

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 DECEMBER 28, 2003.

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TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.

COMMISSION FILE NUMBER 0-12919

PIZZA INN, INC.  
(EXACT NAME OF REGISTRANT IN ITS CHARTER)

MISSOURI 47-0654575  
(STATE OR OTHER JURISDICTION OF (I.R.S. EMPLOYER  
INCORPORATION OR ORGANIZATION) IDENTIFICATION NO.)

3551 PLANO PARKWAY  
THE COLONY, TEXAS 75056  
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES,  
INCLUDING ZIP CODE)

(469) 384-5000  
(REGISTRANT'S TELEPHONE NUMBER,  
INCLUDING AREA CODE)

INDICATE BY CHECK MARK WHETHER THE REGISTRANT (1) HAS FILED ALL REPORTS REQUIRED TO BE FILED BY SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 DURING THE PRECEDING 12 MONTHS (OR 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 12 B-2 OF THE EXCHANGE ACT). YES NO

INDICATE BY CHECK MARK WHETHER THE REGISTRANT HAS FILED ALL DOCUMENTS AND REPORTS REQUIRED TO BE FILED BY SECTIONS 12, 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934 SUBSEQUENT TO THE DISTRIBUTION OF SECURITIES UNDER A PLAN CONFIRMED BY A COURT. YES  NO

AT FEBRUARY 2, 2004, AN AGGREGATE OF 10,073,674 SHARES OF THE REGISTRANT'S COMMON STOCK, PAR VALUE OF \$.01 EACH (BEING THE REGISTRANT'S ONLY CLASS OF COMMON STOCK), WERE OUTSTANDING.

PIZZA INN, INC.

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PART 1. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

PIZZA INN, INC.  
CONSOLIDATED STATEMENTS OF OPERATIONS  
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)  
(UNAUDITED)

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	DECEMBER 28, 2003	DECEMBER 29, 2002	DECEMBER 28, 2003	DECEMBER 29, 2002
REVENUES:				
Food and supply sales . . . . .	\$ 13,032	\$ 13,275	\$ 26,530	\$ 26,804
Franchise revenue . . . . .	1,264	1,307	2,715	2,609
Restaurant sales . . . . .	376	453	782	920
Other income . . . . .	97	129	118	192
	-----	-----	-----	-----
	14,769	15,164	30,145	30,525
	-----	-----	-----	-----
COSTS AND EXPENSES:				
Cost of sales . . . . .	12,074	12,167	24,671	24,572
Franchise expenses . . . . .	728	835	1,542	1,543
General and administrative expenses . . . . .	962	(910)	2,003	649
Interest expense . . . . .	160	205	320	434
	-----	-----	-----	-----
	13,924	12,297	28,536	27,198
	-----	-----	-----	-----
INCOME BEFORE INCOME TAXES . . . . .	845	2,867	1,609	3,327
Provision for income taxes . . . . .	287	975	547	1,131
	-----	-----	-----	-----
NET INCOME . . . . .	\$ 558	\$ 1,892	\$ 1,062	\$ 2,196
	=====	=====	=====	=====
BASIC EARNINGS PER COMMON SHARE . . . . .	\$ 0.06	\$ 0.19	\$ 0.11	\$ 0.22
	=====	=====	=====	=====
DILUTED EARNINGS PER COMMON SHARE . . . . .	\$ 0.06	\$ 0.19	\$ 0.11	\$ 0.22
	=====	=====	=====	=====
WEIGHTED AVERAGE COMMON SHARES . . . . .	10,071	10,058	10,065	10,058
	=====	=====	=====	=====
WEIGHTED AVERAGE COMMON AND POTENTIAL DILUTIVE COMMON SHARES . . . . .	10,123	10,060	10,104	10,059
	=====	=====	=====	=====

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(IN THOUSANDS)

	THREE MONTHS ENDED . . . . .		SIX MONTHS ENDED	
	DECEMBER 28, 2003	DECEMBER 29, 2002	DECEMBER 28, 2003	DECEMBER 29, 2002
Net Income . . . . .	\$ 558	\$ 1,892	\$ 1,062	\$ 2,196
Interest rate swap gain (loss) - (net of tax (expense) benefit of \$31 and \$2 and \$94 and \$141, respectively) . . . . .	(60)	(4)	(183)	(281)
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See accompanying Notes to Consolidated Financial Statements.

PIZZA INN, INC.  
CONSOLIDATED BALANCE SHEETS  
(IN THOUSANDS, EXCEPT SHARE AMOUNTS)

	DECEMBER 28, 2003		JUNE 29, 2003
	-----		-----
ASSETS			
(UNAUDITED)			
CURRENT ASSETS			
Cash and cash equivalents . . . . .	\$ 199		\$ 399
Accounts receivable, less allowance for doubtful accounts of \$340 and \$722, respectively . . . . .	4,346		3,730
Notes receivable, current portion, less allowance for doubtful accounts of \$53 and \$175, respectively . . . . .	260		260
Inventories . . . . .	1,461		1,511
Deferred taxes, net . . . . .	308		585
Prepaid expenses and other . . . . .	321		533
	-----		-----
Total current assets . . . . .	6,895		7,018
Property, plant and equipment, net . . . . .	12,922		13,126
Property under capital leases, net . . . . .	80		120
Deferred taxes, net . . . . .	189		382
Long-term notes receivable, less allowance for doubtful accounts of \$9 and \$19, respectively . . . . .	-		41
Deposits and other . . . . .	1,072		109
	-----		-----
	\$ 21,158		\$ 20,796
	=====		=====
LIABILITIES AND SHAREHOLDERS' EQUITY			
CURRENT LIABILITIES			
Accounts payable - trade . . . . .	\$ 1,489		\$ 1,217
Accrued expenses . . . . .	2,923		1,950
Current portion of long-term debt . . . . .	823		1,448
Current portion of capital lease obligations . . . . .	64		109
	-----		-----
Total current liabilities . . . . .	5,299		4,724
LONG-TERM LIABILITIES			
Long-term debt . . . . .	8,440		9,643
Long-term capital lease obligations . . . . .	28		33
Other long-term liabilities . . . . .	703		989
	-----		-----
	14,470		15,389
	-----		-----
SHAREHOLDERS' EQUITY			
Common Stock, \$.01 par value; authorized 26,000,000 shares; issued 14,971,319 and 14,956,319 shares, respectively; outstanding 10,073,674 and 10,058,674 shares, respectively . . . . .	150		150
Additional paid-in capital . . . . .	7,855		7,825
Loans to officers . . . . .	(562)		(569)
Retained earnings . . . . .	19,197		18,135
Accumulated other comprehensive loss . . . . .	(468)		(650)
Treasury stock at cost			
Shares in treasury: 4,897,645 and 4,897,645 respectively . . . . .	(19,484)		(19,484)
	-----		-----
Total shareholders' equity . . . . .	6,688		5,407
	-----		-----
	\$ 21,158		\$ 20,796
	=====		=====

See accompanying Notes to Consolidated Financial Statements.

PIZZA INN, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(IN THOUSANDS)  
(UNAUDITED)

SIX MONTHS ENDED  
-----  
DECEMBER 28,                      DECEMBER 29,  
2003                                      2002

CASH FLOWS FROM OPERATING ACTIVITIES:

Net income . . . . .	\$	1,062	\$	2,196
Adjustments to reconcile net income to cash provided by operating activities:				
Depreciation and amortization . . . . .		523		768
Non cash settlement of accounts receivable . . . . .		(281)		-
Recovery for bad debt, net . . . . .		(249)		(1,850)
Utilization of deferred taxes . . . . .		547		1,131
Changes in assets and liabilities:				
Notes and accounts receivable . . . . .		(344)		(402)
Inventories . . . . .		50		(229)
Accounts payable - trade . . . . .		272		776
Accrued expenses . . . . .		973		(165)
Prepaid expenses and other . . . . .		75		553
CASH PROVIDED BY OPERATING ACTIVITIES . . . . .		2,628		2,778

CASH FLOWS FROM INVESTING ACTIVITIES:

Proceeds from sale of assets . . . . .		26		-
Acquisition of area development territory . . . . .		(682)		-
Capital expenditures . . . . .		(331)		(236)
CASH USED FOR INVESTING ACTIVITIES . . . . .		(987)		(236)

CASH FLOWS FROM FINANCING ACTIVITIES:

Repayments of long-term bank debt and capital lease obligations		(1,878)		(5,063)
Officer loan payment . . . . .		7		1,950
Proceeds from exercise of stock options . . . . .		30		-
CASH USED FOR FINANCING ACTIVITIES . . . . .		(1,841)		(3,113)

Net decrease in cash and cash equivalents . . . . .		(200)		(571)
Cash and cash equivalents, beginning of period . . . . .		399		770
Cash and cash equivalents, end of period . . . . .	\$	199	\$	199

See accompanying Notes to Consolidated Financial Statements.

PIZZA INN, INC.  
 SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION  
 (IN THOUSANDS)  
 (UNAUDITED)

	SIX MONTHS ENDED	
	-----	-----
	DECEMBER 28, 2003	DECEMBER 29, 2002
	-----	-----

CASH PAYMENTS FOR:

Interest . . . . .	\$	328	\$	432
Income taxes . . . . .		-		-

NON-CASH FINANCING AND INVESTING ACTIVITIES:

Non-cash settlement of accounts receivable	\$	281	\$	-
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See accompanying Notes to Consolidated Financial Statements.

PIZZA INN, INC.  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
 (Unaudited)

(1) The accompanying condensed consolidated financial statements of Pizza Inn, Inc. (the "Company") have been prepared without audit pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in the financial statements have been

omitted pursuant to such rules and regulations. The condensed consolidated financial statements should be read in conjunction with the notes to the Company's audited condensed consolidated financial statements in its Form 10-K for the fiscal year ended June 29, 2003.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments necessary to fairly present the Company's financial position and results of operations for the interim periods. All adjustments contained herein are of a normal recurring nature.

The Company elected to follow APB No. 25, and related Interpretations in accounting for employee stock options because the alternative fair value accounting provided for under SFAS No. 123, "Accounting for Stock Based Compensation," requires use of option valuation models that were not developed for use in valuing employee stock options. Under APB No. 25, because the exercise price of our employee stock options equals or exceeds the fair value of the underlying stock on the date of grant, no compensation expense is recognized.

Pro forma information regarding net income and earnings per share is required to be determined as if the Company had accounted for its stock options granted subsequent to June 25, 1995 under the fair value method of SFAS No. 123. For purposes of pro forma disclosures, the estimated fair value of the stock options is amortized over the option vesting periods. The Company's pro forma information follows (in thousands, except for earnings per share information):

	SIX MONTHS ENDED	
	DECEMBER 28, 2003	DECEMBER 29, 2002
Net income, as reported. . . . .	\$ 1,062	\$ 2,196
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects. . . . .	(1)	(9)
Pro forma net income . . . . .	\$ 1,061	\$ 2,187
Earnings per share		
Basic-as reported. . . . .	\$ 0.11	\$ 0.22
Basic-pro forma. . . . .	\$ 0.11	\$ 0.22
Diluted-as reported. . . . .	\$ 0.11	\$ 0.22
Diluted-pro forma. . . . .	\$ 0.11	\$ 0.22

The effects of applying SFAS No. 123 in this pro forma disclosure are not indicative of future amounts as the pro forma amounts above do not include the impact of additional awards anticipated in future years.

The Company entered into an agreement effective December 29, 2002 with its current lender to provide a \$7.0 million revolving credit line that will expire December 31, 2004, replacing a \$9.5 million line that was due to expire December 31, 2003. The \$7.0 million revolving credit line will reduce quarterly by \$500,000 beginning March 31, 2003 through December 31, 2004. Interest on the revolving credit line is payable monthly. Interest is provided for at a rate equal to prime less an interest rate margin from 1.0% to 0.5% or, at the Company's option, at the LIBOR rate plus 1.25% to 1.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. A 0.375% to 0.5% annual commitment fee is payable on any unused portion of the revolving credit line. As of December 28, 2003 and December 29, 2002, the variable interest rates were 2.64% and 3.46%, respectively, using a LIBOR rate basis. Amounts outstanding under the revolving credit line as of December 28, 2003 and December 28, 2002 were \$1.5 million and \$2.4 million, respectively.

The Company entered into a term note effective March 31, 2000 with its current lender. The \$5,000,000 term note had outstanding balances of \$417,000 and \$1.7 million at December 28, 2003 and December 29, 2002, respectively. The term note requires monthly principal payments of \$104,000 with the balance maturing on March 31, 2004. Interest on the term loan is also payable monthly. Interest is provided for at a rate equal to prime less an interest rate margin of 0.75% or, at the Company's option, at the LIBOR rate plus 1.5%. As of December 28, 2003 and December 29, 2002, the variable interest rates were 2.69% and 2.94%, respectively.

The Company entered into an agreement effective December 28, 2000, as amended, with its current lender to provide up to \$8.125 million of financing for the construction of the Company's new headquarters, training center and distribution facility. The construction loan converted to a term loan effective January 31, 2002 with the unpaid principal balance to mature on December 28, 2007. This term loan will amortize over a term of twenty years, with principal payments of \$34,000 due monthly. Interest on this term loan is also payable monthly. Interest is provided for at a rate equal to prime less an interest rate margin of 0.75% or, at the Company's option, to the LIBOR rate plus 1.5%. As of December 28, 2003 and December 29, 2002, the variable interest rates were 2.65% and 2.89%, respectively. The Company, to fulfill bank requirements, has caused the outstanding principal amount to be subject to a fixed interest rate by utilizing an interest rate swap agreement as discussed below. The \$8.125 million term loan had an outstanding balance of \$7.3 million at December 28, 2003 and \$7.7 million at December 29, 2002.

(3) The Company entered into an interest rate swap effective February 27, 2001, as amended, designated as a cash flow hedge, to manage interest rate risk relating to the financing of the construction of the Company's new headquarters and to fulfill bank requirements. The swap agreement has a notional principal amount of \$8.125 million with a fixed pay rate of 5.84% which began November 1, 2001 and will end November 19, 2007. The swap's notional amount amortizes over a term of twenty years to parallel the terms of the term loan. SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" requires that for cash flow hedges, which hedge the exposure to variable cash flow of a forecasted transaction, the effective portion of the derivative's gain or loss be initially reported as a component of other comprehensive income in the equity section of the balance sheet and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any ineffective portion of the derivative's gain or loss is reported in earnings immediately. At December 28, 2003 there was no hedge ineffectiveness. The Company's expectation is that the hedging relationship will continue to be highly effective at achieving offsetting changes in cash flows.

(4) On April 30, 1998, Mid-South Pizza Development, Inc. ("Mid-South") entered into a promissory note whereby, among other things, Mid-South borrowed \$1,330,000 from a third party lender (the "Loan"). The proceeds of the Loan, less transaction costs, were used by Mid-South to purchase area developer rights from the Company for certain counties in Kentucky and Tennessee. Effective December 28, 2003, the Company reacquired all such area development rights from Mid-South. The Company paid approximately \$963,000 for these rights of which \$682,000 was a cash payment, and a non-cash settlement of accounts receivable of approximately \$281,000. A long-term asset was recorded for the same amount. Restaurants operating or developed in the reacquired territory will now pay all royalties and franchise fees directly to Pizza Inn, Inc. The asset will be amortized against actual incremental cash flows received, which is estimated to be approximately five years.

(5) On January 18, 2002 the Company was served with a lawsuit filed by Blakely-Witt & Associates, Inc. alleging Pizza Inn sent, or caused to be sent, unsolicited facsimile advertisements. The plaintiff has requested this matter be certified as a class action. We plan to vigorously defend our position in this litigation. We cannot assure you that we will prevail in this lawsuit and our defense could be costly and consume the time of our management. We are unable to predict the outcome of this case. However, an adverse resolution of this matter could materially affect our financial position and results of operations.

(6) In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46, "Consolidation of Variable Interest Entities, an interpretation of Accounting Research Bulletin No. 51," ("FIN 46"). FIN 46 requires the consolidation of entities in which an enterprise absorbs a majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both, as a result of ownership, contractual or other financial interests in the entity.

In October 2003, the FASB issued Staff Position No. 46-6, "Effective Date of FASB Interpretation No. 46, Consolidation of Variable Interest Entities," ("FSP FIN 46-6") in which the FASB deferred, for public companies, the required effective dates to implement FIN 46 for interests held in a variable interest entity ("VIE") or potential VIE that was created before February 1, 2003.

In December 2003, the FASB published a revision to FIN 46 to clarify some of the provisions and to exempt certain entities from its requirements. Under the new guidance, special effective date provisions apply to enterprises that have fully or partially applied FIN 46 prior to issuance of the revised interpretation. Otherwise, application of Interpretation 46R ("FIN 46R") is required in financial statements of public entities that have interests in structures that are commonly referred to as special-purpose entities ("SPEs") for periods ending after December 15, 2003. Application by public entities, other than small business issuers, for all other types of VIEs other than SPEs is required in financial statements for periods ending after March 15, 2004.

The Company does not have any interests in structures commonly referred to as SPEs, typically has no equity ownership interests in its franchisees, and has not consolidated any of these entities in the Company's financial statements. The Company will continue to monitor developments regarding the Interpretation as they occur. Implementation of this pronouncement in the third fiscal quarter of 2004 is not expected to have a material impact on the financial statements.

(7) The following table shows the reconciliation of the numerator and denominator of the basic EPS calculation to the numerator and denominator of the diluted EPS calculation (in thousands, except per share amounts).

	INCOME (NUMERATOR)	SHARES (DENOMINATOR)	PER SHARE AMOUNT
	-----	-----	-----
THREE MONTHS ENDED DECEMBER 28, 2003			
BASIC EPS			
Income Available to Common Shareholders	\$ 558	10,071	\$ 0.06
Effect of Dilutive Securities - Stock Options		52	
		--	
DILUTED EPS			
Income Available to Common Shareholders			
Assumed Conversions	\$ 558	10,123	\$ 0.06
	=====	=====	=====
THREE MONTHS ENDED DECEMBER 29, 2002			
BASIC EPS			
Income Available to Common Shareholders	\$ 1,892	10,058	\$ 0.19
Effect of Dilutive Securities - Stock Options		2	
		--	
DILUTED EPS			
Income Available to Common Shareholders			
& Assumed Conversions	\$ 1,892	10,060	\$ 0.19
	=====	=====	=====
SIX MONTHS ENDED DECEMBER 28, 2003			
BASIC EPS			
Income Available to Common Shareholders	\$ 1,062	10,065	\$ 0.11
Effect of Dilutive Securities - Stock Options		39	
		--	
DILUTED EPS			
Income Available to Common Shareholders			
& Assumed Conversions	\$ 1,062	10,104	\$ 0.11
	=====	=====	=====
SIX MONTHS ENDED DECEMBER 29, 2002			
BASIC EPS			
Income Available to Common Shareholders	\$ 2,196	10,058	\$ 0.22
Effect of Dilutive Securities - Stock Options		1	
		--	
DILUTED EPS			
Income Available to Common Shareholders			
& Assumed Conversions	\$ 2,196	10,059	\$ 0.22
	=====	=====	=====



(8) Summarized in the following tables are net sales and operating revenues, operating profit, and geographic information (revenues) for the Company's reportable segments for the three months and six months periods ended December 28, 2003 and December 29, 2002 (in thousands).

	THREE MONTHS ENDED		SIX MONTHS ENDED	
	DECEMBER 28, 2003	DECEMBER 29, 2002	DECEMBER 28, 2003	DECEMBER 29, 2002
<b>NET SALES AND OPERATING REVENUES:</b>				
Food and Equipment Distribution	\$13,032	\$13,275	\$26,530	\$26,804
Franchise and Other	1,640	1,760	3,497	3,529
Intersegment revenues	216	176	363	351
Combined	14,888	15,211	30,390	30,684
Other revenues	97	129	118	192
Less intersegment revenues	(216)	(176)	(363)	(351)
Consolidated revenues	\$14,769	\$15,164	\$30,145	\$30,525
<b>OPERATING PROFIT:</b>				
Food and Equipment Distribution (1)	\$590	\$652	\$1,284	\$1,396
Franchise and Other (1)	584	800	1,241	1,400
Intersegment profit	49	42	91	96
Combined	1,223	1,494	2,616	2,892
Other profit or loss	97	130	118	192
Less intersegment profit	(49)	(42)	(91)	(96)
Corporate administration and other	(426)	1,285	(1,034)	339
Income before taxes	\$845	\$2,867	\$1,609	\$3,327
<b>GEOGRAPHIC INFORMATION (REVENUES):</b>				
United States	\$14,487	\$14,860	\$29,428	\$30,028
Foreign countries	282	304	717	497
Consolidated total	\$14,769	\$15,164	\$30,145	\$30,525

(1) Does not include full allocation of corporate administration.

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

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Management's discussion and analysis is based on the Company's condensed consolidated financial statements and related footnotes contained within this report. The Company's critical accounting policies used in the preparation of those condensed consolidated financial statements are discussed below.

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Significant estimates made by management include the allowance for doubtful accounts, inventory valuation, deferred tax asset valuation allowances, and legal accruals. Actual results could differ from those estimates.

The Company's Norco division sells food, supplies and equipment to franchisees on trade accounts under terms common in the industry. Revenue from such sales is recognized upon shipment. Norco sales are reflected under the caption "food and supply sales." Shipping and handling costs billed to customers are recognized as revenue.

Franchise revenue consists of income from license fees, royalties, and Territory sales. License fees are recognized as income when there has been substantial performance of the agreement by both the franchisee and the Company, generally at the time the unit is opened. Royalties are recognized as income when earned.

Territory sales are the fees paid by selected experienced restaurant operators to the Company for the right to develop Pizza Inn restaurants in

specific geographical territories. When the Company has no continuing substantive obligations of performance to the area developer or master licensee regarding the fee, the Company recognizes the fee to the extent of cash received. If continuing obligations exist, fees are recognized ratably during the performance of those obligations.

Inventories, which consist primarily of food, paper products, supplies and equipment located at the Company's distribution center, are stated at the lower of FIFO (first-in, first-out) cost or market. Provision is made for obsolete inventories and is based upon management's assessment of the market conditions for its products.

Accounts receivable consist primarily of receivables from food and supply sales and franchise royalties. The Company records a provision for doubtful receivables to allow for any amounts which may be unrecoverable and is based upon an analysis of the Company's prior collection experience, customer creditworthiness, and current economic trends.

Notes receivable primarily consist of notes from franchisees for the purchase of area development and master license territories, trade receivables and equipment purchases. These notes generally have terms ranging from one to five years and interest rates of 6% to 9%. The Company records a provision for doubtful receivables to allow for any amounts which may be unrecoverable and is based upon an analysis of the Company's prior collection experience, customer creditworthiness, and current economic trends.

The Company has recorded a valuation allowance to reflect the estimated amount of deferred tax assets that may not be realized based upon the Company's analysis of existing tax credits by jurisdiction and expectations of the Company's ability to utilize these tax attributes through a review of estimated future taxable income and establishment of tax strategies. These estimates could be impacted by changes in future taxable income and the results of tax strategies.

The Company assesses its exposures to loss contingencies including legal and income tax matters based upon factors such as the current status of the cases and consultations with external counsel and provides for an exposure if it is judged to be probable and estimable. If the actual loss from a contingency differs from management's estimate, operating results could be impacted.

#### RESULTS OF OPERATIONS

QUARTER AND SIX MONTHS ENDED DECEMBER 28, 2003 COMPARED TO THE QUARTER AND SIX MONTHS ENDED DECEMBER 29, 2002.

Earnings per share for the quarter were \$0.06 versus \$0.19 for the same period last year. Net income was \$558,000 versus \$1,892,000, on revenues of \$14,769,000 versus \$15,164,000 in the previous year. For the six month period, earnings per share were \$0.11 versus \$0.22 last year. Net income was \$1,062,000 compared to \$2,196,000 on revenues of \$30,145,000 versus \$30,525,000 last year. The prior year's quarter included the reversal of a previously recorded pre-tax charge of approximately \$1,950,000. The reserve was previously recorded in the fourth quarter of fiscal 2002 to fully reserve for the expected nonpayment of a note receivable owed to the Company from the Company's former Chief Executive Officer. The Company received payment in full for the note receivable in December 2002.

Food and supply sales by the Company's Norco division include food and paper products, equipment, marketing material, and other distribution revenues. Food and supply sales for the quarter decreased 2%, or \$243,000 to \$13,032,000 from \$13,275,000 compared to the same period last year. For the six month period, food and supply sales decreased 1%, or \$274,000, to \$26,530,000 from \$26,804,000. Lower retail sales were partially offset by higher cheese prices and higher international sales.

Franchise revenue, which includes income from royalties, license fees and area development and foreign master license (collectively, "Territory") sales, decreased 3% or \$43,000 for the quarter compared to the same period last year and increased 4% or \$106,000 for the six month period. The decrease for the quarter is due to lower royalties due to lower retail sales. The increase for the six month period is due primarily to higher international royalties, which resulted from the collection of previously unrecorded past due royalties, and was partially offset by lower domestic royalties due to lower retail sales.

Restaurant sales, which consist of revenue generated by Company-owned training stores decreased 17% or \$77,000 for the quarter, compared to the same period of the prior year. For the six month period, restaurant sales decreased 15% or \$138,000. These decreases are the result of lower comparable sales at the two Company-owned stores.

Other income consists primarily of interest income, third party commissions, and non-recurring revenue items. Other income decreased 25% or \$32,000 for the quarter, compared to the same period of the prior year. For the six month period, other income decreased 39% or \$74,000. These decreases are due primarily to lower commissions and lower interest income.

Cost of sales decreased 1% or \$93,000 for the quarter and increased \$99,000 for the six month period. Cost of sales, as a percentage of sales for the quarter and the six month period, increased to 90% from 89% for the same periods last year. The decrease for the quarter was due to lower payroll and related

expenses which were partially offset by higher comparable cheese prices. The six month increase is primarily due to higher cheese prices as compared to the same period last year.

Franchise expenses include selling, general and administrative expenses directly related to the sale and continuing service of franchises and Territories. These costs decreased 13% or \$107,000 for the quarter and decreased \$1,000 for the six month period compared to the same period last year. These decreases are primarily the result of lower payroll and related expenses in both periods offset by higher taxes on foreign royalties and marketing expenses in the first quarter.

General and administrative expenses increased 206% or \$1,872,000 for the quarter and 209% or \$1,354,000 for the six months, compared to the same periods last year. This is primarily the result of the reversal of a previously recorded pre-tax charge of approximately \$1,950,000 for bad debt in the prior year as described above. Additional, general and administrative expenses included an accrual for approximately \$200,000 for certain potential tax matters which the Company is currently analyzing.

Interest expense decreased 22% or \$45,000 for the quarter and 26% or \$114,000 for the six months, compared to the same periods of the prior year due to lower debt balances and lower interest rates.

Provision for income taxes decreased 71% or \$688,000 for the quarter, and 52% or \$584,000 for the six months compared to the same periods in the prior year. The effective tax rate was 34% for both the current and prior quarters and six months.

#### LIQUIDITY AND CAPITAL RESOURCES

Cash flows from operating activities are generally the result of net income, deferred taxes, depreciation and amortization, and changes in working capital. In the first six months of fiscal 2004, the company generated cash flows of \$2,628,000 from operating activities as compared to \$2,778,000 in fiscal 2003. Cash provided by operations was utilized primarily to pay down debt.

Cash flows from investing activities primarily reflect the Company's capital expenditure strategy. In the first six months of fiscal 2004, the Company used cash of \$987,000 for investing activities as compared to \$236,000 in fiscal 2003. The cash used during fiscal 2004 consisted primarily of the reacquisition of an area development rights as described above, and costs associated with a Company-owned store which opened in January 2004.

Cash flows from financing activities generally reflect changes in the Company's borrowings during the period, treasury stock transactions, and exercise of stock options. Net cash used for financing activities was \$1,841,000 in the first six months of fiscal 2004 as compared to cash used for financing activities of \$3,113,000 in fiscal 2003.

Management believes that future operations will generate sufficient taxable income, along with the reversal of temporary differences, to fully realize the deferred tax asset, net of a valuation allowance of \$154,000 primarily related to the potential expiration of certain foreign tax credit carryforwards. Additionally, management believes that taxable income based on the Company's existing franchise base should be more than sufficient to enable the Company to realize its net deferred tax asset without reliance on material, non-routine income. The Company's prior net operating loss carryforwards and alternative minimum tax carryforwards have now been fully utilized and the Company began making estimated quarterly tax payments in January 2004.

The Company entered into an agreement effective December 29, 2002 with its current lender to provide a \$7.0 million revolving credit line that will expire December 31, 2004, replacing a \$9.5 million line that was due to expire December 31, 2003. The \$7.0 million revolving credit line will reduce quarterly by \$500,000 beginning March 31, 2003 through December 31, 2004. Interest on the revolving credit line is payable monthly. Interest is provided for at a rate equal to prime less an interest rate margin from 1.0% to 0.5% or, at the Company's option, at the LIBOR rate plus 1.25% to 1.75%. The interest rate margin is based on the Company's performance under certain financial ratio tests. A 0.375% to 0.5% annual commitment fee is payable on any unused portion of the revolving credit line. As of December 28, 2003 and December 29, 2002, the variable interest rates were 2.64% and 2.94%, respectively, using a LIBOR rate basis. Amounts outstanding under the revolving credit line as of December 28, 2003 and December 29, 2002 were \$1.5 million and \$2.4 million, respectively.

The Company entered into a term note effective March 31, 2000 with its current lender. The \$5,000,000 term note had outstanding balances of \$417,000 and \$1.7 million at December 28, 2003 and December 29, 2002, respectively. The term note requires monthly principal payments of \$104,000 with the balance maturing on March 31, 2004. Interest on the term loan is also payable monthly. Interest is provided for at a rate equal to prime less an interest rate margin of 0.75% or, at the Company's option, at the LIBOR rate plus 1.5%. As of December 28, 2003 and December 29, 2002, the variable interest rates were 2.69% and 2.94%, respectively.

The Company entered into an agreement effective December 28, 2000, as amended, with its current lender to provide up to \$8.125 million of financing for the construction of the Company's new headquarters, training center and distribution facility. The construction loan converted to a term loan effective

January 31, 2002 with the unpaid principal balance to mature on December 28, 2007. This term loan will amortize over a term of twenty years, with principal payments of \$34,000 due monthly. Interest on this term loan is also payable monthly. Interest is provided for at a rate equal to prime less an interest rate margin of 0.75% or, at the Company's option, to the LIBOR rate plus 1.5%. As of December 28, 2003 and December 29, 2002, the variable interest rates were 2.65% and 2.89%, respectively. The Company, to fulfill bank requirements, has caused the outstanding principal amount to be subject to a fixed interest rate by utilizing an interest rate swap agreement as discussed below. The \$8.125 million term loan had an outstanding balance of \$7.3 million at December 28, 2003 and \$7.7 million at December 29, 2002.

The Company entered into an interest rate swap effective February 27, 2001, as amended, designated as a cash flow hedge, to manage interest rate risk relating to the financing of the construction of the Company's new headquarters and to fulfill bank requirements. The swap agreement has a notional principal amount of \$8.125 million with a fixed pay rate of 5.84% which began November 1, 2001 and will end November 19, 2007. The swap's notional amount amortizes over a term of twenty years to parallel the terms of the term loan. SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" requires that for cash flow hedges, which hedge the exposure to variable cash flow of a forecasted transaction, the effective portion of the derivative's gain or loss be initially reported as a component of other comprehensive income in the equity section of the balance sheet and subsequently reclassified into earnings when the forecasted transaction affects earnings. Any ineffective portion of the derivative's gain or loss is reported in earnings immediately. At December 28, 2003 there was no hedge ineffectiveness. The Company's expectation is that the hedging relationship will continue to be highly effective at achieving offsetting changes in cash flows.

On April 30, 1998, Mid-South Pizza Development, Inc. ("Mid-South") entered into a promissory note whereby, among other things, Mid-South borrowed \$1,330,000 from a third party lender (the "Loan"). The proceeds of the Loan, less transaction costs, were used by Mid-South to purchase area developer rights from the Company for certain counties in Kentucky and Tennessee. Effective December 28, 2003, the Company reacquired all such area development rights from Mid-South. The Company paid approximately \$963,000 for these rights of which \$682,000 was a cash payment, and a non-cash settlement of accounts receivable of approximately \$281,000. A long-term asset was recorded for the same amount. Restaurants operating or developed in the reacquired territory will now pay all royalties and franchise fees directly to Pizza Inn, Inc. The asset will be amortized against actual incremental cash flows received, which is estimated to be approximately five years.

On January 18, 2002, the Company was served with a lawsuit filed by Blakely-Witt & Associates, Inc. alleging Pizza Inn sent or, caused to be sent, unsolicited facsimile advertisements. The plaintiff has requested this matter be certified as a class action. We plan to vigorously defend our position in this litigation. We cannot assure you that we will prevail in this lawsuit and our defense could be costly and consume the time of our management. We are unable to predict the outcome of this case. However, an adverse resolution of this matter could materially affect our financial position and results of operations.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

The following chart summarizes all of the Company's material obligations and commitments to make future payments under contracts such as debt and lease agreements as of December 28, 2003 (in thousands):

	Less Than 1		1-3	4-5 After 5	
	Total	Year	Years	Years	Years
Bank debt . . . . .	\$ 9,263	\$ 823	\$ 1,906	\$ 406	\$6,128
Operating lease obligations . . . .	3,387	1,106	1,741	432	108
Capital lease obligations (1) . . .	92	64	21	7	
Total contractual cash obligations.	\$12,742	\$1,993	\$ 3,668	\$ 845	\$6,236

(1) Does not include amount representing interest.

FORWARD-LOOKING STATEMENT

This report contains certain forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995) relating to the Company that are based on the beliefs of the management of the Company, as well as assumptions and estimates made by and information currently available to the Company's management. When used in this report, the words "anticipate," "believe," "estimate," "expect," "intend" and similar expressions, as they relate to the Company or the Company's management, identify forward-looking

statements. Such statements reflect the current views of the Company with respect to future events and are subject to certain risks, uncertainties and assumptions relating to the operations and results of operations of the Company as well as its customers and suppliers, including as a result of competitive factors and pricing pressures, shifts in market demand, general economic conditions and other factors including but not limited to, changes in demand for Pizza Inn products or franchises, the impact of competitors' actions, changes in prices or supplies of food ingredients, and restrictions on international trade and business. Should one or more of these risks or uncertainties materialize, or should underlying assumptions or estimates prove incorrect, actual results may vary materially from those described herein as anticipated, believed, estimated, expected or intended.

#### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

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The Company has market risk exposure arising from changes in interest rates. The Company's earnings are affected by changes in short-term interest rates as a result of borrowings under its credit facilities which bear interest based on floating rates.

At December 28, 2003 the Company has approximately \$9.3 million of variable rate debt obligations outstanding with a weighted average interest rate of 2.63%. A hypothetical 10% change in the effective interest rate for these borrowings, assuming debt levels at December 28, 2003, would change interest expense by approximately \$12,000 for the six months ended December 28, 2003. As discussed previously, the Company has entered into an interest rate swap designed to manage the interest rate risk relating to \$7.3 million of the variable rate debt.

#### ITEM 4. CONTROLS AND PROCEDURES

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a) Evaluation of disclosure controls and procedures. Based on their evaluation as of a date within 90 days of the filing date of this Quarterly Report on Form 10-Q, the Company's principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures (as defined in Rules 13a-14(c) and 15d-14(c) under the Securities Exchange Act of 1934 (the "Exchange Act")) are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms. Our Chief Executive Officer and our Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report, and they have concluded that as of that date our disclosure controls and procedures were effective at ensuring that required information will be disclosed on a timely basis in our reports filed under the Exchange Act.

b) Changes in internal controls. There were no significant changes to our internal controls or in other factors that could significantly affect our internal controls subsequent to the date of their evaluation by our Chief Executive Officer and our Chief Financial Officer. There were no significant deficiencies or material weaknesses, and therefore there were no corrective actions taken.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

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On January 18, 2002, the Company was served with a lawsuit filed by Blakely-Witt & Associates, Inc. in the District Court, L-193rd Judicial District, Dallas County, Texas (Cause No. 01-11043). The suit alleges Pizza Inn sent, or caused to be sent, unsolicited facsimile advertisements to plaintiff and others in violation of (i) 47 U.S.C. Section 227(b)(1)(C) and (b)(3), the Telephone Consumer Protection Act, and (ii) Texas Business and Commerce Code Section 35.47. The plaintiff has requested this matter be certified as a class action. We plan to vigorously defend our position in this litigation. We cannot assure you that we will prevail in this lawsuit and our defense could be costly and consume the time of our management. We are unable to predict the outcome of this case. However, an adverse resolution of this matter could materially affect our financial position and results of operations.

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

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None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

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(a) Exhibits:

31.1 Certification of Chief Executive Officer as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of Chief Financial Officer as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of Chief Executive Officer as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of Chief Financial Officer as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Form 8-K

On October 31, 2003 the Company filed a report on Form 8-K, reporting a press release with respect to earnings for the first quarter ended September 28, 2003.

On January 23, 2004 the Company filed a report on Form 8-K, reporting a press release with respect to earnings for the second quarter ended December 28, 2003.

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SIGNATURES  
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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.

PIZZA INN, INC.  
Registrant

By: /s/Ronald W. Parker  
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Ronald W. Parker  
President and Chief Executive Officer

By: /s/Shawn M. Preator  
-----  
Shawn M. Preator  
Chief Financial Officer

Dated: February 6, 2004

CERTIFICATION

I, Ronald W. Parker, President and Chief Executive Officer of Pizza Inn, Inc. certify that:

1. I have reviewed the quarterly report on Form 10-Q of Pizza Inn, Inc. (the "Registrant");

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this quarterly report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Registrant and we have:

a. Designed such disclosure controls and procedures to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b. Evaluated the effectiveness of the Registrant's disclosure controls and procedures as of the end of the period covered by this quarterly report; and

c. Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent function):

a. All significant deficiencies in the design or operation of internal controls which could adversely affect the Registrant's ability to record, process, summarize and report financial data and have identified for the Registrant's auditors any material weaknesses in internal controls; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal controls; and

6. The Registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

February 6, 2004

By: /s/ Ronald W. Parker  
Ronald W. Parker  
President and Chief Executive Officer



CERTIFICATION

I, Shawn M. Preator, Chief Financial Officer (Principal Accounting Officer) of Pizza Inn, Inc. certify that:

1. I have reviewed the quarterly report on Form 10-Q of Pizza Inn, Inc. (the "Registrant");

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the Registrant as of, and for, the periods presented in this quarterly report;

4. The Registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the Registrant and we have:

a. Designed such disclosure controls and procedures to ensure that material information relating to the Registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

b. Evaluated the effectiveness of the Registrant's disclosure controls and procedures as of the end of the period covered by this quarterly report; and

c. Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The Registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the Registrant's auditors and the audit committee of Registrant's board of directors (or persons performing the equivalent function):

a. All significant deficiencies in the design or operation of internal controls which could adversely affect the Registrant's ability to record, process, summarize and report financial data and have identified for the Registrant's auditors any material weaknesses in internal controls; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the Registrant's internal controls; and

6. The Registrant's other certifying officer and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

February 6, 2004

By: /s/ Shawn M. Preator  
Shawn M. Preator  
Chief Financial Officer  
Principal Accounting Officer

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Pizza Inn, Inc. ("the Company") on Form 10-Q for the three months and six months ended December 28, 2003 as filed with Securities and Exchange Commission on the date hereof ("the Report"), I, Ronald W. Parker, President and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and
2. I have reviewed this quarterly report on Form 10-Q of the Company;
3. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
4. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report.

A signed original of this written statement required by Section 906 has been provided to Pizza Inn, Inc. and will be retained by Pizza Inn, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

February 6, 2004

/s/Ronald W. Parker  
Ronald W. Parker  
President and Chief Executive Officer

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Pizza Inn, Inc. ("the Company") on Form 10-Q for the three months and six months ended December 28, 2003 as filed with Securities and Exchange Commission on the date hereof ("the Report"), I, Shawn M. Preator, Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and
2. I have reviewed this quarterly report on Form 10-Q of the Company;
3. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
4. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report.

A signed original of this written statement required by Section 906 has been provided to Pizza Inn, Inc. and will be retained by Pizza Inn, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

February 6, 2004

/s/ Shawn M. Preator  
Shawn M. Preator  
Chief Financial Officer