in base earn-out payments payable in equal installments of \$2.5 million in 2005 through 2008, if Regroup achieves pre-tax income of \$3.5 million in each of the years preceding the year of payment. In the event there is a shortfall in pre-tax income, the earn-out payment will be reduced on a dollar-for-dollar basis. Shortfalls may be carried over or carried back to the extent that pre-tax income in any other payout year exceeds the \$3.5 million level. The Company has also agreed to pay the former members of Regroup an additional \$2.5 million if Regroup earns \$3.5 million in pre-tax income during the 12-month period commencing July 1, 2003. In addition, the Company has also provided the former members of Regroup with an additional incentive to generate earnings in excess of the base \$3.5 million annual earnings target ("Regroup's tier-two earn-out"). Under Regroup's tier-two earn-out, the former members of Regroup are also entitled to receive 50% of the cumulative pre-tax earnings in excess of \$17.5 million generated during the five-year earn-out period subject to a maximum additional earn-out opportunity of \$10.0 million. Regroup would need to generate

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cumulative earnings of \$37.5 million over the five-year earn-out period in order for the former members to receive the full \$22.5 million in contingent earn-out payments.

On August 8, 2003, through two indirect international subsidiaries, we acquired a seventy (70%) percent interest in the assets and operations of the Singapore and Cambodia based operations of the G-Link Group, which provide a full range of international logistics services, including international air and ocean transportation, to a worldwide customer base of manufacturers and distributors. This transaction substantially increased our presence in Southeast Asia and expanded our network of owned offices through which to deliver global supply chain solutions. The transaction was valued at up to \$6.2 million, consisting of cash of \$2.8 million, \$0.9 million of the Company's common stock paid at the closing and an additional \$2.5 million payable over a four-year earn-out period based upon the future financial performance of the acquired operations. We agreed to pay \$2.5 million in base earn-out payments payable in installments of \$0.3 million in 2004, \$0.6 million in 2005 through 2006 and \$1.0 million in 2007, with each installment payable in full if the acquired operations achieve pre-tax income of \$1.8 million in each of the years preceding the year of payment (or the pro rata portion thereof in 2003 and 2007). In the event there is a shortfall in pre-tax income, the earn-out payment will be reduced on a dollar-for-dollar basis. Shortfalls may be carried over or carried back to the extent that pre-tax income in any other payout year exceeds the \$1.8 million level. As additional purchase price, the Company also agreed to pay G-Link for excess net assets amounting to \$1.5 million through the issuance of Company common stock, on a post-closing basis. Based upon 2003 performance, G-Link received an earn-out payment of \$0.2 million on April 1, 2004.

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On February 9, 2004, through a wholly-owned subsidiary, we acquired a 55% interest in Shanghai-based Shaanxi Sunshine Cargo Services International Co., Ltd. (Shaanxi) Shaanxi provides a wide range of customized transportation and logistics services and supply chain solutions. The transaction is valued at up to \$11.0 million, consisting of cash of \$3.5 million and \$2.0 million of the Company's common stock paid at the closing, plus up to an additional \$5.5 million payable over a five-year period based upon the future financial performance of Shaanxi. The earn-out payments are due in five installments of \$1.1 million beginning in 2005, with each installment payable in full if Shaanxi achieves pre-tax income of at least \$4.0 million in each of the earn-out years. In the event there is a shortfall in pre-tax income, the earn-out payment for that year will be reduced on a dollar-for-dollar basis by the amount of the shortfall. Shortfalls may be carried over or back to the extent that pre-tax income in any other payout year exceeds the \$4.0 million level. As additional purchase price, on a post-closing basis the Company has agreed to pay Shaanxi for 55% of its closing date working capital. The common shares issued in the transaction are subject to a one year restriction on sale and are subject to a pro rata forfeiture based upon a formula that compares the actual pre-tax income of Shaanxi through December 31, 2004 with the targeted level of income of \$4.0 million (on an annualized basis). Also, if the trading price of the Company's common stock is less than \$3.17 per share at the end of the one year restriction, the Company will issue additional shares to the seller.

We will be required to make significant payments in the future if the earn-out installments under our various acquisitions become due. While we believe that a significant portion of the required payments will be generated by the acquired subsidiaries, we may have to secure additional sources of capital to fund some portion of the earn-out payments as they become due. This presents us with certain business risks relative to the availability and pricing of future fund raising, as well as the potential dilution to our stockholders if the fund raising involves the sale of equity.

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The following table summarizes our contingent base earn-out payments for the years indicated based on results of the prior year (in thousands) (1) (2):

	2005	2006	2007	2008	2009
-----					
Earn-out payments:					
Domestic	\$ 9,040	\$ 8,050	\$ 2,500	\$ 2,500	\$ --
International	3,904	3,904	4,276	2,542	2,010
	-----	-----	-----	-----	-----
Total earn-out payments	\$ 12,944	\$ 11,954	\$ 6,776	\$ 5,042	\$ 2,010
	=====	=====	=====	=====	=====
Prior year pre-tax earnings targets(3)					
Domestic	\$ 12,306	\$ 12,306	\$ 3,500	\$ 3,500	\$ --
International	10,546	10,546	11,602	6,940	5,823
	-----	-----	-----	-----	-----
Total pre-tax earnings targets	\$ 22,852	\$ 22,852	\$ 15,102	\$ 10,440	\$ 5,823
	=====	=====	=====	=====	=====
Earn-outs as a percentage of prior year pre-tax earnings targets:					
Domestic	73.5%	65.4%	71.4%	71.4%	--
International	37.0%	37.0%	36.9%	36.6%	34.5%
Combined	56.6%	52.3%	44.9%	48.3%	34.5%

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- (1) Excludes the impact of prior year's pre-tax earnings carryforwards (excess or shortfalls versus earnings targets).
  - (2) During the 2003-2007 earn-out period, there is an additional contingent obligation related to tier-two earn-outs that could be as much as \$18.0 million if certain of the acquired companies generate an incremental \$37.0 million in pre-tax earnings.
  - (3) Aggregate pre-tax earnings targets as presented here identify the uniquely defined earnings targets of each acquisition and should not be interpreted to be the consolidated pre-tax earnings of the Company which would give effect for, among other things, amortization or impairment of intangible assets created in connection with each acquisition or various other expenses which may not be charged to the operating groups for purposes of calculating earn-outs.

The Company is a defendant in a number of legal proceedings, including one remaining material legal proceeding that arose prior to our transition to a logistics business. That proceeding has been identified in our Annual Report on Form 10-K for the year ended December 31, 2003. Although we believe that the claims asserted in these proceedings are without merit, and we intend to vigorously defend these matters, there is the possibility that the Company could incur material expenses in the defense and resolution of these matters. Furthermore, since the Company has not established any reserves in connection with such claims, any such liability, if at all, would be recorded as an expense in the period incurred or estimated. This amount, even if not material to the Company's overall financial condition, could adversely affect the Company's results of operations in the period recorded.

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One of the Company's customers which is the subject of a Chapter 11 proceeding under the Bankruptcy Code, paid to the Company approximately \$1.3 million of pre-petition indebtedness for shipping and delivery charges pursuant to an order of a United States Bankruptcy Court authorizing the payment of such charges. One of the creditors in the Chapter 11 proceeding appealed other orders of the Bankruptcy Court authorizing the payment of pre-petition indebtedness to other creditors for other charges and those orders have been reversed by a court proceeding. While no action has been taken in the Bankruptcy Court to challenge the payment made to the Company, if such action were taken in the future and that action were successful, the Company could be required to return all or a substantial portion of the payments made by the customer.

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

The Company's exposure to market risk for changes in interest rates relates primarily to the Company's investment portfolio and its line of credit. The Company does not have any derivative financial instruments in its investment portfolio. The Company is averse to principal loss and ensures the safety and preservation of its invested funds by limiting default risk, market risk and reinvestment risk. The Company invests its excess cash in institutional money market accounts. The Company does not use interest rate derivative instruments to manage its exposure to interest rate changes. If market interest rates were to change by 10% from the levels at March 31, 2004, the change in interest expense would have had an immaterial impact on the Company's results of operations and cash flows.

The Company also has exposure to foreign currency fluctuations with respect to its offshore subsidiaries. The Company does not utilize derivative instruments to manage such exposure. A hypothetical change of 10% in the value of the U.S. dollar would have had an immaterial impact on the Company's results of operations.

### Item 4. Controls and Procedures

As required by Rule 13a-15 under the Securities Exchange Act of 1934, as of the end of the period covered by this report, the Company carried out an evaluation of the effectiveness of the Company's disclosure controls and procedures. This evaluation was carried out under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer. Based upon that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures are effective. Other than as discussed in the fourth paragraph of this Item 4, there have been no significant changes in the Company's internal controls or in other factors, which could significantly affect internal controls subsequent to the date the Company carried out its evaluation.

Disclosure controls and procedures are designed to ensure that information required to be disclosed in Company reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed in Company reports filed under the Exchange Act is accumulated and communicated to management, including the Company's Chief Executive Officer and Chief Financial Officer as appropriate, to allow timely decisions regarding required disclosure.

In January 2004, the Company restated its consolidated statements of

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operations for the last three quarters of fiscal 2002, the first three quarters of fiscal 2003, and for the year ended December 31, 2002, as a result of an error discovered in the legacy accounting processes of Stonepath Logistics International Services, Inc. (f/k/a "Global Transportation Systems, Inc.") and Global Container Line, Inc., its wholly owned subsidiary. The Company determined that a process error existed which resulted in the failure to eliminate certain intercompany transactions in consolidation. This process error had been embedded within the legacy accounting processes of Global Transportation Systems, Inc. for a period which began substantially before its acquisition by the Company in April 2002.

The Company believes that the presence of this error, in and of itself, constitutes a reportable condition as defined under standards established by the American Institute of Certified Public Accountants. A reportable condition is a significant deficiency in the design or operation of internal controls, which could adversely affect an organization's ability to initiate, record, process and report financial data consistent with the assertions of management in the financial statements. To specifically respond to this matter, and in general to meet our obligations under Section 404 of the Sarbanes-Oxley Act of 2002, the Company commenced an overall review of its internal controls over financial reporting. As part of the assessment of its internal controls over financial reporting, the Company is focusing on its recent growth in terms of both size and complexity, coupled with the fact that its finance and accounting functions are largely decentralized. Although this review is not yet completed, the Company has initiated an immediate change in process to correct the error that occurred and to reduce the likelihood that a similar error could occur in the future.

As of the date of this Report, the Company believes it has a plan that, when completed, will eliminate the reportable condition described above. There were no other changes during the first quarter ended March 31, 2004 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

### Part II. OTHER INFORMATION

#### Item 1. Legal Proceedings

Other than as described in the Company's Annual Report on Form 10-K for the year ended December 31, 2003, there have been no material developments in any of the reported legal proceedings.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's overall consolidated financial position, results of operations or liquidity.

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#### Item 2. Changes in Securities, Use of Proceeds and Issuer Purchases of Equity Securities

Effective as of February 9, 2004, we issued 630,915 shares of our common stock to Andy Tsai in partial consideration for the acquisition of a controlling interest in Shaanxi. The shares were valued, for purposes of the acquisition, at \$2.0 million (\$3.17 per share), and were issued in a private placement transaction exempt from the registration requirements of the Securities Act of 1933 pursuant to Section 4(2) and Rule 506 thereunder as an issuer transaction not involving a public offering.

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### Item 3. Defaults Upon Senior Securities

None.

### Item 4. Submission of Matters to a Vote of Security Holders

None.

### Item 5. Other Information

None.

### Item 6. Exhibits and Reports on Form 8-K

(a) The following exhibits are included herein:

- 2.9 Amended and Restated Contract for the Sale of Assets by and between Stonepath Holdings (Hong Kong) Limited and Andy Tsai, dated November 10, 2003. (1)
- 2.10 Amendment Letter Agreement dated February 9, 2004, to the Amended and Restated Contract for the Sale of Assets by and between Stonepath Holdings (Hong Kong) Limited and Andy Tsai. (1)
- 10.14 Amendment to Executive Employment Agreement between Stonepath Logistics International Services, Inc. and Jason Totah dated April 1, 2004.
- 12 Calculation of Ratio of Earnings to Combined Fixed Charges and Preferred Stock Dividends.
- 31.1 Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Certification of Chief Executive Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (This exhibit shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section. Further, this exhibit shall not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.)
- 32.2 Certification of Chief Financial Officer Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. (This exhibit shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section. Further, this exhibit shall not be deemed to be incorporated by reference into any filing under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended.)

(1) Incorporated by reference to the Company's Current Report on Form 8-K dated February 9, 2004.

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(b) Reports on Form 8-K:

On February 24, 2004, the Company filed a Current Report on Form 8-K dated February 9, 2004, reporting under Item 2 on the acquisition of a majority interest in Shaanxi Sunshine Cargo Services International Co., Ltd.

On February 26, 2004, the Company furnished under Items 9 and 12 of Form 8-K, a copy of its earnings release dated February 25, 2004.

On February 27, 2004, the Company furnished an amendment to its Form 8-K dated February 26, 2004, to correct certain typographical errors inadvertently contained in the summary financial data tables that accompanied the February 25, 2004 earnings release.

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SIGNATURES

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

STONEPATH GROUP, INC.

Date: May 10, 2004

/s/ Dennis L. Pelino

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Dennis L. Pelino  
Chief Executive Officer and  
Chairman of the Board of Directors

Date: May 10, 2004

/s/ Bohn H. Crain

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Bohn H. Crain  
Chief Financial Officer and Treasurer

Date: May 10, 2004

/s/ Thomas L. Scully

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Thomas L. Scully  
Vice President and Controller and  
Principal Accounting Officer

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