

\$1 BILLION AND MORE GROWTH IN STORE



AARON RENTS, INC., the industry leader in its market niche, serves consumers and businesses through the sale and lease ownership, rental and retailing of consumer electronics, residential and office furniture, household appliances, computers and accessories. The Company operates over 850 stores in the United States, Puerto Rico and Canada. The Company's major operations are the Aaron's Sales & Lease Ownership division, the Rent-to-Rent division and MacTavish Furniture Industries. MacTavish manufactures the majority of the furniture rented, leased and sold in the Company's stores, operating ten facilities in four states. Aaron Rents caters to the moderate income consumer, offering affordable payment plans, quality merchandise and superior service. The Company's strategic focus is growing the sales and lease ownership business through the addition of new Company-operated stores, by both internal expansion and acquisition, as well as the successful and expanding franchise program.

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FINANCIAL HIGHLIGHTS

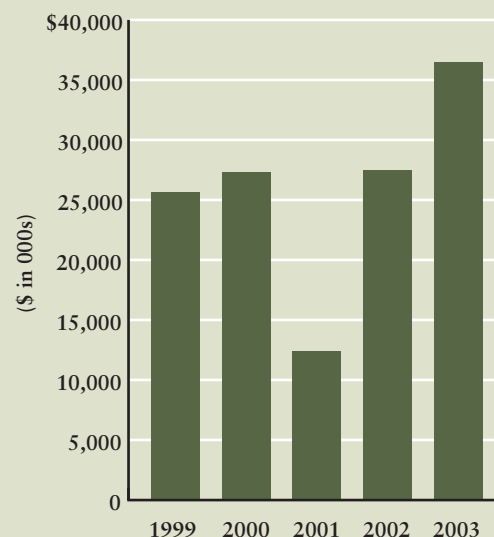
(Dollar Amounts in Thousands, Except Per Share)	Year Ended December 31, 2003	Year Ended December 31, 2002	Percentage Change
Systemwide Revenues ¹	\$1,033,350	\$874,709	18.1%
OPERATING RESULTS			
Revenues	\$ 766,797	\$640,688	19.7%
Earnings Before Taxes	57,843	43,652	32.5
Net Earnings	36,426	27,440	32.7
Earnings Per Share	1.12	.87	28.7
Earnings Per Share Assuming Dilution	1.10	.86	27.9
FINANCIAL POSITION			
Total Assets	\$ 555,292	\$483,648	14.8%
Rental Merchandise, Net	343,013	317,287	8.1
Credit Facilities	79,570	73,265	8.6
Shareholders' Equity	320,186	280,545	14.1
Book Value Per Share	9.77	8.61	13.5
Debt to Capitalization	19.9%	20.7%	
Pre-Tax Profit Margin	7.5	6.8	
Net Profit Margin	4.8	4.3	
Return on Average Equity	12.1	11.0	
STORES OPEN AT YEAR END			
Sales & Lease Ownership	500	412	21.4%
Sales & Lease Ownership Franchised	287	232	23.7
Rent-to-Rent	60	70	(14.3)
Total Stores	847	714	18.6%

¹Refer to page 15 for additional information.

Revenues By Year



Net Earnings By Year

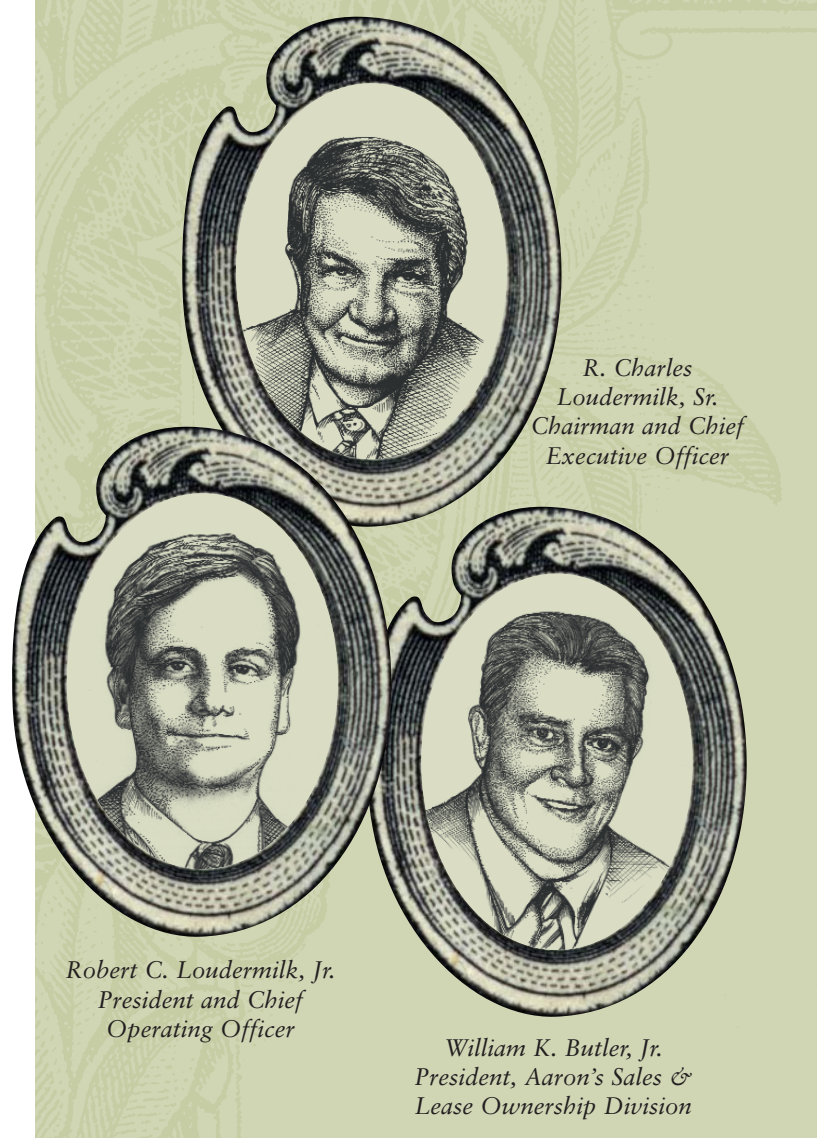


■ Company-Operated Sales & Lease Ownership Stores
■ Rent-to-Rent Stores

TO OUR SHAREHOLDERS

We could not be more proud of the Company's 2003 performance and are confident that there is "more growth in store." Operating highlights for the year include:

- Systemwide revenues reached an all-time record, crossing the one billion dollar milestone. Revenues from Company operations were \$766.8 million, an increase of 20% over the record 2002 performance. Revenues in the Aaron's Sales & Lease Ownership Division increased 26% for the year.
- Net earnings also set records, up 33% for the year to \$36.4 million.
- We are particularly proud to note that 441 of our Company-operated and franchise Aaron's Sales & Lease Ownership stores had revenues in excess of \$1 million in 2003, more than double the industry average for annual store revenues.
- We added 143 new stores to the Aaron's Sales & Lease Ownership system, an increase of 22%. The Company-operated sales and lease ownership store count increased 21% and the number of franchised stores increased 24%. The Company ended 2003 with 847 stores in 43 states, Puerto Rico, and Canada, including 60 units in the Rent-to-Rent division.
- We accelerated an aggressive acquisition strategy in 2003, adding 59 Company-operated stores (of which 26 were acquired franchise stores) through the purchase of rental contracts and/or store fronts from various independent rental operators. We have identified numerous attractive locations in existing and new markets as potential future acquisition candidates. The favorable economics of acquiring rental contracts and stores supplement our internal growth strategy.
- Franchise operations set records in both revenues and earnings in 2003. We awarded area development agreements for 112 new franchise stores, including our first ventures into Canada (six stores to be opened in Ontario) and Alaska. The number of franchised stores to be



*R. Charles
Loudermilk, Sr.
Chairman and Chief
Executive Officer*

*Robert C. Loudermilk, Jr.
President and Chief
Operating Officer*

*William K. Butler, Jr.
President, Aaron's Sales &
Lease Ownership Division*

opened in the future is nearly as large as the year-end franchise store base of 287.

- The 2003 operating performance did not go unnoticed in the stock market. Our Common Stock price increased 38% during 2003 and the Company reached a record market capitalization of over \$650 million. In August of 2003, we effected a 3-for-2 stock split in the form of a 50% stock dividend and increased the cash dividend per share 50%.

For the year, systemwide revenues were \$1 billion, an 18% increase over 2002. Consolidated revenues increased 20% to a record \$766.8 million compared to \$640.7 million in 2002. Net earnings for the year were \$36.4 million, an increase of 33% over the \$27.4 million earned the previous year. Fully diluted earnings per share were \$1.10 in 2003 compared to \$.86 per diluted share in 2002. Same store revenues for the Aaron's Sales & Lease Ownership stores opened in comparable periods increased 10.1% in 2003, an excellent performance.

At the end of December, we had an additional 241 franchise stores in our new store pipeline. There is more growth in store for Aaron Rents.

Note that non-GAAP (generally accepted accounting principles) systemwide revenues are calculated by adding GAAP revenues to the revenues of the Company's franchisees and subtracting the Company's royalty revenues. Franchisee revenues, however, are not revenues of Aaron Rents, Inc. and are not included in our consolidated financial statements.

The aggressive growth in new Aaron's Sales & Lease Ownership stores over the past several years began to contribute materially during 2003 as these stores reported higher revenues and earnings. Approximately 27% of our sales and lease ownership stores have been added within the past two years. Since new stores generally reach maturity in revenues and earnings over a period of years, margin improvement is expected to continue in future periods.

MacTavish Furniture Industries, the Company's manufacturing division, posted a record year in 2003, manufacturing more than \$60 million (at cost) of furniture for our stores out of 10 production facilities. Aaron Rents also now operates twelve distribution centers. We continue to believe that vertical integration is a strategic advantage, enabling our stores to offer rapid delivery of a full product line to our customers and to operate with lower inventory levels. Our nimble manufacturing operation can respond quickly to changes in demand and styling, allowing us to better serve our customers.

The Company's financial strength continues to be a competitive advantage. We have funded acquisition activity out of cash flow and increased our dividend payout with little utilization of our \$87 million revolving credit facility. With our debt-to-capital ratio the lowest in many years, Aaron's has the financial strength to fund expansion goals for the foreseeable future.

Our Board of Directors was strengthened in 2003 by the addition of David L. Kolb, Chief Executive Officer of Mohawk Industries, Inc. from 1988 to 2001. Mr. Kolb, now Chairman of the Board of Directors of Mohawk, has broad corporate experience and serves on a number of corporate and educational boards. He is a valuable addition to our Board.

During 2003, growth within the Aaron's Sales & Lease Ownership Division necessitated the creation of another regional field operation. Michael P. Ryan was named Vice President, Northern Operations, to oversee this new region. In addition, David A. Boggan was promoted to Vice President, Marketing and Merchandising. We are pleased to recognize and promote talented employees who have contributed to the Company's success for a number of years.

There is more growth in store for Aaron Rents. Our Aaron's Sales & Lease Ownership concept is a proven model and is in the early stages of penetrating its market. Experience demonstrates that these stores can be successfully operated in any town or city with a trading area of at least 20,000 people. With fewer than 800 stores in operation, we believe our market potential is substantial.

Our goal is unchanged: to build Aaron's into the premier, market-dominant company in our industry, recognized by our customers and peers as the standard bearer for integrity, honesty and fairness, and a company that earns a premium return for its shareholders.

Reaching the \$1 billion level in systemwide revenues has been a goal for our Company for several years. We now feel that the \$2 billion level is within reach, just a number of years away. As always, our success is based on the dedicated efforts of our associates and the support of our shareholders, for which we are grateful.



R. Charles Loudermilk, Sr.
Chairman and Chief Executive Officer




Robert C. Loudermilk, Jr.
President and Chief Operating Officer



AARON'S SALES AND LEASE OWNERSHIP

More Products, More Stores, More Growth

 Aaron's Sales & Lease Ownership is a unique form of specialty retailing which combines the best features of rent-to-own with the traditional credit retailing format offered by the home furnishings industry. Aaron's offers consumers fast, easy, convenient shopping and a broad range of top quality brand-name products, rapid delivery and low-price guarantees leading to the option of affordable ownership. Aaron's sets the standard for customer service in the rent-to-own industry.

The distinctive Aaron's Sales & Lease Ownership concept reaches and serves a broad market of lease ownership, credit retail and rental customers. The Aaron's Sales & Lease Ownership program attracts a slightly higher economic profile customer than the typical rent-to-own consumer, demonstrated by the fact that approximately 40% of our customers pay by either check or credit card. The typical rent-to-own consumer does not qualify for a credit card account and normally pays in cash. Weekly payments are the norm for the rent-to-own industry while the Aaron's lease ownership program is based on semimonthly or monthly payments, resulting in somewhat lower processing expenses per customer as well as a slightly upgraded account base. Aaron's customers are typically credit-constrained but our losses, in periods of both economic expansion and contraction, are consistently between only 2% to 3% of revenues.

Aaron's customers are automatically approved as the transaction is a lease-to-own plan rather than a credit relationship. The Company's in-house manufacturing and distribution facilities enable same-day or next-day delivery of merchandise. The consumer pays no delivery charges, no application fees, and no balloon payments. Terms are fully disclosed: cash-and-carry price, payment plan, and total cost under the lease ownership plan. Payment options include cash, check and credit cards. The lease-to-own plan requires no long-term obligation, so a customer is free to return merchandise at any time without additional financial responsibility.

Aaron's Sales & Lease Ownership stores are normally twice the size of a rent-to-own or competitor's store and feature more attractive merchandising and store décor. Aaron's product

offerings are typically new whereas many competitors primarily display rental returns. Professionally designed and coordinated furniture suites produced by the Company's manufacturing division and other top national manufacturers better serve the slightly more upscale consumer and generate higher revenues per customer than a traditional rent-to-own transaction. The Company recently introduced a new line of accessories, resulting in significantly more attractive showroom floors and opportunities for add-on revenues. Aaron's stores are usually located in suburban areas and attract generally higher income customers than a traditional rent-to-own business. Aaron's "Dream Products" line-up includes highly popular big-screen televisions and entertainment systems, stainless steel refrigerators, leather upholstered furniture and leading brands of appliances. Riding lawn tractors, originally expected to be a seasonal product line, have become a popular and profitable product in nearly all markets. Computers, a product line expanded several years ago, continue to be a growth area with the Dell and Hewlett Packard brand names proving a competitive advantage.

The Aaron's Sales & Lease Ownership division has been particularly well-positioned to address the market opportunity created by the liquidation of several major credit furniture retailers over the past three years. These bankruptcies, in aggregate, resulted in the closure of over 2,000 stores representing annual sales volume in excess of \$3.5 billion. The 80-plus store locations acquired from the Heilig-Meyers Company in 2001 and converted to Aaron's Sales & Lease Ownership stores continue to mature, posting solid revenue and profit growth.

Operational improvements and uniformity of customer experience continue to be priorities. The Aaron's University program is a tool for standardizing operational procedures throughout the system. The 13-course curriculum for Company and franchise managers is a key element for ensuring uniformity of execution and the development of strong operating talent.

During 2003, the Company introduced an internally developed system which automatically telephones customers of individual stores, reminding them of lease renewal payments due and

other information of interest. This system will be rolled out nationwide in 2004 and should greatly enhance store productivity. The Company also began to introduce bar-coding into store inventory management, achieving significant improvements in both efficiency and customer service. Historically, the weekly physical inventory tied up a substantial number of store associates for an extended period of time. Bar-coding has enabled one person to complete a store inventory in less than two hours, freeing up all other store associates to serve customers. The Company has also rolled out GPS (global positioning system) capability to its fleet of trucks, which will improve fleet operating efficiency and enable stores to more precisely schedule customer deliveries.

The Company's marketing program is built around the "Drive Dreams Home" sponsorship of NASCAR championship racing, which serves the prime demographic for Aaron's products. The Company's theme is carried out through the sponsorship of the #99 NASCAR Busch Grand National Dream Machine driven by Michael Waltrip. The program, which has generated extremely strong response, began with Aaron's title sponsorship of the NASCAR Busch Grand National Car Race at the Atlanta Motor Speedway. Running under the banner of "Aaron's 312," this nationally televised event plays off the three reasons to shop at Aaron's: everyone 1) is preapproved, 2) has a low price guarantee, and 3) can own the merchandise in as little as 12 months. Aaron's is now the title sponsor of the "Aaron's 312" Busch Series races at Talladega Superspeedway and the Atlanta Motor Speedway and the "Aaron's 499" Nextel Cup race at Talladega.

In addition, Aaron's has renewed and extended its national partnership with the Arena Football League. Aaron's Sales & Lease Ownership will be featured in in-arena promotions including public address and scoreboard video announcements, premium give-away opportunities, and one promotional night in each of the AFL's 19 team markets. The AFL will be featured in over 800 Aaron's stores with in-store marketing materials and direct-mail circulars. This AFL partnership includes logo identification on the jerseys of all visiting teams. Arena football is

growing in popularity and will begin its second season of network television coverage in 2004 with NBC telecasts. Aaron's is proud to partner with this exciting sport.

Other elements of the marketing program include sponsorship of the athletic programs of the University of Texas and Georgia Institute of Technology (Georgia Tech). In addition, Aaron's effectively uses direct-mail advertising with more than 16 million flyers mailed monthly to homes in the markets served by Aaron's stores.

The Aaron's Sales & Lease Ownership concept has been successfully executed in both large and smaller markets. The strength of this business model has been demonstrated by the rapid market penetration of new stores. In 2004, the first Aaron's Sales & Lease Ownership stores will open in Alaska and several more stores will open in the Canadian province of Ontario. Extensive analysis suggests that these two markets will be excellent expansion opportunities. At year-end the division had 787 Company-operated and franchise stores across the United States and in Puerto Rico and Canada, a growth rate of 22% in store count over the past year.

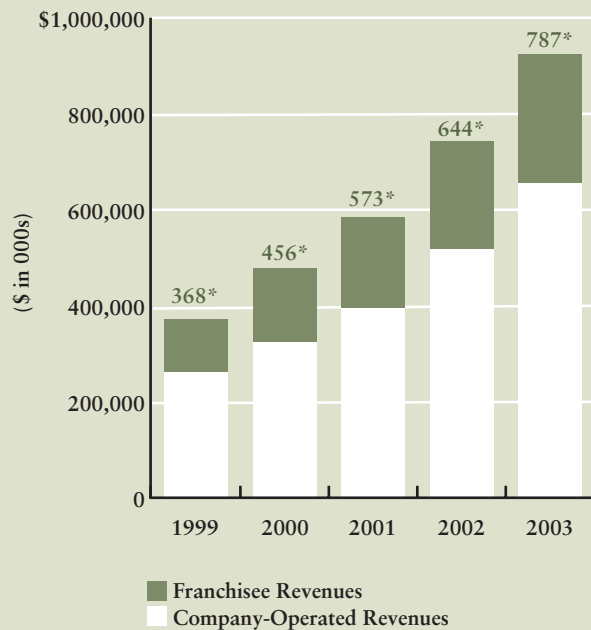
The Aaron's Sales & Lease Ownership concept continues to be the key growth vehicle for the Company. This division posted a 26% increase in revenues in 2003, following an excellent 31% gain in 2002. Same store revenues increased 10.1% in 2003, following a 13% increase in 2002, clearly one of the stronger performances in the retailing industry.

During 2003, the Aaron's Sales & Lease Ownership division added a net of 143 stores, including 59 Company-operated stores added through acquisition (26 of which were acquired from franchisees). At year-end, Aaron's operated 500 Company-operated sales and lease ownership stores. A large number of Aaron's Sales & Lease Ownership stores opened over the past five years and are now in the maturation phase, experiencing margin expansion and solidifying market share. We continue to believe that the Aaron's Sales & Lease Ownership division will post profit margin expansion over the next several years.

Aaron's Sales & Lease Ownership offers its "Dream Products" on the Internet at www.shopaaron.com.

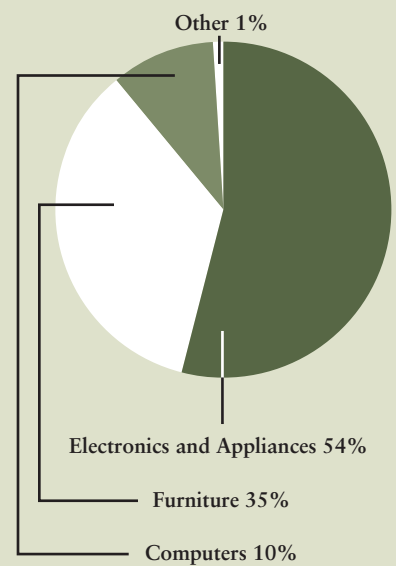


Sales & Lease Ownership Systemwide¹
Revenue Growth and Store Count



* Number of Stores

Sales & Lease Ownership
Rental Revenues



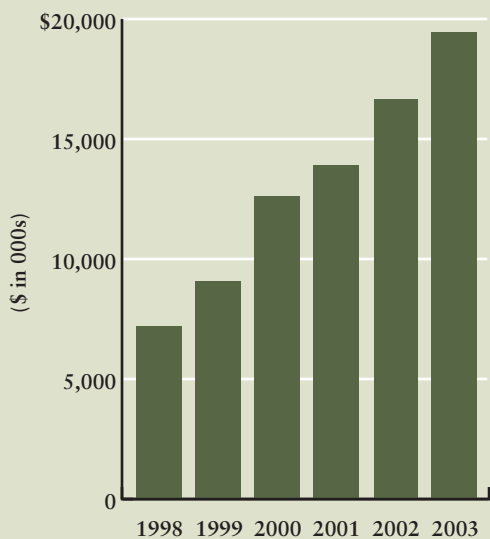
¹ Refer to page 15 for additional information.



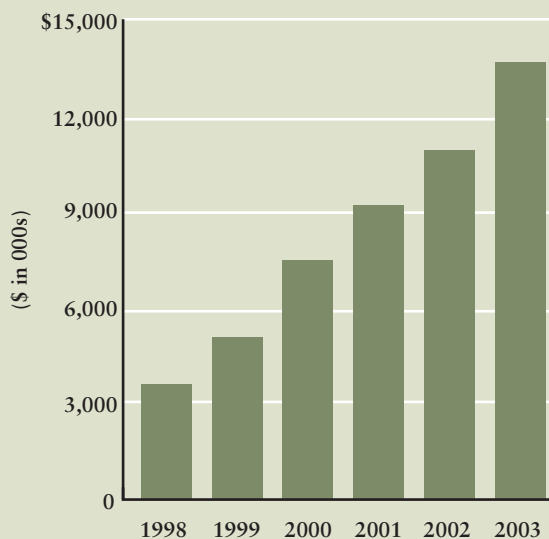
In November of 2003, Clay Tabor and Gene Hall opened their first Aaron's Sales & Lease Ownership store in Canada. This store is in Kitchener, Ontario and is the first of several planned franchise stores.



Revenues From Franchising



Pretax Income From Franchising



FRANCHISE OPERATIONS

A Blueprint for Growth

The Aaron's Sales & Lease Ownership franchise program reached new milestones in 2003, the eleventh year of the Company's franchising history. Area development agreements for 112 new stores were awarded.

The franchise program is a win-win situation. The franchisees benefit from Aaron's national reputation, industry experience, operating standards and purchasing, manufacturing and distribution systems. The benefits to Aaron's include a steadily growing stream of franchise revenues and the opportunity to accelerate store growth. The number of franchise stores has more than doubled over the past five years and the year-end pipeline of 241 stores scheduled to open over the next few years represents an 80%+ increase over the December 2003 store base of 287.

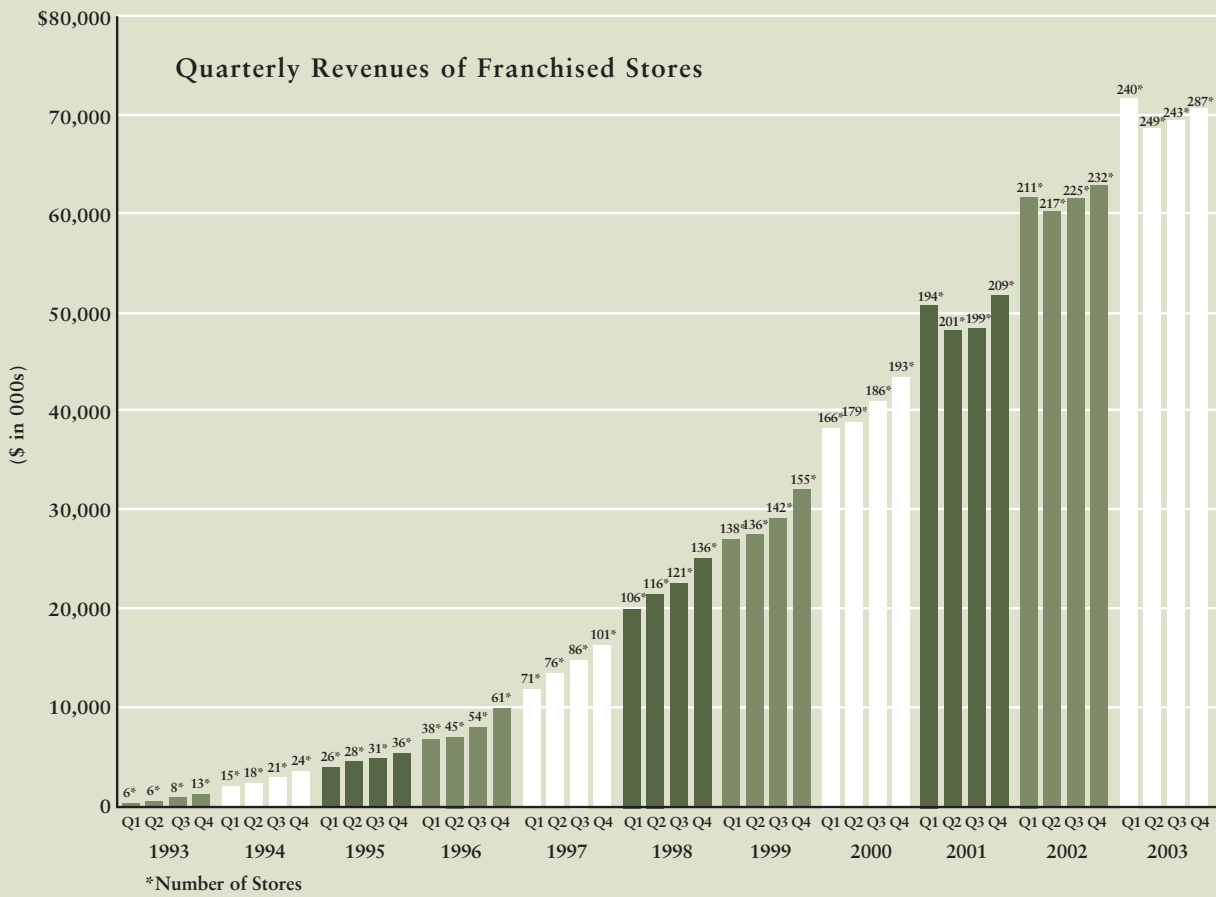
The Aaron's Sales & Lease Ownership franchise program has attracted a variety of experienced business professionals including former executives in banking, broadcasting, multiunit restaurant operations, technology and manufacturing. In addition, Aaron's has been fortunate to recruit strong operating management from the home furnishings retailing industry with a superior business model for the credit-constrained consumer market. Aaron's franchisees achieving strong and profitable growth with their first Aaron's stores often acquire additional franchise territories. The typical franchisee owns and operates three to four store locations but some major groups operate more than 15 locations.

Aaron's supports franchise principals with a full range of services beginning with assistance during the start-up phase. First, the franchise owner bases his or her individual business plan on the Company's proven business model in both Company-operated stores and franchise locations. Next, the franchisee utilizes the expertise of the Aaron's system in the store site selection process,

including a market analysis identifying the strengths and weaknesses of competitors. This analysis is the basis of an effective marketing program to reach the customer base. Aaron's provides franchise principals with initial and ongoing training in the management and operation of Aaron's stores as well as necessary computer software and assistance in advertising, marketing and publicity. Aaron's willingness to repurchase stores provides an exit strategy for franchisees and attractive acquisition opportunities for the Company. In fact, the Company acquired 26 stores from franchisees in 2003 and continues to pursue acquisition opportunities. Thirty-one stores owned by Rosey Rentals were converted to franchised units in 2003, and Rosey was awarded an area development agreement for an additional 18 stores.

The entire Aaron organization benefits from the shared experience and expertise of the principals and operating management of Company-operated stores. The Aaron's Franchise Association and the Aaron's Management Team, comprised of both franchise principals and representatives of the Company, are the key vehicles for communication and cross-fertilization.

Aaron's leadership in franchising is confirmed through annual surveys of franchise programs. For years, Aaron's has placed at or near the top in its category of appliance and furniture rentals in surveys sponsored by *Entrepreneur* magazine. The program also has ranked in the top 100 franchise chains by worldwide sales in the *Franchise Times*. To win the coveted upper-tier ratings, Aaron's must meet high standards of financial performance based on growth of revenues, franchise fees, and the Company's proprietary products and services. In addition, Aaron's is judged on the performance and strength of its management, the relationship with franchise owners, and the opportunities available for the growth of franchised stores.



Charles Smithgall now owns and operates 44 Aaron's stores with a long-term goal of 100 stores.

His Aaron's franchisee operations were the subject of a recent article in The Wall Street Journal.

Charles acquired his first franchise in 1995. His company, SEI/Aaron's Inc., is the Company's largest franchisee with stores in Kentucky, Rhode Island, Connecticut, Indiana, New York and Massachusetts.





This store in El Paso, Texas was opened as a franchise store in 2002 and was acquired by the Company in 2003. This profitable and growing store represents an ideal acquisition for Aaron's.



ACQUISITIONS

Strengthening Existing Markets and Entering New

The Company continues to pursue acquisition opportunities to complement new store openings and to achieve economies of scale in such areas as distribution and marketing. In terms of economic returns, the most attractive targets are competitive stores where the acquisition terms exclude storefronts and real estate obligations and the book of acquired contracts is folded into an existing Aaron's store, significantly leveraging fixed costs. The Company also seeks acquisitions of small chains (20–25 units) and single units to increase penetration in existing markets and to enter new markets. Generally, these acquisitions are based on a multiple of rental revenue, and the stores are converted to the Aaron's name as quickly as possible in order to leverage advertising and name recognition.

Aaron's acquired rental contracts of 98 stores in 2003, including 26 franchise stores, resulting in a net gain of 59 new storefronts obtained through acquisition. The acquired stores are excellent additions to the store base. The Company's strong cash flow has helped fund the acquisition program.



RENT-TO-RENT

Refurbished and Renewed

The rent-to-rent division of Aaron Rents, the Company's original line of business, generates solid cash flow important to the Company's growth and continues to adapt to changing industry dynamics. This division, characterized by a broad, high-quality product line and high service standards (for example, consumers may submit rental applications on-line), is the second largest operation in the temporary furniture rental market in the United States.

Traditionally, the rent-to-rent division has served residential and business customers (e.g. students, military personnel, new businesses, major corporations with temporary rental needs). Corporate business, consisting of residential furniture for employee relocations and office furniture, now represents the majority of divisional revenues. Aaron's meets the needs of each customer category, offering flexible options of renting, purchasing or lease ownership. To the corporate market, Aaron's is the "Source for Workplace Solutions," offering free in-office consultation and short-term or special event rentals. Customers can expect next-day delivery on a broad range of office furnishings, including panel systems, and have the option of purchasing previously rented furniture. Aaron's leverages the overhead of the rent-to-rent stores by using those locations as clearance centers for rental return merchandise.

Customers may select from a broad assortment of living room, dining room and bedroom furnishings and accessories, as well as big-screen televisions and personal computers. Aaron Rents offers special housewares and linen rental programs, offering customers a complete, one-stop shopping experience. The Company's MacTavish Furniture Industries division manufactures the majority of the Company's wide range of rent-to-rent products, but Aaron Rents has also long been among the leaders in rentals of La-Z-Boy furniture and other popular brands.

The reputation of Aaron Rents as an industry leader has been built over nearly 50 years, customer by customer, order by order. A key factor in this reputation is the commitment to competitive prices, high-quality products and first-rate service, including next-day delivery of in-stock merchandise; replacement without charge of any furniture the customer considers unsatisfactory regardless of the reason; and the right to return furniture for a full refund during the first week after delivery.

Over the past 15 years, residential rentals have become more of a corporate relocation business as consumers now have additional financial options (rent-to-own, for example). The corporate relocation business is served by the rent-to-rent industry, extended stay hotels (such as Residence Inn and Suburban Lodges) and by furnished apartments. In response, the rent-to-rent division has taken steps to consolidate operations and reduce expenses while focusing on marketing opportunities. Aaron Rents is positioned to benefit from improving economic trends.



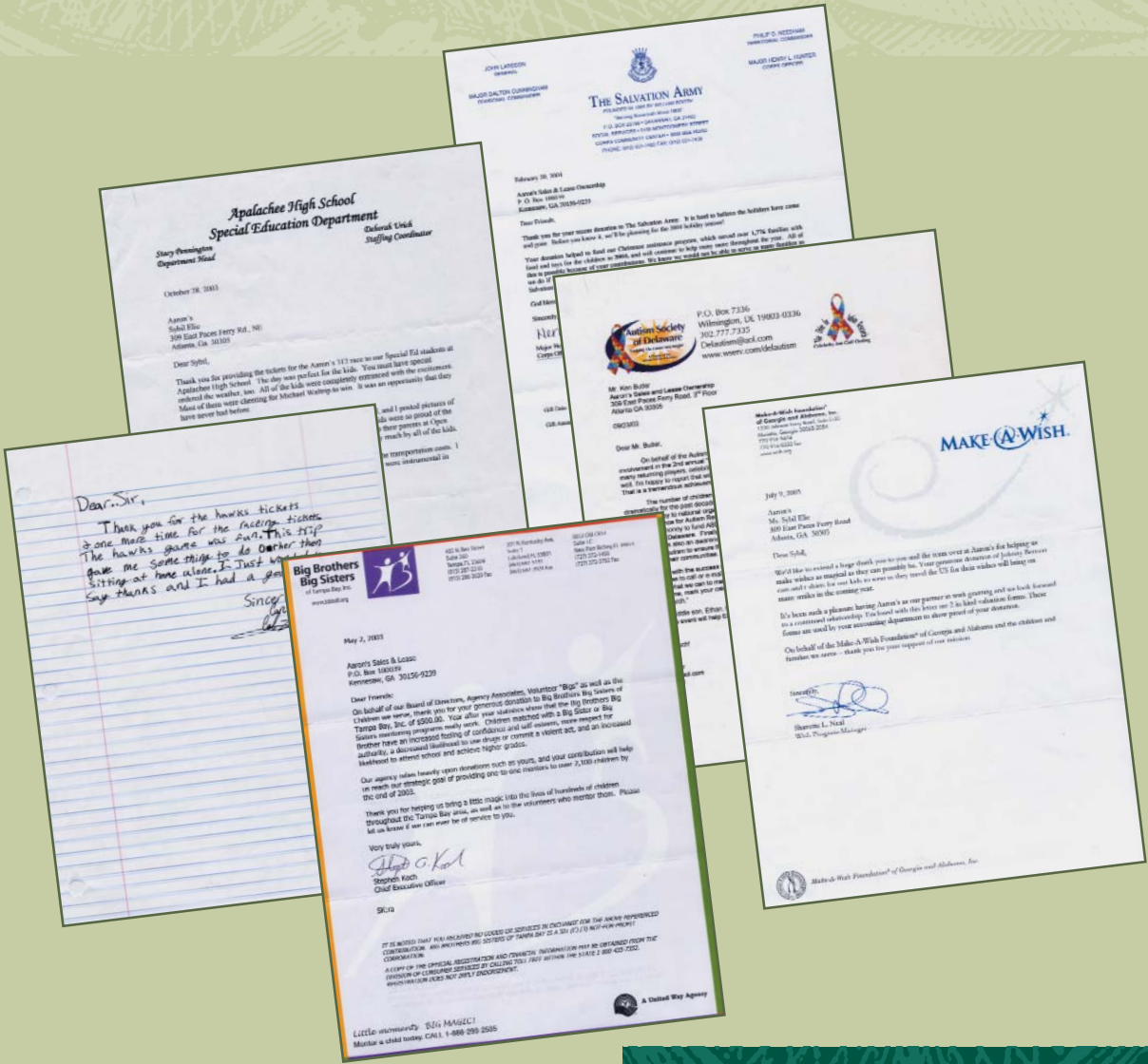
MACTAVISH FURNITURE
INDUSTRIES AND DISTRIBUTION CENTERS
Stocking the Stores



Aaron's vertical integration and volume purchasing are competitive advantages and key factors in assuring timely delivery of merchandise to customers. Unique in its industry, Aaron's produces the majority of the furniture for its stores at the ten MacTavish facilities comprising the Company's manufacturing division, creating cost benefits that are passed on to customers. Vertical integration also allows the Company to control design and quality, ensuring the functionality and durability required for multiple rentals. During 2003, MacTavish produced more than \$60 million in furniture, accessories and bedding at cost, ranking this division among the top furniture manufacturers in the United States.

Supporting this manufacturing capability is a network of distribution centers, a dedicated store service system unmatched by any competitor. Twelve distribution centers are located in key regions of the country, enabling stores

to provide same-day or next-day delivery, another competitive edge. The Magnolia, Mississippi distribution center is the Company's newest, having opened in early 2004. The Company expects to open several more distribution centers in 2004 to accommodate expected store growth.



**AARON'S COMMUNITY
OUTREACH PROGRAM:
We Take Stock in
Our Communities**

Aaron's associates continue to give their time and talents as volunteers in many worthy causes, and Aaron's Community Outreach Program (ACORP) has made substantial contributions to communities served by the Company's stores. Through this program, a store may earn, based on attained performance goals, up to \$500 each month to donate to local charities selected by the store's associates. Recipients of the Aaron's donations include a wide range of organizations including Boys and Girls Clubs, the Make-A-Wish Foundation, the Muscular Dystrophy Association and Toys For Tots. In 2003, through efforts with

Charlie Loudermilk, Chairman and Chief Executive Officer, won the International Furniture Rental Association's highest honor at the trade group's annual meeting in 2003. The Carl F. Barron Outstanding Achievement Award recognizes an individual who has provided exemplary service to the furniture rental industry.

the Warrick Dunn Foundation and Kurt Warner's First Things First, ACORP helped 12 single mothers achieve their goal of becoming first-time homeowners. Since 1999, ACORP has donated more than \$1.4 million to deserving charities in communities served by Aaron's stores, a tangible expression of the spirit of giving of Aaron's associates.

SELECTED FINANCIAL INFORMATION

(Dollar Amounts in Thousands, Except Per Share)	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001	Year Ended December 31, 2000	Year Ended December 31, 1999
Systemwide Revenues ¹	\$1,033,350	\$874,709	\$735,389	\$656,096	\$547,255
OPERATING RESULTS					
Revenues:					
Rentals & Fees	\$ 553,773	\$459,179	\$403,385	\$359,880	\$318,154
Retail Sales	68,786	72,698	60,481	62,417	62,296
Non-Retail Sales	120,355	88,969	66,212	65,498	45,394
Other	23,883	19,842	16,603	15,125	11,515
	766,797	640,688	546,681	502,920	437,359
Costs & Expenses:					
Retail Cost of Sales	50,913	53,856	43,987	44,156	45,254
Non-Retail Cost of Sales	111,714	82,407	61,999	60,996	42,451
Operating Expenses	344,884	293,346	276,682	227,587	201,923
Depreciation of Rental Merchandise	195,661	162,660	137,900	120,650	102,324
Interest	5,782	4,767	6,258	5,625	4,105
	708,954	597,036	526,826	459,014	396,057
Earnings Before Income Taxes	57,843	43,652	19,855	43,906	41,302
Income Taxes	21,417	16,212	7,519	16,645	15,700
Net Earnings	\$ 36,426	\$ 27,440	\$ 12,336	\$ 27,261	\$ 25,602
Earnings Per Share	\$ 1.12	\$.87	\$.41	\$.92	\$.85
Earnings Per Share Assuming Dilution	1.10	.86	.41	.91	.84
Dividends Per Share:					
Common	\$.033	\$.027	\$.027	\$.027	\$.027
Class A	.033	.027	.027	.027	.027
FINANCIAL POSITION					
Rental Merchandise, Net	\$ 343,013	\$317,287	\$258,932	\$267,713	\$219,831
Property, Plant & Equipment, Net	99,584	87,094	77,282	63,174	55,918
Total Assets	555,292	483,648	397,196	380,379	318,408
Interest-Bearing Debt	79,570	73,265	77,713	104,769	72,760
Shareholders' Equity	320,186	280,545	219,967	208,538	183,718
AT YEAR END					
Stores Open:					
Company-Operated	560	482	439	361	320
Franchised	287	232	209	193	155
Rental Agreements in Effect	464,800	369,000	314,600	281,000	254,000
Number of Employees	5,400	4,800	4,200	3,900	3,600
¹ Non-GAAP systemwide revenues are calculated by adding GAAP revenues to the revenues of the Company's franchisees and subtracting the Company's royalty revenues. Franchisee revenues, however, are not revenues of Aaron Rents, Inc. Below is a reconciliation of non-GAAP systemwide revenues to Company revenues:					
Company Gross Revenues	\$ 766,797	\$640,688	\$546,681	\$502,920	\$437,359
Franchisees' Revenues	280,552	246,338	198,640	161,238	115,680
Less Company Royalty Revenues	(13,999)	(12,317)	(9,932)	(8,062)	(5,784)
Systemwide Revenues	\$1,033,350	\$874,709	\$735,389	\$656,096	\$547,255

The Company adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*, on January 1, 2002. If the Company had applied the non-amortization provisions of Statement 142 for all periods presented, net earnings and diluted earnings per share would have increased by approximately \$688,000 (\$.02 per share), \$431,000 (\$.01 per share), and \$323,000 (\$.01 per share) for the years ended December 31, 2001, 2000, and 1999, respectively.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

EXECUTIVE SUMMARY

Aaron Rents, Inc. is a leading U.S. company engaged in the combined businesses of the rental, lease ownership and specialty retailing of consumer electronics, residential and office furniture, household appliances and accessories. As of December 31, 2003, we had 847 systemwide stores, which includes both our Company-operated and franchised stores, and operated in 43 states, Puerto Rico and Canada. During 2003, we achieved a significant milestone, reaching and exceeding \$1 billion in systemwide revenues. See below for a description of how we calculate systemwide revenues, a non-GAAP measure that includes revenues of our franchisees, and reconcile them to our GAAP revenues.

Our major operating divisions are the Aaron's Sales & Lease Ownership division, the Aaron Rents' Rent-to-Rent division, and the MacTavish Furniture Industries division.

- Our sales and lease ownership division now operates in excess of 500 stores and has more than 287 franchised stores in 43 states, Puerto Rico and Canada. Our sales and lease ownership division represents the fastest growing segment of our business, accounting for 86%, 81%, and 72% of our total revenues in 2003, 2002, and 2001, respectively.
- Our rent-to-rent division, which we have operated since our Company was founded in 1955, remains an important part of our business and continues to generate significant cash flow to help fund our growth. The rent-to-rent division is one of the largest providers of temporary rental furniture in the United States, operating 60 stores in 14 states at December 31, 2003. Over the last few years, we have consolidated or closed stores in the rent-to-rent division as we focus on maintaining the profitability of the division.
- Our MacTavish Furniture Industries division manufactures and supplies nearly one-half of the furniture and related accessories rented and sold in our stores.

Most of our growth comes from the opening of new sales and lease ownership stores, and improvements in same store revenues for previously opened stores. We added 143 sales and lease ownership stores in 2003, through the opening of new Company-operated stores, franchise stores, and acquisitions. We acquire sales and lease ownership stores from time to time, generally either from small operators of rental stores or from our franchisees. In 2003, we acquired 33 stores from other operators and 26 stores from our franchisees. We expect to open approximately 80 Company-operated stores in 2004. In 2001, we accelerated the growth of our sales and lease ownership store openings when we acquired the real estate locations of approximately 80 retail stores from a furniture retailer in bankruptcy proceedings. While this accelerated schedule depressed our earnings during the start-up period of these stores, we have been pleased with the performance of these new locations and they have subsequently become accretive to earnings.

We also use our franchise program to help us expand our sales and lease ownership concept more quickly and into more areas than we otherwise would by opening only Company-operated stores. Our franchisees opened 51 stores in 2003, and we converted 31 stores of a third-party rental operator to franchise stores. We expect to open approximately 60 franchise stores in 2004. Franchise royalties and other related fees represent a growing source of revenue for us, accounting for 2.5%, 2.6% and 2.5% of our total revenues in 2003, 2002 and 2001, respectively.

KEY COMPONENTS OF INCOME

Systemwide Revenues. The non-GAAP measure systemwide revenues is calculated by adding Company revenues determined in accordance with GAAP to the revenues of the Company's franchisees and subtracting the Company's royalty revenues. Franchisee revenues, however, are not revenues of Aaron Rents, Inc. Management believes that presentation of non-GAAP financial measures such as systemwide revenues is useful because it allows investors and management to evaluate and compare the overall growth and penetration of the Aaron's brand in a more meaningful manner than relying exclusively on GAAP financial measures. Non-GAAP financial measures, however, should not be considered in isolation or as an alternative to financial measures calculated and presented in accordance with GAAP. Because systemwide revenues is not a measurement determined in accordance with GAAP and is thus susceptible to varying calculations, systemwide revenues as used herein may not be comparable to other similarly titled measures used by other companies. We have determined that Company revenues calculated and presented in accordance with GAAP is the most directly comparable financial measure to non-GAAP systemwide revenues, and a reconciliation of Company revenues to systemwide revenues is presented below:

(In Thousands)	Year Ended December 31, 2003
Company Gross Revenues	\$ 766,797
Franchisees' Revenues	280,552
Less Company Royalty Revenues	(13,999)
Non-GAAP Systemwide Revenues	\$1,033,350

Revenues. We separate our total revenues into four components: rentals and fees, retail sales, non-retail sales, and other revenues. Rentals and fees includes all revenues derived from rental agreements from our sales and lease ownership and rent-to-rent stores, including agreements that result in our customers acquiring ownership at the end of the term. Retail sales represents sales of both new and rental return merchandise. Non-retail sales mainly represents merchandise sales to our franchisees from our sales and lease ownership division. Other revenues represents franchise fees and royalty income, and other related income from our franchise stores and other miscellaneous revenues

Cost of Sales. We separate our cost of sales into two components: retail and non-retail. Retail cost of sales represents the original or depreciated cost of merchandise sold through our Company-operated stores. Non-retail cost of sales mainly represents the cost of merchandise sold to our franchisees.

Depreciation of Rental Merchandise. Depreciation of rental merchandise reflects the expense associated with depreciating merchandise held for rent and rented to customers by our Company-operated sales and lease ownership and rent-to-rent stores.

CRITICAL ACCOUNTING POLICIES

REVENUE RECOGNITION

Rental revenues are recognized in the month they are due on the accrual basis of accounting. For internal management reporting purposes, rental revenues from the sales and lease ownership division are recognized as revenue in the month the cash is collected. On a monthly basis, we record an accrual for rental revenues due but not yet received, net of allowances, and a deferral of revenue for rental payments received prior to the month due. Our revenue recognition accounting policy matches the rental revenue with the corresponding costs—mainly depreciation—associated with the rental merchandise. At the years ended December 31, 2003 and 2002, we had a net revenue deferral representing cash collected in advance of being due or otherwise earned totaling approximately \$12.4 million and \$7.5 million, respectively. Revenues from the sale of residential and office furniture and other merchandise are recognized at the time of shipment.

RENTAL MERCHANDISE DEPRECIATION

Our sales and lease ownership division depreciates merchandise over the agreement period, generally 12 to 24 months when rented, and 36 months when not rented, to 0% salvage value. Prior to 2002, we depreciated sales and lease ownership merchandise as soon as it was delivered to our stores from our distribution centers. In the first quarter of 2002, we began depreciating this merchandise upon the earlier to occur of its initial lease to a customer or 12 months after it is acquired from the vendor. See Note B to the Consolidated Financial Statements. Nevertheless, sales and lease ownership merchandise is generally depreciated at a faster rate than our rent-to-rent merchandise. As sales and lease ownership revenues continue to comprise an increasing percentage of total revenues, we expect rental merchandise depreciation to increase at a correspondingly faster rate. Our rent-to-rent division depreciates merchandise over its estimated useful life, which ranges from six months to 60 months, net of its salvage value, which ranges from 0% to 60%.

Our policies require weekly rental merchandise counts by store managers, which includes a write-off for unsalable, damaged, or missing merchandise inventories. Full physical inventories are generally taken at our distribution and manufacturing facilities on a quarterly basis, and appropriate provisions are made for missing, damaged and unsalable merchandise. In addition, we monitor rental merchandise levels and mix by division, store and distribution center, as well as the average age of merchandise on hand. If unsalable rental merchandise cannot be returned to vendors, its carrying value is adjusted to its net realizable value or written off. All rental merchandise is available for rental and sale. On a monthly basis, we write off damaged, lost or unsalable merchandise as identified. These write-offs totaled approximately \$11.9 million, \$10.1 million, and \$10 million during the years ended December 31, 2003, 2002, and 2001, respectively.

CLOSED STORE RESERVES

From time to time, we close or consolidate retail stores. We record an estimate of the future obligation related to closed stores based upon the present value of the future lease payments and related commitments, net of estimated sublease income which we base upon historical experience. At the years ended December 31, 2003 and 2002, our reserve for closed stores was \$2.2 million and \$1.5 million, respectively. If our estimates related to sublease income are not correct, our actual liability may be more or less than the liability recorded at December 31, 2003.

INSURANCE PROGRAMS

Aaron Rents maintains insurance contracts for paying of workers' compensation and group health insurance claims. Using actuarial analysis and projections, we estimate the liabilities associated with open and incurred but not reported workers' compensation claims. This analysis is based upon an assessment of the likely outcome or historical experience, net of any stop loss or other supplementary coverages. We also calculate the projected outstanding plan liability for our group health insurance program. Our liability for workers' compensation insurance claims and group health insurance was approximately \$3.8 million and \$3.1 million, respectively, at the years ended December 31, 2003 and 2002.

If we resolve existing workers' compensation claims for amounts that are in excess of our current estimates and within policy stop loss limits, we will be required to pay additional amounts beyond those accrued at December 31, 2003. Additionally, if the actual group health insurance liability exceeds our projections, we will be required to pay additional amounts beyond those accrued at December 31, 2003.

The assumptions and conditions described above reflect management's best assumptions and estimates, but these items involve inherent uncertainties as described above, which may or may not be controllable by management. As a result, the accounting for such items could result in different amounts if management used different assumptions or if different conditions occur in future periods.

SAME STORE REVENUES

We refer to changes in same store revenues as a key performance indicator. For the year ended December 31, 2003, we calculated this figure by comparing GAAP revenues as of December 31, 2003 and 2002 for all stores open for the entire 24-month period ended December 31, 2003, excluding stores that received or transferred rental agreements from other closed or merged stores.

RESULTS OF OPERATIONS

Year Ended December 31, 2003 Versus Year Ended December 31, 2002

The following table shows key selected financial data for the years ended December 31, 2003 and 2002, and the changes in dollars and as a percentage to 2003 from 2002. Please refer to this table in conjunction with Management's Discussion and Analysis:

(In Thousands)	Year Ended December 31, 2003	Year Ended December 31, 2002	Increase/ (Decrease) in Dollars to 2003 from 2002	% Increase/ (Decrease) to 2003 from 2002
REVENUES:				
Rentals and Fees	\$553,773	\$459,179	\$ 94,594	20.6%
Retail Sales	68,786	72,698	(3,912)	(5.4)
Non-Retail Sales	120,355	88,969	31,386	35.3
Other	23,883	19,842	4,041	20.4
	766,797	640,688	126,109	19.7
COSTS AND EXPENSES:				
Retail Cost of Sales	50,913	53,856	(2,943)	(5.5)
Non-Retail Cost of Sales	111,714	82,407	29,307	35.6
Operating Expenses	344,884	293,346	51,538	17.6
Depreciation of Rental Merchandise	195,661	162,660	33,001	20.3
Interest	5,782	4,767	1,015	21.3
	708,954	597,036	111,918	18.7
EARNINGS BEFORE TAXES	57,843	43,652	14,191	32.5
INCOME TAXES	21,417	16,212	5,205	32.1
NET EARNINGS	\$ 36,426	\$ 27,440	\$ 8,986	32.7%

REVENUES

The 19.7% increase in total revenues in 2003 from 2002 is primarily attributable to continued growth in our sales and lease ownership division, both from the opening and acquisition of new Company-operated stores and improvement in same store revenues. Revenues for our sales and lease ownership division increased \$137.5 million to \$656.5 million in 2003 compared with \$519.0 million in 2002, a 26.5% increase. This increase was attributable to a 10.1% increase in same store revenues and the addition of 136 Company-operated stores since the beginning of 2002. Total revenues were impacted by a decrease in rent-to-rent division revenues, which decreased \$11.4 million to \$110.3 million in 2003 from \$121.7 million in 2002, a 9.3% decrease, due primarily to a decline in same store revenues as well as a net reduction of 15 stores since the beginning of 2002.

The 20.6% increase in rentals and fees revenues was attributable to a \$100.9 million increase from our sales and lease ownership division related to the growth in same store revenues and the increase in the number of stores described above. The growth in our sales and lease ownership division was offset by a \$6.3 million decrease in rental revenues in our rent-to-rent division. The decrease in rent-to-rent division revenues is primarily the result of the decline in same store revenues and the net reduction in stores described above.

Revenues from retail sales fell 5.4% due to a decrease of \$4.6 million in our rent-to-rent division caused by the decline in same store revenues and the store closures described above, partially offset by an increase of \$0.7 million in our sales and lease ownership division caused by the increase in same store revenues and the increase in the number of stores also described above. This increase in our sales and lease ownership division was negatively impacted by the introduction of an alternative shorter-term lease, which replaced many retail sales.

The 35.3% increase in non-retail sales in 2003 reflects the significant growth of our franchise operations.

The 20.4% increase in other revenues was primarily attributable to franchise fees, royalty income, and other related revenues from our franchise stores increasing \$2.7 million, or 16.5%, to \$19.3 million compared with \$16.6 million in 2002, reflecting the net addition of 78 franchised stores since the beginning of 2002 and improved operating revenues at older franchised stores.

COST OF SALES

The 5.5% decrease in retail cost of sales is primarily a result of a decrease in sales in our rent-to-rent division, where sales decreased \$3.9 million to \$25.2 million in 2003 from \$29.1 million in 2002, a 13.4% decline. This decrease was primarily due to the decline in same store revenues and to closing or merging underperforming stores. This decrease is partially offset by a \$1.0 million increase to \$25.7 million in 2003 from \$24.7 million in 2002, representing a 3.9% increase, in our sales and lease ownership division driven by the increases in same store revenues and additional store openings described above. Retail cost of sales as a percentage of retail sales remained comparable between 2003 and 2002.

Cost of sales from non-retail sales increased 35.6%, primarily due to the growth of our franchise operations as described above, corresponding to the similar increase in non-retail sales. As a percentage of non-retail sales, non-retail cost of sales increased slightly to 92.8% in 2003 as compared to 92.6% in 2002, primarily due to changes in product mix.

EXPENSES

The 17.6% increase in 2003 operating expenses was driven by the growth of our sales and lease ownership division described above. As a percentage of total revenues, operating expenses improved to 45.0% for 2003 from 45.8% for 2002, with the decrease driven by the maturing of new Company-operated sales and lease ownership stores added over the past several years and a 10.1% increase in same store revenues.

The 20.3% increase in depreciation of rental merchandise was driven by the growth of our sales and lease ownership division described above. As a percentage of total rentals and fees, depreciation of rental merchandise decreased slightly to 35.3% in 2003 from 35.4% in 2002. The decrease as a percentage of rentals and fees reflects an improvement in rental margins, partially offset by increased depreciation expense as a result of a larger number of short-term leases in 2003.

The increase in interest expense as a percentage of total revenues was primarily due to a higher long-term average debt balance during 2003 arising from the Company's August 2002 private debt placement.

The 32.1% increase in income tax expense between years was driven primarily by a comparable increase in pretax income, offset by a slightly lower effective tax rate of 37.0% in 2003 compared to 37.1% in 2002.

NET EARNINGS

The 32.7% increase in net earnings was primarily due to the maturing of new Company-operated sales and lease ownership stores added over the past several years, a 10.1% increase in same store revenues, and a 16.5% increase in franchise fees, royalty income, and other related franchise income. As a percentage of total revenues, net earnings improved to 4.8% in 2003 from 4.3% in 2002.

Year Ended December 31, 2002 Versus Year Ended December 31, 2001

The following table shows key selected financial data for the years ended December 31, 2002 and 2001, and the changes in dollars and as a percentage to 2002 from 2001. Please refer to this table in conjunction with Management's Discussion and Analysis:

(In Thousands)	Year Ended December 31, 2002	Year Ended December 31, 2001	Increase/ (Decrease) in Dollars to 2002 from 2001	% Increase/ (Decrease) to 2002 from 2001
REVENUES:				
Rentals and Fees	\$459,179	\$403,385	\$55,794	13.8%
Retail Sales	72,698	60,481	12,217	20.2
Non-Retail Sales	88,969	66,212	22,757	34.4
Other	19,842	16,603	3,239	19.5
	640,688	546,681	94,007	17.2
COSTS AND EXPENSES:				
Retail Cost of Sales	53,856	43,987	9,869	22.4
Non-Retail Cost of Sales	82,407	61,999	20,408	32.9
Operating Expenses	293,346	276,682	16,664	6.0
Depreciation of Rental Merchandise	162,660	137,900	24,760	18.0
Interest	4,767	6,258	(1,491)	(23.8)
	597,036	526,826	70,210	13.3
EARNINGS BEFORE TAXES	43,652	19,855	23,797	119.9
INCOME TAXES	16,212	7,519	8,693	115.6
NET EARNINGS	\$ 27,440	\$ 12,336	\$ 15,104	122.4%

REVENUES

The 17.2% increase in total revenues in 2002 from 2001 is primarily attributable to continued growth in our sales and lease ownership division, both from the opening and acquisition of new Company-operated stores and improvement in same store revenues. Revenues for our sales and lease ownership division increased \$124.2 million to \$519.0 million in 2002 compared with \$394.8 million in 2001, a 31.5% increase. This increase was attributable to an average increase of 13% in same store revenues in 2002 and to the addition of 149 Company-operated stores since the beginning of 2001. Total revenues were impacted by a decrease in rent-to-rent division revenues, which decreased 19.9% to \$121.7 million from \$151.9 million in 2001, due primarily to our decision to close, merge, or sell 29 underperforming stores since the beginning of 2001, as well as a decline of same store revenues.

The 13.8% increase in rentals and fees revenues was attributable to a \$77.3 million increase from our sales and lease ownership division, driven by the growth in same store revenues and number of stores as described above. The growth in our sales and lease ownership division was offset by a \$21.5 million decrease in rental revenues in our rent-to-rent division. The decrease in rent-to-rent division revenues was caused primarily by the closure of underperforming stores and decline in same store revenues described above.

Revenues from retail sales increased 20.2% due to an increase of \$20.8 million in the sales and lease ownership

division offset by a decrease of \$8.6 million in our rent-to-rent division relating to the respective changes in same store revenues and numbers of open stores.

The 34.4% increase in non-retail sales reflects the significant growth of our franchise operations.

The 19.5% increase in other revenues was primarily attributable to franchise fee and royalty income increasing \$3 million, or 21.8%, to \$16.6 million in 2002 compared with \$13.6 million in 2001, reflecting the net addition of 23 franchised stores in 2002 and improved operating revenues at older franchised stores.

COST OF SALES

The increase in retail cost of sales as a percentage of sales was primarily due to a slight decrease in margins in both the rent-to-rent and sales and lease ownership divisions in 2002 along with lower margins on retail sales from our newly

acquired Sight & Sound stores. The increased margins on non-retail sales were primarily the result of higher margins on certain products sold to franchisees.

EXPENSES

As a percentage of total revenues, operating expenses were 45.8% in 2002 and 50.6% in 2001. Operating expenses decreased in 2002 as a percentage of total revenues primarily due to higher costs in 2001 associated with the acquisition of sales and lease ownership store locations formerly operated by one of the nation's largest furniture retailers along with other new store openings, coupled with noncash charges of \$5.6 million related to the rent-to-rent division. In addition, we discontinued amortizing goodwill in 2002 in connection with the adoption of a new accounting standard. As a result of this adoption, we incurred no goodwill amortization expense in 2002, compared with approximately \$688,000 in 2001.

As a percentage of total rentals and fees, depreciation of rental merchandise increased to 35.4% in 2002 from 34.2% in 2001. The increase as a percentage of rentals and fees reflects a greater percentage of our rentals and fees revenues coming from our sales and lease ownership division, which depreciates its rental merchandise at a faster rate than our rent-to-rent division.

On January 1, 2002, we began depreciating sales and lease ownership merchandise upon the earlier to occur of its initial lease to a customer or 12 months after it is acquired from the vendor. Previously, we began

depreciating sales and lease ownership merchandise as soon as it was delivered to our stores from our distribution centers. This change in accounting method increased net earnings by approximately \$3 million, or \$.09 per diluted common share in 2002.

As a percentage of total revenues, interest expense decreased to 0.7% in 2002 from 1.1% in 2001. The decrease in interest expense as a percentage of total revenues was primarily due to lower debt levels in 2002.

Income tax expense increased due to increased pretax earnings. Aaron Rents' effective tax rate was 37.1% in 2002 compared with 37.9% in 2001, primarily due to lower nondeductible expenses.

NET EARNINGS

As a percentage of total revenues, net earnings were 4.3% in 2002 and 2.3% in 2001. The increase in net earnings was primarily due to the non-cash charges of \$5.6 million incurred in the third quarter of 2001 along with the maturing 100 Company-operated sales and lease ownership stores added in 2001 and a 13% increase in same store revenue growth, coupled with the change in our rental merchandise depreciation method and the non-amortization of goodwill. In addition, the Company experienced higher than usual operating expenses in 2001 associated with the addition of 100 Company-operated stores.

BALANCE SHEET

Cash. Our cash balance remained virtually unchanged with balances of \$95,000 and \$96,000 at December 31, 2003 and 2002, respectively. The consistency of the cash balance is the result of the Company being a net borrower, with all excess cash being used to pay down debt balances.

Deferred Income Taxes Payable. The increase of \$4.8 million in deferred income taxes payable at December 31, 2003 from December 31, 2002 is primarily the result of March 2002 tax law changes, effective September 2001, that allow additional accelerated depreciation of rental merchandise for tax purposes. Additional tax law changes effective May 2003 increased the allowable acceleration and extended the life of the March 2002 changes to December 31, 2004.

Accounts Payable and Accrued Expenses. The increase of \$19.7 million in accounts payable and accrued expenses relates primarily to accrued operating expenses relating to the growth of the Company's sales and lease ownership division.

Credit Facilities. The increase in credit facilities of \$6.3 million to December 31, 2003 from December 31, 2002 is primarily the result of increased borrowing on our working capital line of credit to fund expansion of our sales and lease ownership division.

Goodwill and Other Intangibles. The increase of \$29.5 million to December 31, 2003 from December 31, 2002 is the result of a series of acquisitions of sales and lease ownership businesses during 2003. The aggregate purchase price for these asset acquisitions totaled approximately \$45.0 million, and the principal tangible assets acquired consisted of rental merchandise and certain fixtures and equipment.

LIQUIDITY AND CAPITAL RESOURCES

GENERAL

Cash flows from operating activities for the years ended December 31, 2003 and 2002 were \$67.0 million and \$10.1 million, respectively. Our cash flows include profits on the sale of rental return merchandise. Our primary capital requirements consist of buying rental merchandise for both

Company-operated sales and lease ownership and rent-to-rent stores. As Aaron Rents continues to grow, the need for additional rental merchandise will continue to be our major capital requirement. These capital requirements historically have been financed through:

- cash flow from operations
- bank credit
- trade credit with vendors
- proceeds from the sale of rental return merchandise
- private debt
- stock offerings

At December 31, 2003, \$13.9 million was outstanding under our revolving credit agreement. The increase in borrowings is primarily attributable to cash invested in new store growth throughout 2003. From time to time, we use interest rate swap agreements as part of our overall long-term financing program. We also have \$50 million in aggregate principal amount of 6.88% senior unsecured notes due August 2009 currently outstanding, principal repayments for which are first required in 2005.

Our revolving credit agreement, senior unsecured notes, the construction and lease facility, and the franchisee loan program discussed below contain financial covenants which, among other things, forbid us from exceeding certain debt to equity levels and require us to maintain minimum fixed charge coverage ratios. If we fail to comply with these covenants, we will be in default under these commitments, and all amounts would become due immediately. We were in compliance with all these covenants at December 31, 2003.

We purchase our common shares in the market from time to time as authorized by our Board of Directors. As of December 31, 2003, our Board of Directors has authorized us to purchase up to an additional 1,780,335 common shares.

At our annual shareholders meeting in May 2003, our shareholders authorized an increase in the authorized number of shares of Common Stock by 25 million shares for a total of 50 million shares. The purpose of increasing the number of shares of authorized Common Stock is to give the Company greater flexibility in connection with its capital structure, possible future financing requirements, potential acquisitions, employee compensation, and other corporate matters, including stock splits like the 3-for-2 split described below.

We have a consistent history of paying dividends, having paid dividends for 17 consecutive years. A \$.013 per share dividend on Common Stock and Class A Common Stock was paid in January 2003 and July 2003. In addition, our Board of Directors declared a 3-for-2 stock split, effected in the form of a 50% stock dividend, which was distributed to shareholders in August 2003, for a total fiscal year cash outlay of \$924,000. Subject to sufficient operating profits, to any future capital needs, and to other contingencies, we currently expect to continue our policy of paying dividends.

We currently hold 474,500 shares, or 8%, of the outstanding common stock of Rainbow Rentals Inc., a NASDAQ-listed rental company that has entered into an agreement to be acquired by Rent-A-Center, Inc. for a purchase price of \$16.00 per share. We had acquired these shares in three separate transactions in September 2002 and January 2003, and held the shares for investment purposes. If the sale is consummated in the second quarter of 2004 as announced by those parties, we would receive cash proceeds of approximately \$7.6 million and recognize approximately a \$5.5 million gain. We are not, however, a party to the agreement between Rainbow Rentals and Rent-A-Center, and the closing of that transaction is subject to all of the closing conditions of that agreement.

We believe that our expected cash flows from operations, existing credit facilities and vendor credit will be sufficient to fund our capital and liquidity needs for at least the next 24 months.

COMMITMENTS

Construction and Lease Facility. On October 31, 2001, we renewed our \$25 million construction and lease facility. From 1996 to 1999, we arranged for a bank holding company to purchase or construct properties identified by us pursuant to this facility, and we subsequently leased these properties from the bank holding company under operating lease agreements. The total amount advanced and outstanding under this facility at December 31, 2003 was approximately \$24.9 million. Since the resulting leases are accounted for as operating leases, we do not record any debt obligation on our balance sheet. This construction and lease facility expires in 2006. Lease payments fluctuate based upon current interest rates and are generally based upon LIBOR plus 1.1%. The lease facility contains residual value guarantee and default guarantee provisions that would require us to make payments to the lessor if the underlying properties are worth less at termination of the facility than agreed-upon values in the agreement. Although we believe the likelihood of funding to be remote, the maximum guarantee obligation under the residual value and default guarantee provisions upon termination are approximately \$21.1 million and \$24.9 million, respectively, at December 31, 2003.

Leases. Aaron Rents leases warehouse and retail store space for substantially all of its operations under operating leases expiring at various times through 2017. Most of the leases contain renewal options for additional periods ranging from one to 15 years or provide for options to purchase the related property at predetermined purchase prices that do not represent bargain purchase options. We also lease transportation and computer equipment under operating leases expiring during the next three years. We expect that most leases will be renewed or replaced by other leases in the normal course of business. Approximate future minimum rental payments required under operating leases that have initial or remaining noncancelable terms in excess of one year as of December 31, 2003, including leases under our construction and lease facility described above, are as follows: \$40,329,000 in 2004; \$31,637,000 in 2005; \$22,263,000 in 2006; \$14,126,000 in 2007; \$7,592,000 in 2008; and \$8,147,000 thereafter.

We have 13 capital leases, 12 of which are with limited liability companies (LLCs) whose owners include Aaron Rents' executive officers and majority shareholder. Eleven of these related-party leases relate to properties purchased from Aaron Rents in December 2002 by one of the LLCs for a total purchase price of approximately \$5 million. This LLC is leasing back these properties to Aaron Rents for a 15-year term at an aggregate annual rental of approximately \$635,000. The other related-party capital lease relates to a property sold by Aaron Rents to a second LLC for \$6.3 million in April 2002 and leased back to Aaron Rents for a 15-year term at an annual rental of approximately \$617,000. See Note E to the Consolidated Financial Statements.

Franchise Guaranty. We have guaranteed the borrowings of certain independent franchisees under a franchise loan program with two banks. In the event these franchisees are unable to meet their debt service payments or otherwise experience an event of default, we would be unconditionally liable for a portion of the outstanding balance of the franchisees' debt obligations, which would be due in full within 90 days of the event of default. At December 31, 2003, the portion that we might be obligated to repay in the event our franchisees defaulted was approximately \$67.5 million. However, due to franchisee borrowing limits, we believe any losses associated with any defaults would be mitigated through recovery of rental merchandise and other assets. Since its inception, we have had no losses associated with the franchisee loan and guaranty program.

We have no long-term commitments to purchase merchandise. See Note G to the Consolidated Financial Statements for further information. The following table shows our approximate contractual obligations and commitments to make future payments as of December 31, 2003:

(In Thousands)	Total	Period Less Than 1 Year	Period 1-3 Years	Period 4-5 Years	Period Over 5 Years
Credit Facilities, Excluding Capital Leases	\$ 68,107	\$13,874	\$20,008	\$20,010	\$14,215
Capital Leases	11,463	388	889	1,249	8,937
Operating Leases	124,094	40,329	53,900	21,718	8,147
Total Contractual Cash Obligations	\$203,664	\$54,591	\$74,797	\$42,977	\$31,299

The following table shows the Company's approximate commercial commitments as of December 31, 2003:

(In Thousands)	Total	Period Less Than 1 Year	Period 1-3 Years	Period 4-5 Years	Period Over 5 Years
Guaranteed Borrowings of Franchisees	\$67,455	\$67,455	\$	\$	\$
Residual Value Guarantee Under Operating Leases	21,149		21,149		
Total Commercial Commitments	\$88,604	\$67,455	\$21,149	\$	\$

Purchase orders or contracts for the purchase of rental merchandise and other goods and services are not included in the table above. We are not able to determine the aggregate amount of such purchase orders that represent contractual obligations, as purchase orders may represent authorizations to purchase rather than binding agreements. Our purchase orders are based on our current distribution needs and are fulfilled by our vendors within short time horizons. We do not have significant agreements for the purchase of rental merchandise or other goods specifying minimum quantities or set prices that exceed our expected requirements for three months.

MARKET RISK

We manage our exposure to changes in short-term interest rates, particularly to reduce the impact on our variable payment construction and lease facility and floating-rate borrowings, by entering into interest rate swap agreements. These swap agreements involve the receipt of amounts by us when floating rates exceed the fixed rates and the payment of amounts by us to the counterparties when fixed rates exceed the floating rates in the agreements over their term. We accrue the differential we may pay or receive as interest rates change and recognize it as an adjustment to the floating-rate interest expense related to our debt. The counterparties to these contracts are high credit-quality commercial banks, which we believe minimizes to a large extent the risk of counterparty default.

At December 31, 2003, we had swap agreements with total notional principal amounts of \$20 million that effectively fixed the interest rates on obligations in the notional amount of \$20 million of debt under our variable payment construction and lease facility at an average rate of

7.6% until June 2005. In 2002, we reassigned approximately \$28 million of notional amount of swaps to the variable payment obligations under our construction and lease facility and other debt as described above. Certain of these swaps have since expired. Since August 2002, fixed rate swap agreements in the notional amount of \$32 million were not being utilized as a hedge of variable obligations, and accordingly, changes in the valuation of such swap agreements are recorded directly to earnings. These swaps have since expired as well. The fair value of interest rate swap agreements was a liability of approximately \$1.4 million at December 31, 2003. A 1% adverse change in interest rates on variable rate obligations would not have a material adverse impact on the future earnings and cash flows of the Company.

We do not use any market-risk-sensitive instruments to hedge commodity, foreign currency, or risks other than interest rate risk and hold no market-risk-sensitive instruments for trading or speculative purposes.

RECENT ACCOUNTING PRONOUNCEMENTS

Effective January 1, 2002, the Company adopted SFAS No. 141, *Business Combinations* (SFAS No. 141), and SFAS No. 142. SFAS No. 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. SFAS No. 142 requires that entities assess the fair value of the net assets underlying all acquisition-related goodwill on a reporting unit basis (see Note B to the Consolidated Financial Statements).

In June 2002, the Financial Accounting Standards Board (FASB) issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities* (SFAS No. 146) which addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)*. SFAS No. 146 requires that a liability for costs associated with an exit or disposal activity be recognized when the liability is incurred as opposed to the date of an entity's commitment to an exit plan. SFAS No. 146 also establishes fair value as the objective for initial measurement of the liability. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002. Adoption of SFAS No. 146 did not have a material effect on the Company's financial statements.

In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* (FIN 45). FIN 45 requires an entity to disclose in its interim and annual financial statements information with respect to its obligations under certain guarantees that it has issued. It also requires an entity to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The disclosure requirements of FIN 45 are effective for interim and annual periods ending after December 15, 2002. These disclosures are presented in Note G to the Consolidated Financial Statements. The initial recognition and measurement requirements of FIN 45 are effective prospectively for guarantees issued or modified after December 31, 2002. The adoption of the recognition provisions of FIN 45 had no significant effect on the consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51* (FIN 46). FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary

of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective immediately for all new variable interest entities created or acquired after January 31, 2003. The Company has not entered into transactions with, created, or acquired significant potential variable interest entities subsequent to that date. For interests in variable interest entities arising prior to February 1, 2003, the Company must apply the provisions of FIN 46 as of December 31, 2003. The Company has concluded that certain independent franchisees, as discussed in Note J to the Consolidated Financial Statements, are not subject to the interpretation and are therefore not included in the Company's consolidated financial statements. In addition, as discussed in Note E to the Consolidated Financial Statements, the Company has certain capital leases with partnerships controlled by related parties of the Company. The Company has concluded that these partnerships are not variable interest entities. The Company has concluded that the accounting and reporting of its construction and lease facility (see Note G to the Consolidated Financial Statements) are not subject to the provisions of FIN 46 since the lessor is not a variable interest entity, as defined by FIN 46.

In January 2003, the Emerging Issues Task Force (EITF) of the FASB issued EITF Issue No. 02-16, *Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor* (EITF 02-16). EITF 02-16 addresses accounting and reporting issues related to how a reseller should account for cash consideration received from vendors. Generally, cash consideration received from vendors is presumed to be a reduction of the prices of the vendor's products or services and should, therefore, be characterized as a reduction of cost of sales when recognized in the customer's income statement. However, under certain circumstances this presumption may be overcome and recognition as revenue or as a reduction of other costs in the income statement may be appropriate. The Company does receive cash consideration from vendors subject to the provisions of EITF 02-16. EITF 02-16 is effective for fiscal periods beginning after December 15, 2002. The Company adopted EITF 02-16 as of January 1, 2003. Such adoption did not have a material effect on the Company's financial statements since substantially all cooperative advertising consideration received from vendors represents a reimbursement of specific identifiable and incremental costs incurred in selling those vendors' products.

FORWARD-LOOKING STATEMENTS

Certain written and oral statements made by our Company may constitute "forward-looking statements" as defined under the Private Securities Litigation Reform Act of 1995, including statements made in this report and other filings with the Securities and Exchange Commission. All statements which address operating performance, events, or developments that we expect or anticipate will occur in the future—including growth in store openings and franchises awarded, market share, and statements expressing general optimism about future operating results—are forward-looking statements. Forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially. The Company undertakes no obligation to publicly update or revise any forward-looking statements. For a discussion of such risks and uncertainties see "Certain Factors Affecting Forward-Looking Statements" in Item I of the Company's Annual Report for the year ended December 31, 2003 on Form 10-K.

CONSOLIDATED BALANCE SHEETS

(In Thousands, Except Share Data)	December 31, 2003	December 31, 2002
ASSETS		
Cash	\$ 95	\$ 96
Accounts Receivable (net of allowances of \$1,718 in 2003 and \$1,195 in 2002)	30,878	26,973
Rental Merchandise	518,741	470,225
Less: Accumulated Depreciation	(175,728)	(152,938)
	343,013	317,287
Property, Plant & Equipment, Net	99,584	87,094
Goodwill and Other Intangibles, Net	55,485	25,985
Prepaid Expenses & Other Assets	26,237	26,213
Total Assets	\$555,292	\$483,648
LIABILITIES & SHAREHOLDERS' EQUITY		
Accounts Payable & Accrued Expenses	\$ 83,854	\$ 64,131
Dividends Payable	655	434
Deferred Income Taxes Payable	55,290	50,517
Customer Deposits & Advance Payments	15,737	14,756
Credit Facilities	79,570	73,265
Total Liabilities	235,106	203,103
Commitments & Contingencies		
Shareholders' Equity		
Common Stock, Par Value \$.50 Per Share; Authorized: 50,000,000 Shares; Shares Issued: 29,993,475 and 29,993,980 at December 31, 2003 and 2002, respectively	14,997	14,997
Class A Common Stock, Par Value \$.50 Per Share; Authorized: 25,000,000 Shares; Shares Issued: 8,042,602 and 8,042,641 at December 31, 2003 and 2002, respectively	4,021	4,021
Additional Paid-In Capital	88,305	87,502
Retained Earnings	252,924	217,589
Accumulated Other Comprehensive Loss		(1,868)
	360,247	322,241
Less: Treasury Shares at Cost, Common Stock, 2,815,750 and 3,018,705 Shares at December 31, 2003 and 2002, respectively	(24,157)	(25,792)
Class A Common Stock, 2,445,082 Shares at December 31, 2003 and 2002, respectively	(15,904)	(15,904)
Total Shareholders' Equity	320,186	280,545
Total Liabilities & Shareholders' Equity	\$555,292	\$483,648

The accompanying notes are an integral part of the Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF EARNINGS

(In Thousands, Except Per Share)	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001
REVENUES			
Rentals & Fees	\$553,773	\$459,179	\$403,385
Retail Sales	68,786	72,698	60,481
Non-Retail Sales	120,355	88,969	66,212
Other	23,883	19,842	16,603
	766,797	640,688	546,681
COSTS & EXPENSES			
Retail Cost of Sales	50,913	53,856	43,987
Non-Retail Cost of Sales	111,714	82,407	61,999
Operating Expenses	344,884	293,346	276,682
Depreciation of Rental Merchandise	195,661	162,660	137,900
Interest	5,782	4,767	6,258
	708,954	597,036	526,826
Earnings Before Taxes	57,843	43,652	19,855
Income Taxes	21,417	16,212	7,519
Net Earnings	\$ 36,426	\$ 27,440	\$ 12,336
Earnings Per Share	\$ 1.12	\$.87	\$.41
Earnings Per Share Assuming Dilution	\$ 1.10	\$.86	\$.41
Weighted Average Shares Outstanding	32,643	31,364	29,892
Weighted Average Shares Outstanding Assuming Dilution	33,189	31,850	30,213

The accompanying notes are an integral part of the Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

(In Thousands, Except Per Share)	Treasury Stock		Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	
	Shares	Amount	Common	Class A			Derivatives Designated As Hedges	Marketable Securities
BALANCE, DECEMBER 31, 2000	(5,645)	(\$42,722)	\$9,135	\$2,681	\$53,662	\$185,782	\$	\$
Dividends, \$.027 per share						(797)		
Reissued Shares	150	1,660			184			
Net Earnings						12,336		
Change in Fair Value of Financial Instruments, Net of Income Taxes of \$1,191							(1,954)	
BALANCE, DECEMBER 31, 2001	(5,495)	(41,062)	9,135	2,681	53,846	197,321	(1,954)	
Reacquired Shares	(147)	(1,667)						
Stock Offering			863		33,215			
Dividends, \$.027 per share						(833)		
Reissued Shares	177	1,033			441			
Net Earnings						27,440		
Change in Fair Value of Financial Instruments, Net of Income Taxes of \$51							(18)	104
BALANCE, DECEMBER 31, 2002	(5,465)	(41,696)	9,998	2,681	87,502	223,928	(1,972)	104
Dividends, \$.033 per share						(1,090)		
Stock Dividend			4,999	1,340	(54)	(6,340)		
Reissued Shares	204	1,635			857			
Net Earnings						36,426		
Change in Fair Value of Financial Instruments, Net of Income Taxes of \$1,209							1,031	837
BALANCE, DECEMBER 31, 2003	(5,261)	(\$40,061)	\$14,997	\$4,021	\$88,305	\$252,924	(\$ 941)	\$941

The accompanying notes are an integral part of the Consolidated Financial Statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In Thousands)	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001
OPERATING ACTIVITIES			
Net Earnings	\$ 36,426	\$ 27,440	\$ 12,336
Depreciation & Amortization	215,397	179,040	153,548
Additions to Rental Merchandise	(373,874)	(351,389)	(237,912)
Book Value of Rental Merchandise Sold	167,905	140,435	115,527
Deferred Income Taxes	3,496	29,554	1,168
Gain on Sale of Property, Plant & Equipment	(814)	(573)	(920)
Change in Accounts Payable & Accrued Expenses	16,503	(3,725)	27,320
Change in Accounts Receivable	(3,905)	(488)	(1,657)
Other Changes, Net	5,915	(10,152)	(3,357)
Cash Provided by Operating Activities	67,049	10,142	66,053
INVESTING ACTIVITIES			
Additions to Property, Plant & Equipment	(37,898)	(42,913)	(34,785)
Proceeds from Sale of Property, Plant & Equipment	8,025	18,296	7,525
Contracts & Other Assets Acquired	(44,347)	(14,033)	(12,125)
Cash Used by Investing Activities	(74,220)	(38,650)	(39,385)
FINANCING ACTIVITIES			
Proceeds from Credit Facilities	86,424	139,542	162,219
Repayments on Credit Facilities	(80,119)	(143,990)	(189,275)
Proceeds from Stock Offering		34,078	
Dividends Paid	(924)	(798)	(797)
Acquisition of Treasury Stock		(1,667)	
Issuance of Stock Under Stock Option Plans	1,789	1,346	1,183
Cash Provided (Used) by Financing Activities	7,170	28,511	(26,670)
(Decrease) Increase in Cash	(1)	3	(2)
Cash at Beginning of Year	96	93	95
Cash at End of Year	\$ 95	\$ 96	\$ 93
Cash Paid (Received) During the Year:			
Interest	\$ 6,759	\$ 4,361	\$ 6,183
Income Taxes	\$ 4,987	\$ (2,151)	\$ 3,544

The accompanying notes are an integral part of the Consolidated Financial Statements.

NOTE A: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

As of December 31, 2003 and 2002, and for the Years Ended December 31, 2003, 2002 and 2001.

Basis of Presentation—The consolidated financial statements include the accounts of Aaron Rents, Inc. and its wholly-owned subsidiaries (the Company). All significant intercompany accounts and transactions have been eliminated. The preparation of the Company's consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying notes. Actual results could differ from those estimates. Generally, actual experience has been consistent with management's prior estimates and assumptions. Management does not believe these estimates or assumptions will change significantly in the future absent unanticipated or unforeseen events.

On July 21, 2003, the Company announced a 3-for-2 stock split effected in the form of a 50% stock dividend on both Common Stock and Class A Common Stock. New shares were distributed on August 15, 2003 to shareholders of record as of the close of business on August 1, 2003. All share and per share information has been restated for all periods presented to reflect this stock dividend.

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

Line of Business—The Company is engaged in the business of renting and selling residential and office furniture, consumer electronics, appliances and other merchandise throughout the U.S., Puerto Rico, and Canada. The Company manufactures furniture principally for its rent-to-rent and sales and lease ownership operations.

Rental Merchandise—Rental merchandise consists primarily of consumer electronics, residential and office furniture, appliances, computers and other merchandise and is recorded at cost. The sales and lease ownership division depreciates merchandise over the rental agreement period, generally 12 to 24 months when on rent and 36 months when not on rent, to a 0% salvage value. The rent-to-rent division depreciates merchandise over its estimated useful life, which ranges from six months to 60 months, net of its salvage value, which ranges from 0% to 60% of historical cost. Our policies require weekly rental merchandise counts by store managers, which include a write-off for unsalable, damaged, or missing merchandise inventories. Full physical inventories are generally taken at our distribution and manufacturing facilities on a quarterly basis, and appropriate provisions are made for missing, damaged and unsalable merchandise. In addition, we monitor rental merchandise levels and mix by division, store, and distribution center, as well as the average age of merchandise on hand. If unsalable rental merchandise cannot be returned to vendors, it is adjusted to its net realizable value or written off.

All rental merchandise is available for rental and sale.

On a monthly basis, we write off damaged, lost or unsalable merchandise as identified. These write-offs, recorded as a component of operating expenses, totaled approximately \$11.9 million, \$10.1 million, and \$10 million during the years ended December 31, 2003, 2002, and 2001, respectively.

Property, Plant and Equipment—Property, plant and equipment are recorded at cost. Depreciation and amortization are computed on a straight-line basis over the estimated useful lives of the respective assets, which are from eight to 40 years for buildings and improvements and from one to five years for other depreciable property and equipment. Gains and losses related to dispositions and retirements are recognized as incurred. Maintenance and repairs are also expensed as incurred; renewals and betterments are capitalized.

Goodwill and Other Intangibles—Goodwill represents the excess of the purchase price paid over the fair value of the net assets acquired in connection with business acquisitions. Effective January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets* (SFAS No. 142). SFAS No. 142 requires that entities assess the fair value of the net assets underlying all acquisition-related goodwill on a reporting unit basis effective beginning in 2002. When the fair value is less than the related carrying value, entities are required to reduce the amount of goodwill (see Note B). The approach to evaluating the recoverability of goodwill as outlined in SFAS No. 142 requires the use of valuation techniques using estimates and assumptions about projected future operating results and other variables. The Company has elected to perform this annual evaluation on September 30. More frequent evaluations will be completed if indicators of impairment become evident. The impairment-only approach required by SFAS No. 142 may have the effect of increasing the volatility of the Company's earnings if goodwill impairment occurs at a future date. Other Intangibles represent the value of customer relationships acquired in connection with business acquisitions, recorded at fair value as determined by the Company. These intangibles are amortized on a straight-line basis over a two-year useful life.

Impairment—The Company assesses its long-lived assets other than goodwill for impairment whenever facts and circumstances indicate that the carrying amount may not be fully recoverable. To analyze recoverability, the Company projects undiscounted net future cash flows over the remaining life of such assets. If these projected cash flows were less than the carrying amount, an impairment would be recognized, resulting in a write-down of assets with a corresponding charge to earnings. Impairment losses, if any, are measured based upon the difference between the carrying amount and the fair value of the assets.

Investments in Marketable Securities—The Company holds certain marketable equity securities and has designated these securities as available-for-sale. The fair value of these securities was approximately \$3,606,000 and \$1,560,000 as of December 31, 2003 and 2002, respectively. These amounts are included in prepaid expenses and other assets in the accompanying consolidated balance sheets. Unrealized gains on these securities, net of tax, included in accumulated

other comprehensive income approximated \$837,000 and \$104,000 for the years ended December 31, 2003 and 2002, respectively. The Company did not sell any of its investments in marketable securities during the three-year period ended December 31, 2003.

Deferred Income Taxes—Deferred income taxes are provided for temporary differences between the amounts of assets and liabilities for financial and tax reporting purposes. Such temporary differences arise principally from the use of accelerated depreciation methods on rental merchandise for tax purposes.

Fair Value of Financial Instruments—The carrying amounts reflected in the consolidated balance sheets for cash, accounts receivable, bank and other debt approximate their respective fair values. The fair value of the liability for interest rate swap agreements, included in accounts payable and accrued expenses in the consolidated balance sheet, was approximately \$1,369,000 and \$3,321,000 at December 31, 2003 and 2002, respectively, based upon quotes from financial institutions. At December 31, 2003 and 2002, the carrying amount for variable rate debt approximates fair market value since the interest rates on these instruments are reset periodically to current market rates.

At December 31, 2003 and 2002, the fair market value of fixed rate long-term debt was approximately \$52,903,000 and \$50,000,000, respectively, based primarily on quoted prices for these or similar instruments. The fair value of fixed rate long-term debt was estimated by calculating the present value of anticipated cash flows. The discount rate used was an estimated borrowing rate for similar debt instruments with like maturities.

Revenue Recognition—Rental revenues are recognized as revenue in the month they are due. Rental payments received prior to the month due are recorded as deferred rental revenue. The Company maintains ownership of the rental merchandise until all payments are received under sales and lease ownership agreements. Revenues from the sale of residential and office furniture and other merchandise are recognized at the time of shipment, at which time title and risk of ownership are transferred to the customer. Please refer to Note J for discussion of recognition of franchise-related revenues.

Cost of Sales—Cost of sales includes the net book value of merchandise sold, primarily using specific identification in the sales and lease ownership division and first-in, first-out in the rent-to-rent division. It is not practicable to allocate operating expenses between selling and rental operations.

Shipping and Handling Costs—Shipping and handling costs are classified as operating expenses in the accompanying consolidated statements of earnings and totaled approximately \$24,907,000 in 2003, \$20,554,000 in 2002, and \$18,965,000 in 2001.

Advertising—The Company expenses advertising costs as incurred. Such costs aggregated approximately \$18,716,000 in 2003, \$15,406,000 in 2002, and \$14,204,000 in 2001.

Stock Based Compensation—The Company has elected to follow Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* and related Interpretations in accounting for its employee stock options and adopted the disclosure-only provisions of Statement of Financial Accounting Standards No. 123, *Accounting for Stock Based Compensation* (SFAS 123). The Company grants stock options for a fixed number of shares to employees with an exercise price equal to the fair value of the shares at the date of grant and, accordingly, recognizes no compensation expense for the stock option grants. Income tax benefits resulting from stock option exercises credited to additional

paid-in capital totaled approximately \$703,000, \$341,000, and \$288,000 in 2003, 2002, and 2001, respectively.

Closed Store Reserves—From time to time the Company closes underperforming stores. The charges related to the closing of these stores primarily consist of reserving the net present value of future minimum payments under the stores' real estate leases.

Insurance Reserves—Estimated insurance reserves are accrued primarily for group health and workers' compensation benefits provided to the Company's employees. Estimates for these insurance reserves are made based on actual reported but unpaid claims and actuarial analyses of the projected claims run off for both reported and incurred but not reported claims.

Derivative Instruments and Hedging Activities—From time to time, the Company uses interest rate swap agreements to synthetically manage the interest rate characteristics of a portion of its outstanding debt and to limit the Company's exposure to rising interest rates. The Company designates at inception that interest rate swap agreements hedge risks associated with future variable interest payments and monitors each swap agreement to determine if it remains an effective hedge. The effectiveness of the derivative as a hedge is based on a high correlation between changes in the value of the underlying hedged item and the derivative instrument. The Company records amounts to be received or paid as a result of interest rate swap agreements as an adjustment to interest expense. Generally, the Company's interest rate swaps are designated as cash flow hedges. In the event of early termination or redesignation of interest rate swap agreements, any resulting gain or loss would be deferred and amortized as an adjustment to interest expense of the related debt instrument over the remaining term of the original contract life of the agreement. In the event of early extinguishment of a designated debt obligation, any realized or unrealized gain or loss from the associated swap would be recognized in income or expense at the time of extinguishment. For the years ended December 31, 2003 and 2002, the Company's net income included an after-tax benefit of approximately \$170,000 and an after-tax expense of approximately \$156,000, respectively, related to swap ineffectiveness. The Company does not enter into derivatives for speculative or trading purposes.

Comprehensive Income—Comprehensive income totaled approximately \$38,294,000, \$27,526,000, and \$10,382,000 for the years ended December 31, 2003, 2002 and 2001, respectively.

New Accounting Pronouncements—Effective January 1, 2002, the Company adopted SFAS No. 141, *Business Combinations* (SFAS No. 141), and SFAS No. 142. SFAS No. 141 requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001. SFAS No. 142 requires that entities assess the fair value of the net assets underlying all acquisition-related goodwill on a reporting unit basis (see Note B).

In June 2002, the Financial Accounting Standards Board (FASB) issued SFAS No. 146, *Accounting for Costs Associated with Exit or Disposal Activities* (SFAS No. 146), which addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force Issue No. 94-3, *Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)*. SFAS No. 146 requires

that a liability for costs associated with an exit or disposal activity be recognized when the liability is incurred as opposed to the date of an entity's commitment to an exit plan. SFAS No. 146 also establishes fair value as the objective for initial measurement of the liability. SFAS No. 146 is effective for exit or disposal activities that are initiated after December 31, 2002. Adoption of SFAS No. 146 did not have a material effect on the Company's financial statements.

In November 2002, the FASB issued Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others* (FIN 45). FIN 45 requires an entity to disclose in its interim and annual financial statements information with respect to its obligations under certain guarantees that it has issued. It also requires an entity to recognize, at the inception of a guarantee, a liability for the fair value of the obligation undertaken in issuing the guarantee. The disclosure requirements of FIN 45 are effective for interim and annual periods ending after December 15, 2002. These disclosures are presented in Note G. The initial recognition and measurement requirements of FIN 45 are effective prospectively for guarantees issued or modified after December 31, 2002. The adoption of the recognition provisions of FIN 45 had no significant effect on the consolidated financial statements.

In January 2003, the FASB issued Interpretation No. 46, *Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51* (FIN 46). FIN 46 requires certain variable interest entities to be consolidated by the primary beneficiary of the entity if the equity investors in the entity do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 is effective immediately for all new variable interest entities created or acquired after January 31, 2003. The Company has not entered into transactions with, created, or acquired significant potential variable interest entities subsequent to that date. For interests in variable interest entities arising prior to February 1, 2003, the Company must apply the provisions of FIN 46 as of December 31, 2003. The Company has concluded that certain independent franchisees, as discussed in Note J, are not subject to the interpretation, and are therefore not included in the Company's consolidated financial statements. In addition, as discussed in Note E, the Company has certain capital leases with partnerships controlled by related parties of the Company. The Company has concluded that these partnerships are not variable interest entities. The Company has concluded that the accounting and reporting of its construction and lease facility (see Note G) are not subject to the provisions of FIN 46 since the lessor is not a variable interest entity, as defined by FIN 46.

In January 2003, the Emerging Issues Task Force (EITF) of the FASB issued EITF Issue No. 02-16, *Accounting by a Customer (Including a Reseller) for Certain Consideration Received from a Vendor* (EITF 02-16). EITF 02-16 addresses accounting and reporting issues related to how a reseller should account for cash consideration received from vendors. Generally, cash consideration received from vendors is presumed to be a reduction of the prices of the vendor's products or services and should, therefore, be characterized as a reduction of cost of sales when recognized in the customer's income statement. However, under certain circumstances this presumption may be overcome and

recognition as revenue or as a reduction of other costs in the income statement may be appropriate. The Company does receive cash consideration from vendors subject to the provisions of EITF 02-16. EITF 02-16 is effective for fiscal periods beginning after December 15, 2002. The Company adopted EITF 02-16 as of January 1, 2003. Such adoption did not have a material effect on the Company's financial statements since substantially all cooperative advertising consideration received from vendors represents a reimbursement of specific identifiable and incremental costs incurred in selling those vendors' products.

NOTE B: ACCOUNTING CHANGES

Effective January 1, 2002, the Company prospectively changed its method of depreciation for sales and lease ownership rental merchandise. Previously, all sales and lease ownership rental merchandise began being depreciated when received at the store over a period of the shorter of 36 months or the length of the rental periods, to a salvage value of zero. Due to changes in business, the Company changed the depreciation method such that sales and lease ownership rental merchandise received into a store begins being depreciated at the earlier of the expiration of 12 months from the date of acquisition or upon being subject to a sales and lease ownership agreement. Under the previous and the new depreciation method, rental merchandise in distribution centers does not begin being depreciated until 12 months from the date of acquisition. The Company believes the new depreciation method results in a better matching of the costs of rental merchandise with the corresponding revenue. The change in method of depreciation had the effect of increasing net income by approximately \$3,038,000, or approximately \$.09 diluted earnings per share, for the year ended December 31, 2002.

Effective January 1, 2002, the Company adopted SFAS No. 141 and SFAS No. 142. The Company concluded that the enterprise fair values of the Company's reporting units were greater than the carrying values, and accordingly no further impairment analysis was considered necessary.

Prior to the adoption of SFAS No. 142, the Company amortized goodwill over estimated useful lives up to a maximum of 20 years. Had the Company accounted for goodwill consistent with the provisions of SFAS No. 142 in the year ended December 31, 2001, the Company's income would have been affected as follows:

(In Thousands, Except Per Share)

Net Earnings, As Reported	\$12,336
Add Back: Goodwill Amortization, Net of Tax	688
Net Earnings, As Adjusted	<u>\$13,024</u>
Basic Earnings Per Common Share:	
As Reported	\$.41
Add Back: Goodwill Amortization	.02
As Adjusted	<u>\$.43</u>
Diluted Earnings Per Common Share:	
As Reported	\$.41
Add Back: Goodwill Amortization	.02
As Adjusted	<u>\$.43</u>

NOTE C: EARNINGS PER SHARE

Earnings per share is computed by dividing net income by the weighted average number of common shares outstanding during the year, which were 32,643,000 shares in 2003, 31,364,000 shares in 2002, and 29,892,000 shares in 2001. The computation of earnings per share assuming dilution includes the dilutive effect of stock options and awards. Such stock options and awards had the effect of increasing the weighted average shares outstanding assuming dilution by approximately 546,000 shares in 2003, 486,000 shares in 2002, and 321,000 shares in 2001.

NOTE D: PROPERTY, PLANT & EQUIPMENT

(In Thousands)	December 31, 2003	December 31, 2002
Land	\$ 10,370	\$ 9,077
Buildings & Improvements	39,772	32,943
Leasehold Improvements & Signs	54,348	44,587
Fixtures & Equipment	32,135	29,768
Assets Under Capital Lease:		
With Related Parties	10,308	10,308
With Unrelated Parties	1,432	1,432
Construction in Progress	3,647	4,318
	<u>\$152,012</u>	<u>\$132,433</u>
Less: Accumulated Depreciation & Amortization	<u>(52,428)</u>	<u>(45,339)</u>
	<u>\$ 99,584</u>	<u>\$ 87,094</u>

NOTE E: CREDIT FACILITIES

Following is a summary of the Company's credit facilities at December 31:

(In Thousands)	December 31, 2003	December 31, 2002
Bank Debt	\$13,870	\$ 7,325
Private Placement	50,000	50,000
Capital Lease Obligations:		
With Related Parties	10,144	10,308
With Unrelated Parties	1,319	1,432
Other Debt	4,237	4,200
	<u>\$79,570</u>	<u>\$73,265</u>

Bank Debt—The Company has a revolving credit agreement dated March 30, 2001 with several banks providing for unsecured borrowings up to \$86.7 million, which includes an \$8 million credit line to fund daily working capital requirements. Amounts borrowed bear interest at the lower of the lender's prime rate or LIBOR plus 1.00%. The pricing under the working capital line is based upon overnight bank borrowing rates. At December 31, 2003 and 2002, an aggregate of approximately \$13,870,000 (bearing interest at 2.24%) and \$7,325,000 (bearing interest at 2.65%) was outstanding under the revolving credit agreement, respectively. The Company pays a .25% commitment

fee on unused balances. The weighted average interest rate on borrowings under the revolving credit agreement (before giving effect to interest rate swaps) was 2.53% in 2003, 3.86% in 2002, and 5.77% in 2001. The revolving credit agreement expires May 31, 2004.

The revolving credit agreement contains certain covenants which require that the Company not permit its consolidated net worth as of the last day of any fiscal quarter to be less than the sum of (a) \$235,232,000 plus (b) 50% of the Company's consolidated net income (but not loss) for the period beginning July 1, 2002 and ending on the last day of such fiscal quarter. It also places other restrictions on additional borrowings and requires the maintenance of certain financial ratios. At December 31, 2003, \$59,472,000 of retained earnings was available for dividend payments and stock repurchases under the debt restrictions, and the Company was in compliance with all covenants.

Private Placement—On August 14, 2002 the Company sold \$50,000,000 in aggregate principal amount of senior unsecured notes (the Notes) in a private placement to a consortium of insurance companies. The Notes mature August 13, 2009. Quarterly interest-only payments at an annual rate of 6.88% are due for the first two years followed by annual \$10,000,000 principal repayments plus interest for the five years thereafter.

Capital Leases with Related Parties—In April 2002, the Company sold land and buildings with a carrying value of approximately \$6,258,000 to a limited liability corporation (LLC) controlled by the Company's major shareholder. Simultaneously, the Company and the LLC entered into a 15-year lease for the building and a portion of the land, with two five-year renewal options at the discretion of the Company. The LLC obtained borrowings collateralized by the land and building totaling approximately \$6,401,000. The Company occupies the land and building collateralizing the obligation associated with the lease. The transaction has been accounted for as a financing in the accompanying consolidated financial statements. The rate of interest implicit in the lease financing is approximately 8.7%. Accordingly, the land and building and the debt obligation are recorded in the Company's consolidated financial statements. No gain or loss was recognized associated with this transaction.

In December 2002, the Company sold 11 properties, including leasehold improvements, to a separate limited liability corporation (LLC) controlled by a group of Company executives and managers, including the Company's majority shareholder. The LLC obtained borrowings collateralized by the land totaling approximately \$5,000,000. The Company occupies the land and buildings collateralizing the obligations associated with the leases. The transaction has been accounted for as a financing in the accompanying consolidated financial statements. The rate of interest implicit in the leases is approximately 11.1%. Accordingly, the land and buildings and the lease obligations are recorded in the Company's consolidated financial statements. No gain or loss was recognized associated with this transaction.

Other Debt—Other debt at December 31, 2003 and 2002 includes \$4,200,000 of industrial development corporation revenue bonds. The average weighted borrowing rate on these bonds in 2003 was 1.58%. No principal payments are due on the bonds until maturity in 2015. At December 31, 2003, other debt also includes a note payable for approximately \$37,000 assumed by the Company in connection with a store acquisition.

Future maturities under the Company's Credit Facilities are as follows:

(In Thousands)	
2004	\$14,262
2005	10,429
2006	10,468
2007	10,561
2008	10,697
Thereafter	23,153

NOTE F: INCOME TAXES

(In Thousands)	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001
Current Income Tax Expense (Benefit):			
Federal	\$16,506	(\$11,431)	\$6,239
State	1,415	(1,911)	112
	<u>17,921</u>	<u>(13,342)</u>	<u>6,351</u>
Deferred Income Tax Expense:			
Federal	3,220	26,209	953
State	276	3,345	215
	<u>3,496</u>	<u>29,554</u>	<u>1,168</u>
	<u>\$21,417</u>	<u>\$16,212</u>	<u>\$7,519</u>

Significant components of the Company's deferred income tax liabilities and assets are as follows:

(In Thousands)	December 31, 2003	December 31, 2002
Deferred Tax Liabilities:		
Rental Merchandise and Property, Plant & Equipment	\$62,795	\$59,432
Other, Net	3,035	3,486
Total Deferred Tax Liabilities	<u>65,830</u>	<u>62,918</u>
Deferred Tax Assets:		
Accrued Liabilities	4,250	5,437
Advance Payments	5,770	5,371
Other, Net	520	1,593
Total Deferred Tax Assets	<u>10,540</u>	<u>12,401</u>
Net Deferred Tax Liabilities	<u>\$55,290</u>	<u>\$50,517</u>

The Company's effective tax rate differs from the statutory U.S. federal income tax rate as follows:

	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001
Statutory Rate	35.0%	35.0%	35.0%
Increases in U.S. Federal Taxes Resulting From:			
State Income Taxes, Net of Federal Income Tax Benefit	2.0	2.1	1.1
Other, Net			1.8
Effective Tax Rate	<u>37.0%</u>	<u>37.1%</u>	<u>37.9%</u>

NOTE G: COMMITMENTS

The Company leases warehouse and retail store space for substantially all of its operations under operating leases expiring at various times through 2017. The Company also leases certain properties under capital leases that are more fully described in Note E. Most of the leases contain renewal options for additional periods ranging from one to 15 years or provide for options to purchase the related property at predetermined purchase prices that do not represent bargain purchase options. In addition, certain properties occupied under operating leases contain normal purchase options. The Company also has a \$25,000,000 construction and lease facility. Properties acquired by the lessor are purchased or constructed and then leased to the Company under operating lease agreements. The total amount advanced and outstanding under this facility at December 31, 2003 was approximately \$24,881,000. Since the resulting leases are operating leases, no debt obligation is recorded on the Company's balance sheet. The Company also leases transportation equipment under operating leases expiring during the next three years. Management expects that most leases will be renewed or replaced by other leases in the normal course of business.

Future minimum rental payments required under operating leases that have initial or remaining noncancelable terms in excess of one year as of December 31, 2003, are as follows: \$40,329,000 in 2004; \$31,636,000 in 2005; \$22,263,000 in 2006; \$14,127,000 in 2007; \$7,592,000 in 2008; and \$8,147,000 thereafter. Certain operating leases expiring in 2006 contain residual value guarantee provisions and other guarantees in the event of a default. Although the likelihood of funding under these guarantees is considered by the Company to be remote, the maximum amount the Company may be liable for under such guarantees is approximately \$24,881,000.

Rental expense was \$44,145,000 in 2003, \$38,970,000 in 2002, and \$36,506,000 in 2001.

In addition to the related-party capital leases described in Note E, the Company leases one building from a partnership of which the Company's majority shareholder is a partner under a lease expiring in 2008 for annual rentals aggregating \$212,700.

The Company maintains a 401(k) savings plan for all full-time employees with at least one year of service with the Company and who meet certain eligibility requirements. The plan allows employees to contribute up to 10% of their annual compensation with 50% matching by the Company on the first 4% of compensation. The Company's expense related to the plan was \$512,000 in 2003, \$453,000 in 2002, and \$436,000 in 2001.

NOTE H: SHAREHOLDERS' EQUITY

During 2002 the Company purchased approximately 147,000 shares of the Company's Class A Common Stock at an aggregate cost of \$1,667,490. The Company also transferred 14,826 shares of the Company's Common Stock at an aggregate cost of approximately \$218,000 back into treasury, reflected net against reissued shares in the consolidated statement of shareholders' equity. The Company was authorized to purchase an additional 1,780,335 shares and held a total of 5,260,832 common shares in its treasury at December 31, 2003. The Company's articles of incorporation provide that no cash dividends may be paid on the Class A Common Stock unless equal or higher dividends are paid on the Common Stock.

The Company has 1,000,000 shares of preferred stock authorized. The shares are issuable in series with terms for each series fixed by the Board and such issuance is subject to approval by the Board of Directors. No preferred shares have been issued.

NOTE I: STOCK OPTIONS

The Company has stock option plans under which options to purchase shares of the Company's Common Stock are granted to certain key employees. Under the plans, options granted become exercisable after a period of three years, and unexercised options lapse 10 years after the date of the grant. Options are subject to forfeiture upon termination of service. Under the plans, approximately 132,000 of the Company's shares are reserved for future grants at December 31, 2003. The weighted average fair value of options granted was \$8.22 in 2003, \$6.56 in 2002 and \$6.45 in 2001.

Pro forma information regarding net earnings and earnings per share is required by FAS 123 and has been determined as if the Company had accounted for its employee stock options granted in 2003, 2002 and 2001 under the fair value method. The fair value for these options was estimated at the date of grant using a Black-Scholes option pricing model with the following weighted average assumptions for 2003, 2002, and 2001, respectively: risk-free interest rates of 3.41%, 5.78%, and 6.05%; a dividend yield

of .23%, .18%, and .24%; a volatility factor of the expected market price of the Company's Common Stock of .52, .46, and .45; and weighted average expected lives of the option of six, five, and eight years.

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options that have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

For purposes of pro forma disclosures under SFAS No. 123 as amended by Statement of Financial Accounting Standards No. 148, the estimated fair value of the options is amortized to expense over the options' vesting period. The following table illustrates the effect on net earnings and earnings per share if the fair-value-based method had been applied to all outstanding and unvested awards in each period:

(In Thousands, Except Per Share)	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001
Net Earnings As Reported	\$36,426	\$27,440	\$12,336
Deduct: Total Stock-based Employee Compensation Expense Determined Under Fair-Value-Based Method For All Awards, Net of Related Tax Effects	(1,345)	(1,165)	(1,262)
Pro Forma Net Earnings	\$35,081	\$26,275	\$11,074
Earnings Per Share:			
Basic—As Reported	\$ 1.12	\$.87	\$.41
Basic—Pro Forma	\$ 1.07	\$.84	\$.37
Diluted—As Reported	\$ 1.10	\$.86	\$.41
Diluted—Pro Forma	\$ 1.07	\$.83	\$.37

The following table summarizes information about stock options outstanding at December 31, 2003:

Range of Exercise Prices	Options Outstanding			Options Exercisable	
	Number Outstanding December 31, 2003	Weighted Average Remaining Contractual Life (in years)	Weighted Average Exercise Price	Number Exercisable December 31, 2003	Weighted Average Exercise Price
\$ 6.58–10.00	1,048,000	4.20	\$ 7.63	1,048,000	\$ 7.63
10.01–15.00	750,150	7.08	12.31	303,900	11.25
20.01–23.02	392,000	9.76	21.57		
\$ 6.58–23.02	2,190,150	6.18	\$11.73	1,351,900	\$ 8.45

The table below summarizes option activity for the periods indicated in the Company's stock option plans:

	Options (In Thousands)	Weighted Average Exercise Price
Outstanding at December 31, 2000	2,066	\$ 8.68
Granted	200	10.87
Exercised	(165)	7.18
Forfeited	(149)	10.96
Outstanding at December 31, 2001	1,952	8.86
Granted	307	13.91
Exercised	(147)	9.18
Forfeited	(105)	11.56
Outstanding at December 31, 2002	2,007	9.47
Granted	492	19.93
Exercised	(214)	9.27
Forfeited	(95)	12.12
Outstanding at December 31, 2003	2,190	\$11.73
Exercisable at December 31, 2003	1,352	\$ 8.45

NOTE J: FRANCHISING OF AARON'S SALES & LEASE OWNERSHIP STORES

The Company franchises Aaron's Sales & Lease Ownership stores. As of December 31, 2003 and 2002, 528 and 445 franchises had been awarded, respectively. Franchisees pay a nonrefundable initial franchise fee of \$35,000 and an ongoing royalty of 5% to 6% of gross revenues. Franchise fees and area development fees are generated from the sale of rights to develop, own and operate Aaron's Sales & Lease Ownership stores. These fees are recognized as income when substantially all of the Company's obligations per location are satisfied, generally at the date of the store opening. Franchise fees and area development fees received prior to the substantial completion of the Company's obligations are deferred. The Company includes this income in Other Revenues in the Consolidated Statement of Earnings. Substantially all of the amounts reported as Non-Retail Sales and Non-Retail Cost of Sales in the accompanying Consolidated Statements of Earnings relate to the sale of rental merchandise to franchisees.

Initial franchise fee revenue approximated \$2,171,000, \$1,631,000 and \$1,580,000 and royalty revenues approximated \$13,999,000, \$12,317,000 and \$9,932,000 for the years ended December 31, 2003, 2002 and 2001, respectively.

The Company has guaranteed certain debt obligations of some of the franchisees amounting to approximately \$67,455,000 at December 31, 2003. The Company receives guarantee fees based on such franchisees' outstanding debt obligations, which it recognizes as the guarantee obligation is satisfied. The Company has recourse rights to the assets securing the debt obligations. As a result, the Company does not expect to incur any significant losses under these guarantees.

Franchised Sales and Lease Ownership store activity is summarized as follows:

	2003	2002	2001
Franchise Stores Open at January 1	232	209	193
Opened	82	31	30
Purchased by the Company	(26)	(5)	(13)
Closed or Liquidated	(1)	(3)	(1)
Franchise Stores Open at December 31	287	232	209

Company-operated Sales and Lease Ownership store activity is summarized as follows:

	2003	2002	2001
Company-Operated Stores Open at January 1	412	364	263
Opened	38	27	100
Added Through Acquisition	59	30	14
Merged or Closed	(9)	(9)	(13)
Company-Operated Stores Open at December 31	500	412	364

In 2003 the Company acquired the rental contracts, merchandise, and other related assets of 98 stores, including 26 franchise stores. Many of these stores and/or their accompanying assets were merged into other stores resulting in a net gain of 59 stores. The 2002 and 2001 acquisitions were all primarily additional new store locations.

NOTE K: ACQUISITIONS AND DISPOSITIONS

During 2003, the Company acquired 98 sales and lease ownership stores with an aggregate purchase price of \$45,041,000. Fair value of acquired tangible assets included approximately \$16,116,000 for rental merchandise, \$999,000 for fixed assets, and \$53,000 for other assets. Fair value of liabilities assumed approximated \$1,271,000. The excess cost over the net fair market value of tangible assets acquired, representing goodwill and customer lists, was \$26,400,000 and \$2,744,000 respectively. The estimated amortization of these customer lists in future years approximates \$1,390,000 for 2004 and \$849,000 for 2005. Also, in 2003 the Company acquired one rent-to-rent store. The purchase price of the 2003 rent-to-rent acquisition was not significant.

During 2002, the Company acquired 10 sales and lease ownership stores and 25 credit retail stores with an aggregate purchase price of approximately \$14,033,000. The excess cost over the fair market value of tangible and identifiable intangible assets acquired, representing goodwill, was approximately \$3,889,000.

In 2001, the Company acquired 23 sales and lease ownership stores including 13 stores purchased from franchisees. The aggregate purchase price of these 2001 acquisitions was \$10,423,000 and the excess cost over the fair market value of tangible assets acquired was approximately \$4,553,000. Also in 2001, the Company acquired two rent-to-rent stores. The aggregate purchase price of these 2001 rent-to-rent acquisitions was not significant.

These acquisitions were accounted for under the purchase method and, accordingly, the results of operations of the acquired businesses are included in the Company's results of operations from their dates of acquisition. The effect of these acquisitions on the 2003, 2002 and 2001 consolidated financial statements was not significant.

In 2003, the Company sold three of its sales and lease ownership locations to an existing franchisee and sold one

of its rent-to-rent stores. In 2002, the Company sold four of its sales and lease ownership stores to an existing franchisee. In 2001, the Company sold three of its sales and lease ownership stores to existing franchisees and sold five of its rent-to-rent stores. The effect of these sales on the consolidated financial statements was not significant.

NOTE L: SEGMENTS

Description of Products and Services of Reportable Segments

Aaron Rents, Inc. has four reportable segments: sales and lease ownership, rent-to-rent, franchise, and manufacturing. The sales and lease ownership division offers electronics, residential furniture, appliances, and computers to consumers primarily on a monthly payment basis with no credit requirements. The rent-to-rent division rents and sells residential and office furniture to businesses and consumers who meet certain minimum credit requirements. The Company's franchise operation sells and supports franchises of its sales and lease ownership concept. The manufacturing division manufactures upholstered furniture, office furniture, lamps and accessories, and bedding predominantly for use by the other divisions.

Earnings before income taxes for each reportable segment are generally determined in accordance with accounting principles generally accepted in the United States with the following adjustments:

- A predetermined amount of each reportable segment's revenues is charged to the reportable segment as an allocation of corporate overhead. This allocation was approximately 2.3% in 2003 and 2.2% in 2002 and 2001.
- Accruals related to store closures are not recorded on the reportable segments' financial statements, but are rather maintained and controlled by corporate headquarters.
- The capitalization and amortization of manufacturing variances are recorded on the consolidated financial statements as part of Cash to Accrual and Other Adjustments and are not allocated to the segment that holds the related rental merchandise.
- Interest on borrowings is estimated at the beginning of each year. Interest is then allocated to operating segments on the basis of relative total assets.
- Sales and lease ownership revenues are reported on the cash basis for management reporting purposes.

Revenues in the "Other" category are primarily from leasing space to unrelated third parties in our corporate headquarters building and revenues from several minor unrelated activities. The pretax losses in the "Other" category are the net result of the activity mentioned above, net of the portion of corporate overhead not allocated to the reportable segments.

Measurement of Segment Profit or Loss and Segment Assets

The Company evaluates performance and allocates resources based on revenue growth and pretax profit or loss from operations. The accounting policies of the reportable segments are the same as those described in the summary of significant accounting policies except that the sales and lease ownership division revenues and certain other items are presented on a cash basis. Intersegment sales are completed at internally negotiated amounts ensuring competitiveness with outside vendors. Since the intersegment profit and loss affect inventory valuation, depreciation and cost of goods sold are adjusted when intersegment profit is eliminated in consolidation.

Factors Used by Management to Identify the Reportable Segments

The Company's reportable segments are business units that service different customer profiles using distinct payment arrangements. The reportable segments are each managed separately because of differences in both customer base and infrastructure.

Information on segments and a reconciliation to earnings before income taxes are as follows:

(In Thousands)	Year Ended December 31, 2003	Year Ended December 31, 2002	Year Ended December 31, 2001
Revenues From			
External Customers:			
Sales & Lease Ownership	\$634,489	\$501,390	\$380,404
Rent-to-Rent	109,083	119,885	150,002
Franchise	19,347	16,663	13,913
Other	4,206	4,746	4,243
Manufacturing	60,608	56,002	47,035
Elimination of			
Intersegment Revenues	(60,995)	(56,141)	(47,801)
Cash to Accrual Adjustments	59	(1,857)	(1,115)
Total Revenues From			
External Customers	<u>\$766,797</u>	<u>\$640,688</u>	<u>\$546,681</u>
Earnings Before Income Taxes:			
Sales & Lease Ownership	\$ 43,325	\$ 31,220	\$ 11,314
Rent-to-Rent	6,341	9,057	9,152
Franchise	13,600	10,919	9,212
Other	(2,356)	(5,544)	(3,244)
Manufacturing	1,222	989	(587)
Earnings Before Income			
Taxes For Reportable			
Segments	62,132	46,641	25,847
Elimination of Intersegment			
Profit	(2,338)	(760)	(1,449)
Cash to Accrual and			
Other Adjustments	(1,951)	(2,229)	(4,543)
Total Earnings Before			
Income Taxes	<u>\$ 57,843</u>	<u>\$ 43,652</u>	<u>\$ 19,855</u>
Assets:			
Sales & Lease Ownership	\$408,244	\$327,845	\$241,245
Rent-to-Rent	79,984	89,133	107,882
Franchise	19,493	12,627	13,991
Other	29,244	35,488	17,533
Manufacturing	18,327	18,555	16,545
Total Assets	<u>\$555,292</u>	<u>\$483,648</u>	<u>\$397,196</u>
Depreciation & Amortization:			
Sales & Lease Ownership	\$191,777	\$154,310	\$121,953
Rent-to-Rent	21,266	22,901	29,736
Franchise	547	486	444
Other	839	541	690
Manufacturing	968	802	725
Total Depreciation			
& Amortization	<u>\$215,397</u>	<u>\$179,040</u>	<u>\$153,548</u>
Interest Expense:			
Sales & Lease Ownership	\$ 5,215	\$ 4,768	\$ 4,620
Rent-to-Rent	1,583	2,493	3,010
Franchise	93	83	119
Other	(1,109)	(2,577)	(1,491)
Total Interest Expense	<u>\$ 5,782</u>	<u>\$ 4,767</u>	<u>\$ 6,258</u>

NOTE M: QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

(In Thousands, Except Per Share)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
YEAR ENDED DECEMBER 31, 2003				
Revenues	\$191,260	\$177,741	\$188,406	\$209,390
Gross Profit*	92,986	90,912	97,475	103,253
Earnings Before Taxes	13,907	13,906	13,733	16,297
Net Earnings	8,748	8,761	8,651	10,266
Earnings Per Share	.27	.27	.26	.31
Earnings Per Share Assuming Dilution	.27	.26	.26	.31
YEAR ENDED DECEMBER 31, 2002				
Revenues	\$156,663	\$151,162	\$157,838	\$175,025
Gross Profit*	79,074	78,822	79,948	84,079
Earnings Before Taxes	9,457	10,666	10,669	12,860
Net Earnings	5,921	6,696	6,721	8,102
Earnings Per Share	.20	.22	.21	.25
Earnings Per Share Assuming Dilution	.20	.21	.20	.25

* Gross profit is the sum of rentals and fees, retail sales, and non-retail sales less retail cost of sales, non-retail cost of sales, and depreciation of rental merchandise.

REPORT OF INDEPENDENT AUDITORS

To the Board of Directors and Shareholders of Aaron Rents, Inc.:

We have audited the accompanying consolidated balance sheets of Aaron Rents, Inc. and Subsidiaries as of December 31, 2003 and December 31, 2002, and the related consolidated statements of earnings, shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2003. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Aaron Rents, Inc. and Subsidiaries as of December 31, 2003 and 2002, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States.

As discussed in Note B, on January 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*, and changed its method of depreciating sales and lease ownership rental merchandise.

Ernst & Young LLP

Atlanta, Georgia
February 24, 2004

COMMON STOCK MARKET PRICES & DIVIDENDS

The following table shows, for the periods indicated, the range of high and low prices per share for the Common Stock and Class A Common Stock and the cash dividends declared per share.

The Company's Common Stock and Class A Common Stock are listed on the New York Stock Exchange under the symbols "RNT" and "RNT.A," respectively.

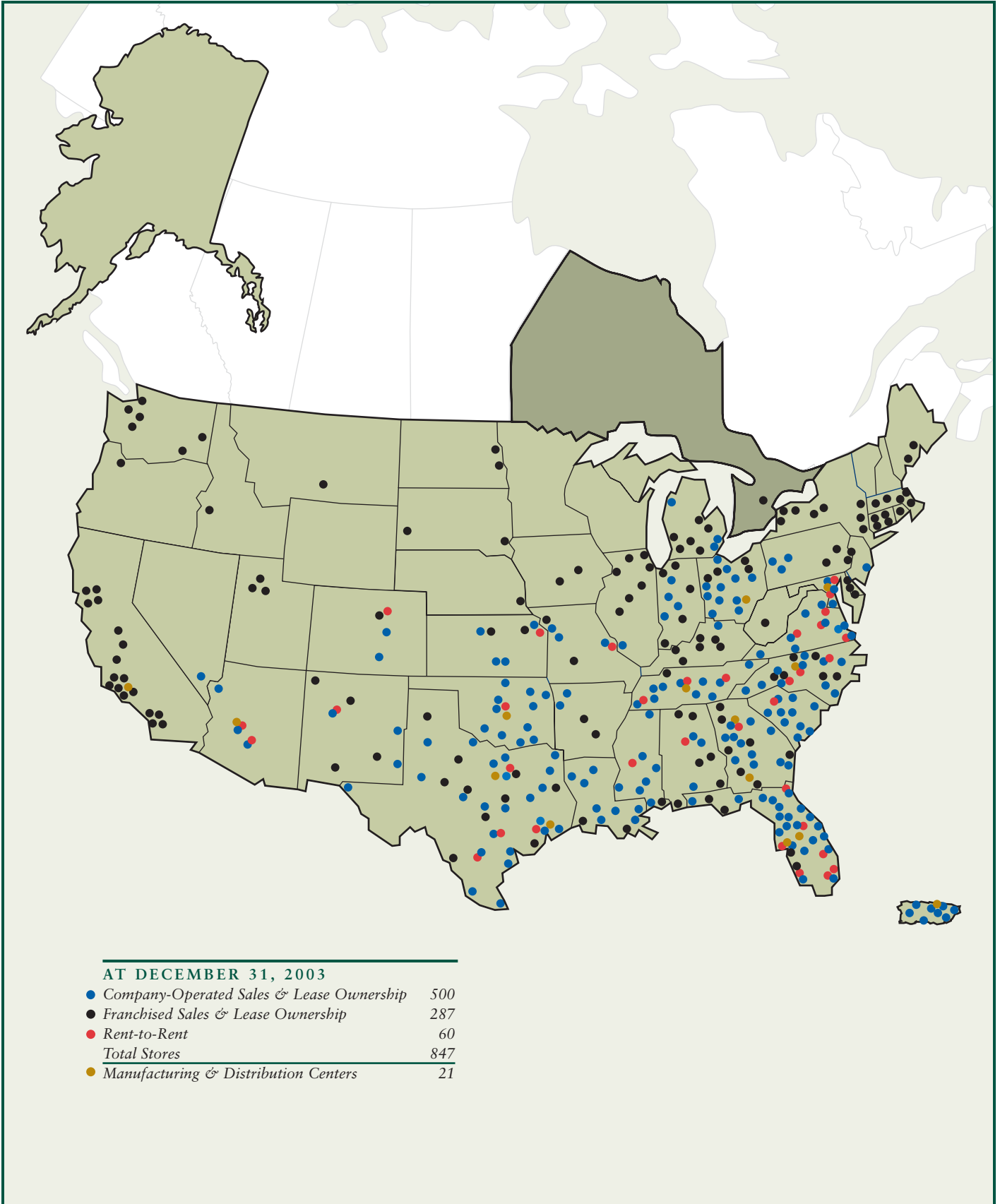
The approximate number of shareholders of the Company's Common Stock and Class A Common Stock at March 5, 2004 was 2,600. The closing prices for the Common Stock and Class A Common Stock at March 5, 2004 were \$24.79 and \$22.25, respectively.

Subject to our continuing to earn sufficient income, to any future capital needs and to other contingencies, we currently expect to continue our policy of paying dividends. Our articles of incorporation provide that no cash dividends may be paid on our Class A Common Stock unless equal or higher dividends are paid on the Common Stock. Under our revolving credit agreement, we may pay cash dividends in any fiscal year only if the dividends do not exceed 50% of our consolidated net earnings for the prior fiscal year plus the excess, if any, of the cash dividend limitation applicable to the prior year over the dividend actually paid in the prior year.

Common Stock	High	Low	Cash Dividends Per Share
DECEMBER 31, 2003			
First Quarter	\$14.72	\$11.37	
Second Quarter	17.72	13.53	\$.013
Third Quarter	23.10	17.01	
Fourth Quarter	23.63	20.13	.020
DECEMBER 31, 2002			
First Quarter	\$15.43	\$ 9.63	
Second Quarter	18.99	13.43	\$.013
Third Quarter	15.73	12.33	
Fourth Quarter	15.47	13.40	.013

Class A Common Stock	High	Low	Cash Dividends Per Share
DECEMBER 31, 2003			
First Quarter	\$15.17	\$12.53	
Second Quarter	17.30	13.47	\$.013
Third Quarter	21.67	16.00	
Fourth Quarter	21.20	18.49	.020
DECEMBER 31, 2002			
First Quarter	\$14.83	\$ 7.00	
Second Quarter	18.33	14.27	\$.013
Third Quarter	16.40	13.73	
Fourth Quarter	15.83	14.10	.013

STORE LOCATIONS IN THE UNITED STATES, PUERTO RICO,
AND CANADA



BOARD OF DIRECTORS

R. Charles Loudermilk, Sr.
Chairman of the Board,
Chief Executive Officer,
Aaron Rents, Inc.

Ronald W. Allen⁽¹⁾
Retired Chairman, President
and Chief Executive Officer
of Delta Air Lines

Leo Benatar⁽²⁾
Principal, Benatar &
Associates

William K. Butler, Jr.
President, Aaron's Sales &
Lease Ownership Division

Gilbert L. Danielson
Executive Vice President,
Chief Financial Officer,
Aaron Rents, Inc.

Earl Dolive⁽¹⁾
Vice Chairman of the Board,
Emeritus, Genuine Parts
Company

Ingrid Saunders Jones⁽²⁾
Senior Vice President,
Corporate External Affairs,
The Coca-Cola Company

David L. Kolb⁽¹⁾
Chairman of the Board,
Mohawk Industries, Inc.

Robert C. Loudermilk, Jr.
President, Chief Operating
Officer, Aaron Rents, Inc.

Ray M. Robinson
President, East Lake Golf
Club and Vice Chairman,
East Lake Community
Foundation

⁽¹⁾ Member of Audit Committee

⁽²⁾ Member of Stock Option
Committee

OFFICERS

R. Charles Loudermilk, Sr.
Chairman of the Board,
Chief Executive Officer,
Aaron Rents, Inc.

Robert C. Loudermilk, Jr.
President, Chief Operating
Officer, Aaron Rents, Inc.

Gilbert L. Danielson
Executive Vice President,
Chief Financial Officer,
Aaron Rents, Inc.

William K. Butler, Jr.
President, Aaron's Sales &
Lease Ownership Division

Eduardo Quiñones
President, Aaron Rents'
Rent-to-Rent Division

James L. Cates
Senior Group Vice President
and Corporate Secretary,
Aaron Rents, Inc.

David A. Boggan
Vice President, Marketing
and Merchandising, Aaron's
Sales & Lease Ownership
Division

K. Todd Evans
Vice President, Franchising,
Aaron's Sales & Lease
Ownership Division

B. Lee Landers, Jr.
Vice President, Chief
Information Officer,
Aaron Rents, Inc.

Mitchell S. Paull
Senior Vice President,
Aaron Rents, Inc.

David M. Rhodus
Vice President, General
Counsel, Aaron Rents, Inc.

Marc S. Rogovin
Vice President, Real Estate
and Construction, Aaron
Rents, Inc.

Robert P. Sinclair, Jr.
Vice President, Corporate
Controller, Aaron Rents, Inc.

Ronald Benedict
Vice President, Office
Division, Aaron Rents'
Rent-to-Rent Division

David L. Buck
Vice President, Western
Operations, Aaron's Sales &
Lease Ownership Division

Christopher D. Counts
Vice President, Western
Residential Region, Aaron
Rents' Rent-to-Rent Division

Joseph N. Fedorchak
Vice President, Eastern
Operations, Aaron's Sales &
Lease Ownership Division

Bert L. Hanson
Vice President, Mid-
American Operations,
Aaron's Sales & Lease
Ownership Division

Michael B. Hickey
Vice President, Management
Development, Aaron's Sales
& Lease Ownership Division

James C. Johnson
Vice President, Internal
Audit, Aaron Rents, Inc.

Phil J. Karl
Vice President, Southeast
Residential Region, Aaron
Rents' Rent-to-Rent Division

Donald P. Lange
Vice President, Marketing
and Advertising, Aaron
Rents' Rent-to-Rent Division

Tristan J. Montanero
Vice President, Central
Operations, Aaron's Sales
& Lease Ownership Division

Michael P. Ryan
Vice President, Northern
Operations, Aaron's Sales
& Lease Ownership Division

Danny Walker, Sr.
Vice President, Internal
Security, Aaron Rents, Inc.

CORPORATE AND SHAREHOLDER INFORMATION

Corporate Headquarters
309 E. Paces Ferry Rd., N.E.
Atlanta, Georgia 30305-2377
(404) 231-0011
<http://www.aaronrents.com>

Subsidiaries
Aaron Investment Company
4005 Kennett Pike
Greenville, Delaware 19807
(302) 888-2351

Aaron Rents, Inc. Puerto Rico
Avenue Barbosa #376
Hato Rey, Puerto Rico 00917
(787) 764-0420

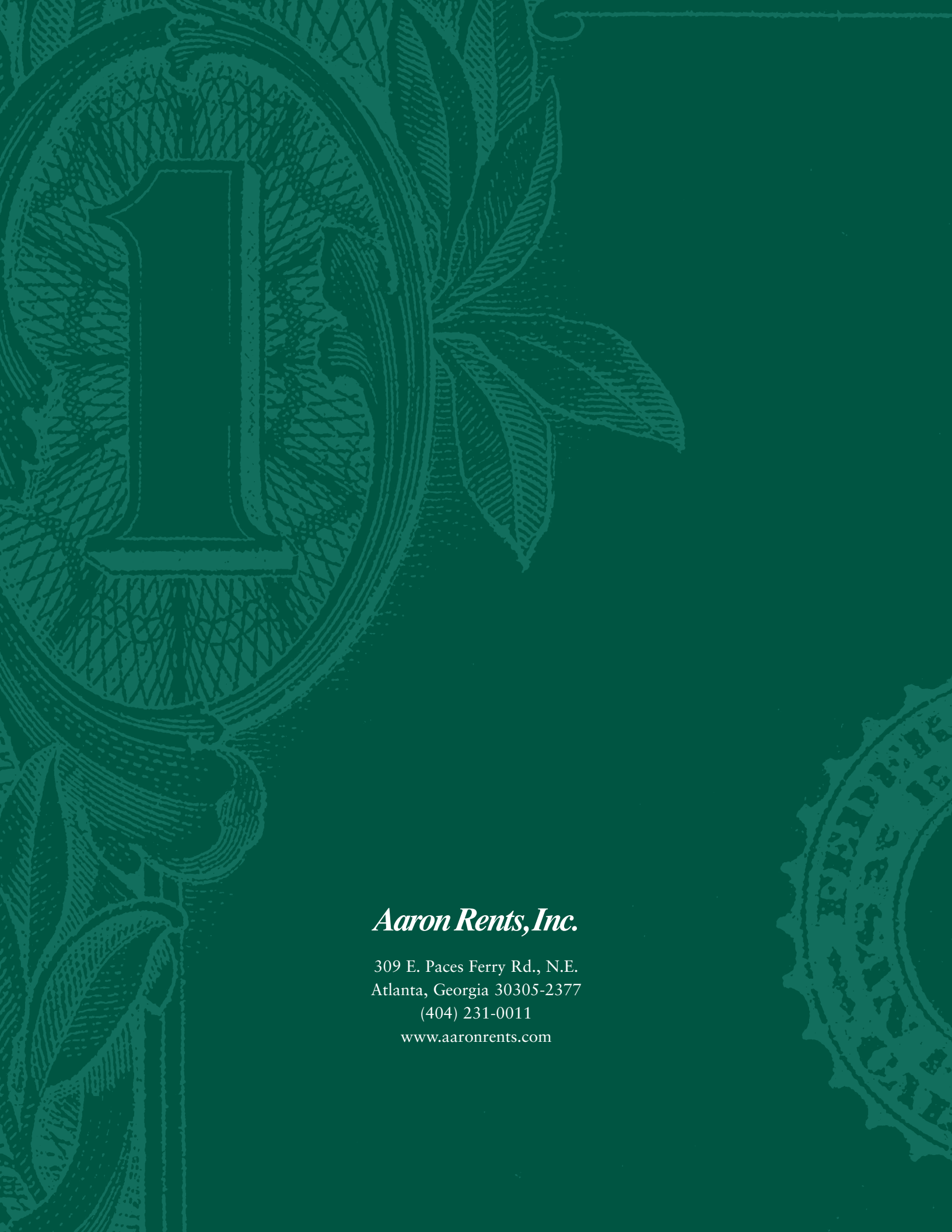
Annual Shareholders Meeting
The annual meeting of the
shareholders of Aaron Rents,
Inc. will be held on Tuesday,
April 27, 2004 at 10:00 a.m.
E.D.T. on the 4th Floor,
SunTrust Plaza,
303 Peachtree Street,
Atlanta, Georgia 30303.

Form 10-K
Shareholders may obtain
a copy of the Company's
annual report on Form 10-K
filed with the Securities and
Exchange Commission upon
written request, without
charge. Such requests should
be sent to the attention of
Gilbert L. Danielson,
Executive Vice President,
Chief Financial Officer,
Aaron Rents, Inc., 309 E.
Paces Ferry Rd., N.E.,
Atlanta, Georgia 30305-
2377.

Stock Listing
RNT Aaron Rents,
Inc.'s Common
Listed Stock and Class
NYSE A Common
Stock are traded
on the New York
Stock Exchange under the
symbols "RNT" and
"RNT.A," respectively.

Transfer Agent and Registrar
SunTrust Bank, Atlanta
Atlanta, Georgia

General Counsel
Kilpatrick Stockton LLP
Atlanta, Georgia



Aaron Rents, Inc.

309 E. Paces Ferry Rd., N.E.
Atlanta, Georgia 30305-2377

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