FRIENDLY ICE CREAM CORP
Form 10-Q
October 24, 2001

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2001
OR

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

FOR THE TRANSITION PERIOD FROM ______________ TO ______________

COMMISSION FILE NO. 0-3930

FRIENDLY ICE CREAM CORPORATION

(Exact name of registrant as specified in its charter)

MASSACHUSETTS	5812	04-2053130
(State of Incorporation)	(Primary Standard Industrial Classification Code Number)	(I.R.S. Employer Identification No.)

1855 BOSTON ROAD
WILBRAHAM, MASSACHUSETTS 01095
(413) 543-2400

(Address, including zip code, and telephone number, including area code, of registrant's principal executive offices)

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

CLASS	OUTSTANDING AT OCTOBER 19, 2001
Common Stock, $.01 par value	7,352,710 shares

PART I--FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED BALANCE SHEETS

(IN THOUSANDS)

	SEPTEMBER 30, 2001 (UNAUDITED)	DECEMBER 31, 2000
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 7,557	$ 14,584
Restricted cash	--	1,737
Accounts receivable, net	8,494	6,157
Inventories	15,394	11,570
Deferred income taxes	10,395	10,395
Prepaid expenses and other current assets	3,352	2,799
TOTAL CURRENT ASSETS	45,192	47,242
PROPERTY AND EQUIPMENT, net	194,219	226,865
INTANGIBLES AND DEFERRED COSTS, net	19,783	21,529
OTHER ASSETS	10,261	2,050
TOTAL ASSETS	$ 269,455	$ 297,686
LIABILITIES AND STOCKHOLDERS' DEFICIT		
CURRENT LIABILITIES:		
Current maturities of long-term debt	$ 3,990	$ 13,029
Current maturities of capital lease and finance obligations	1,885	2,143
Accounts payable	21,622	20,100
Accrued salaries and benefits	10,242	10,956
Accrued interest payable	7,103	3,515
Insurance reserves	13,764	13,095
Restructuring reserve	3,658	5,571

Other accrued expenses..................................	14,121	14,262
TOTAL CURRENT LIABILITIES.................................	76,385	82,671
DEFERRED INCOME TAXES.....................................	15,668	13,276
CAPITAL LEASE AND FINANCE OBLIGATIONS, less current maturities..	6,722	8,223
LONG-TERM DEBT, less current maturities....................	251,350	275,435
OTHER LONG-TERM LIABILITIES................................	14,905	18,064
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' DEFICIT:		
Common stock..	74	74
Additional paid-in capital..............................	139,223	138,988
Accumulated deficit.....................................	(234,872)	(239,045)
TOTAL STOCKHOLDERS' DEFICIT................................	(95,575)	(99,983)
TOTAL LIABILITIES AND STOCKHOLDERS' DEFICIT................	$ 269,455	$ 297,686

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

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(UNAUDITED)
(IN THOUSANDS, EXCEPT PER SHARE DATA)

	FOR THE THREE MONTHS ENDED		FOR THE NINE MONTHS EN	
	SEPTEMBER 30, 2001	OCTOBER 1, 2000	SEPTEMBER 30, 2001	OCTOBER 2000
REVENUES................................	$152,015	$161,841	$430,295	$465,2
COSTS AND EXPENSES:				
Cost of sales.........................	54,840	54,081	149,757	149,1
Labor and benefits....................	39,674	47,822	120,684	145,3
Operating expenses....................	31,930	32,611	89,690	94,5
General and administrative expenses....	8,393	8,857	27,070	30,4
Restructuring costs...................	--	--	--	12,0
Write-downs of property and equipment..........................	35	664	103	19,0
Depreciation and amortization..........	7,037	7,426	21,686	23,1
(Gain) loss on franchise sales of restaurant operations and properties...	(219)	75	(4,042)	(1,9
Gain on disposition of other property and equipment............................	(317)	(960)	(2,559)	(1,0
OPERATING INCOME (LOSS)..................	10,642	11,265	27,906	(5,5

Interest expense, net	6,464	7,594	20,967	23,4
INCOME (LOSS) BEFORE (PROVISION FOR) BENEFIT FROM INCOME TAXES AND EXTRAORDINARY ITEM	4,178	3,671	6,939	(29,0
(Provision for) benefit from income taxes	(1,613)	(425)	(2,545)	16,7
INCOME (LOSS) BEFORE EXTRAORDINARY ITEM	2,565	3,246	4,394	(12,2
Extraordinary item, net of income tax benefit of $153	(221)	--	(221)	
NET INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS)	$ 2,344	$ 3,246	$ 4,173	$(12,2
BASIC NET INCOME (LOSS) PER SHARE:				
Income (loss) before extraordinary item	$ 0.35	$ 0.44	$ 0.60	$ (1.
Extraordinary item, net of income tax benefit	(0.03)	--	(0.03)	
Net income (loss)	$ 0.32	$ 0.44	$ 0.57	$ (1.
DILUTED NET INCOME (LOSS) PER SHARE:				
Income (loss) before extraordinary item	$ 0.35	$ 0.44	$ 0.60	$ (1.
Extraordinary item, net of income tax benefit	(0.03)	--	(0.03)	
Net income (loss)	$ 0.32	$ 0.44	$ 0.57	$ (1.
WEIGHTED AVERAGE SHARES:				
Basic	7,359	7,409	7,366	7,4
Diluted	7,416	7,437	7,382	7,4

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

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(UNAUDITED)
(IN THOUSANDS)

	FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001	FOR THE NINE MONTHS ENDED OCTOBER 1, 2000
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	$ 4,173	$ (12,259)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Extraordinary item, net of income tax benefit	221	--
Stock compensation expense	235	429
Depreciation and amortization	21,686	23,166
Write-downs of property and equipment	103	19,024
Deferred income tax expense (benefit)	2,545	(16,790)
Gain on asset retirements and sales	(6,710)	(3,562)
Changes in operating assets and liabilities:		
Accounts receivable	(2,337)	(1,940)
Inventories	(3,824)	(2,178)
Other assets	(3,204)	2,608
Accounts payable	1,522	579
Accrued expenses and other long-term liabilities	(1,840)	(2,883)
NET CASH PROVIDED BY OPERATING ACTIVITIES	12,570	6,194
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(8,440)	(12,808)
Proceeds from sales of property and equipment	23,556	32,594
NET CASH PROVIDED BY INVESTING ACTIVITIES	15,116	19,786
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from borrowings	51,405	74,000
Repayments of debt	(84,529)	(101,678)
Repayments of capital lease and finance obligations	(1,589)	(1,344)
NET CASH USED IN FINANCING ACTIVITIES	(34,713)	(29,022)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(7,027)	(3,042)
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	14,584	12,062
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 7,557	$ 9,020
SUPPLEMENTAL DISCLOSURES:		
Cash paid during the period for:		
Interest	$ 16,699	$ 18,101
Income taxes	3	62
Capital lease obligations incurred	--	2,891
Capital lease obligations terminated	170	711
Notes received from sales of property and equipment	4,250	577

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

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(UNAUDITED)

1. BASIS OF PRESENTATION

INTERIM FINANCIAL INFORMATION--

The accompanying condensed consolidated financial statements as of September 30, 2001 and for the third quarter and nine months ended September 30, 2001 and October 1, 2000 are unaudited, but, in the opinion of management, include all adjustments which are necessary for a fair presentation of the consolidated financial position, results of operations, cash flows and comprehensive income (loss) of Friendly Ice Cream Corporation ("FICC") and subsidiaries (unless the context indicates otherwise, collectively, the "Company"). Such adjustments consist solely of normal recurring accruals. Operating results for the three and nine month periods ended September 30, 2001 and October 1, 2000 are not necessarily indicative of the results that may be expected for the entire year due, in part, to the seasonality of the Company's business. Historically, higher revenues and operating income have been experienced during the second and third fiscal quarters. The Company's Consolidated Financial Statements, including the notes thereto, which are contained in the 2000 Annual Report on Form 10-K should be read in conjunction with these Condensed Consolidated Financial Statements.

REFINANCING STATUS AND DEBT--

The Company entered into its existing credit facility in November 1997. The credit facility includes the revolving credit loan, term loans and letters of credit. Since 1997, the Company has executed several amendments to the credit facility. The most recent amendment occurred on March 19, 2001. All of the existing financial covenants were amended and a new financial covenant was added requiring minimum cumulative Consolidated EBITDA, as defined, on a monthly basis. Interest rates on term loans, borrowings under the revolving credit facility and issued letters of credit increased 0.25%. In addition, automatic increases in the interest rates will occur on August 2, 2001, January 2, 2002, April 1, 2002, September 30, 2002 and October 1, 2002 of 0.25%, 0.50%, 0.25%, 0.25% and 0.25%, respectively. Interest payments on all ABR loans, Eurodollar loans and issued letters of credit are required on a monthly basis rather than quarterly.

Also due to the March 19, 2001 amendment, the maturity dates of Tranche B and Tranche C of the term loans were changed to November 15, 2002 from their original maturity dates of November 15, 2004 and November 15, 2005, respectively. Annual scheduled principal payments due through October 15, 2002 did not change. However, the amendment requires additional minimum cumulative prepayments on the term loans, excluding prepayments made pursuant to the J&B Agreement, by the dates specified below as follows:

October 15, 2001	$6,000,000
January 15, 2002	7,500,000
April 15, 2002	8,500,000
July 15, 2002	10,000,000

As of October 15, 2001, the Company has paid additional minimum cumulative prepayments of $6,793,000 on the term loans, which exceed the minimum cumulative prepayment requirement.

Tranche A of the term loans was prepaid and extinguished during the third quarter ended September 30, 2001. Any remaining unpaid balances due on Tranches B and C of the term loans will be paid on November 15, 2002.

1. BASIS OF PRESENTATION (CONTINUED)

FICC paid an amendment fee of approximately $256,000 to the lenders contemporaneous with the execution of the seventh amendment. FICC paid an additional amendment fee (the "Additional Fee") of $441,459 on October 1, 2001 pursuant to the seventh amendment, which will be expensed over the remaining term of the credit facility using the effective yield method. If all obligations under the credit facility were satisfied before September 30, 2001, the Additional Fee would have been reduced to approximately $128,000. The Company believes that based on the terms of the seventh amendment, the Company has adequate cash and availability on its revolving credit facility to meet its obligations through September 30, 2002. Additionally, the Company believes that it can comply with the revised covenant requirements under the amendment through December 30, 2001.

The Company is undertaking a refinancing plan (collectively, the "Refinancing Plan"), which has the following three principal components:

(i) obtaining a new revolving credit facility from one or more financial institutions for $35 million;

(ii) obtaining $55 million in loans from GE Capital Franchise Finance Corporation which will be secured by first mortgage liens upon 75 of the Company's restaurants; and

(iii) entering into a sale and leaseback arrangement with one or more financial institutions involving 45 of the Company's restaurants that is expected to provide the Company up to $37.5 million in cash.

The Company would use the proceeds of these financings to repay the amounts outstanding on its existing credit facility ($55,114,000 as of September 30, 2001), to increase working capital and, to the extent the proceeds of the financings are sufficient, after giving effect to the foregoing, to finance a tender offer for a portion of the Company's senior notes (the "Notes"). The Company has obtained a commitment letter from GE Capital Franchise Finance Corporation relating to the mortgage financing, but the Company does not have any commitments or other agreements from any financial institutions relating to the new revolving credit facility or the sale and leaseback arrangements described above. The commitment letter received is contingent upon obtaining a new revolving credit facility. The closing of each of the three financings described above will be subject, among other things, to the negotiation of definitive agreements and other definitive documentation. There can be no assurance that the Company will be able to successfully implement any of the components of the Refinancing Plan. The availability of funds from the closing of these transactions will be a condition to the Company's ability to purchase any Notes.

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

1. BASIS OF PRESENTATION (CONTINUED)
INVENTORIES--

Inventories are stated at the lower of first-in, first-out cost or market. Inventories as of September 30, 2001 and December 31, 2000 were as follows (in thousands):

	SEPTEMBER 30, 2001	DECEMBER 31, 2000
Raw materials	$ 2,983	$ 1,307
Goods in process	145	66
Finished goods	12,266	10,197
Total	$15,394	$11,570

RECLASSIFICATIONS--

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

2. EARNINGS PER SHARE

Basic net income (loss) per share is calculated by dividing income (loss) available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted earnings per share is calculated by dividing earnings available to common stockholders by the weighted average number of shares of common stock and common stock equivalents outstanding during the period. Common stock equivalents are dilutive stock options that are assumed exercised for calculation purposes. The number of common stock equivalents which could dilute basic earnings per share in the future, that were not included in the computation of diluted earnings per share because to do so would have been antidilutive, was 21,833 for the nine months ended October 1, 2000.

Presented below is the reconciliation between basic and diluted weighted average shares for the three and nine months ended September 30, 2001 and October 1, 2000 (in thousands):

	FOR THE THREE MONTHS ENDED			
	BASIC		DILUTED	
	SEPTEMBER 30, 2001	OCTOBER 1, 2000	SEPTEMBER 30, 2001	OC
Weighted average number of common shares outstanding during the period	7,359	7,409	7,359	
Assumed exercise of stock options	--	--	57	

Weighted average number of shares outstanding...	7,359	7,409	7,416

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

2. EARNINGS PER SHARE (CONTINUED)

	FOR THE NINE MONTHS ENDED			
	BASIC		DILUTED	
	SEPTEMBER 30, 2001	OCTOBER 1, 2000	SEPTEMBER 30, 2001	OC
Weighted average number of common shares outstanding during the period................	7,366	7,439	7,366	
Assumed exercise of stock options..............	--	--	16	
Weighted average number of shares outstanding...	7,366	7,439	7,382	

3. SEGMENT REPORTING

Operating segments are components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision-maker, or decision-making group, in deciding how to allocate resources and in assessing performance. The Company's chief operating decision-maker is the Chairman of the Board and Chief Executive Officer of the Company. The Company's operating segments include restaurant, foodservice and franchise. The revenues from these segments include both sales to unaffiliated customers and intersegment sales, which generally are accounted for on a basis consistent with sales to unaffiliated customers. Intersegment sales and other intersegment transactions have been eliminated in the accompanying condensed consolidated financial statements.

The Company's restaurants target families with children and adults who desire a reasonably-priced meal in a full-service setting. The Company's menu offers a broad selection of freshly-prepared foods which appeal to customers throughout all dayparts. The menu currently features over 100 items comprised of a broad selection of breakfast, lunch, dinner and afternoon and evening snack items. Foodservice operations manufactures frozen dessert products and distributes such manufactured products and purchased finished goods to the Company's restaurants and franchised operations. Additionally, it sells frozen dessert products to distributors and retail and institutional locations. The Company's franchise segment includes a royalty based on franchise restaurant revenue. In addition, the Company receives rental income from various franchised restaurants. The Company does not allocate general and administrative expenses associated with its headquarters operations to any business segment. These costs include general and administrative expenses of the following functions: legal, accounting, personnel not directly related to a segment, information systems and other headquarters activities.

On May 1, 2001, foodservice decreased its ice cream pricing to all restaurants. This resulted in decreased foodservice restaurant revenues of 4.7% and 3.0% for the third quarter and nine months ended September 30, 2001, respectively.

The accounting policies of the operating segments are the same as those described in the summary of significant accounting policies except that the financial results for the foodservice operating segment, prior to intersegment eliminations, have been prepared using a management approach, which is consistent with the basis and manner in which the Company's management internally reviews financial information for the purpose of assisting in making internal operating decisions. The Company evaluates performance based on stand-alone operating segment income (loss) before income taxes and generally

3. SEGMENT REPORTING (CONTINUED)

accounts for intersegment sales and transfers as if the sales or transfers were to third parties, that is, at current market prices.

EBITDA represents net income (loss) before (i) (provision for) benefit from income taxes, (ii) interest expense, net, (iii) depreciation and amortization, (iv) extraordinary item and (v) write-downs and all other non-cash items plus cash distributions from unconsolidated subsidiaries. The Company has included information concerning EBITDA in this Form 10-Q because it believes that such information is used by certain investors as one measure of a company's historical ability to service debt. EBITDA should not be considered as an alternative to, or more meaningful than, earnings (loss) from operations or other traditional indications of a company's operating performance.

	FOR THE THREE MONTHS ENDED		FOR THE NINE MONTHS EN	
	SEPTEMBER 30, 2001	OCTOBER 1, 2000	SEPTEMBER 30, 2001	OCTOBER 2000
	(IN THOUSANDS)			
Revenues:				
Restaurant	$118,931	$137,462	$345,029	$ 399,
Foodservice	64,905	65,501	177,712	183,
Franchise	2,535	1,763	7,197	5,
Total	$186,371	$204,726	$529,938	$ 588,
Intersegment revenues:				
Restaurant	$ --	$ --	$ --	$
Foodservice	(34,356)	(42,885)	(99,643)	(123,
Franchise	--	--	--	
Total	$(34,356)	$(42,885)	$(99,643)	$(123,

External revenues:				
Restaurant	$118,931	$137,462	$345,029	$ 399,
Foodservice	30,549	22,616	78,069	59,
Franchise	2,535	1,763	7,197	5,
Total	$152,015	$161,841	$430,295	$ 465,

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

3. SEGMENT REPORTING (CONTINUED)

	FOR THE THREE MONTHS ENDED		FOR THE NINE MONTHS EN	
	SEPTEMBER 30, 2001	OCTOBER 1, 2000	SEPTEMBER 30, 2001	OCTOBER 2000
	(IN THOUSANDS)			
EBITDA:				
Restaurant	$ 16,587	$ 16,085	$ 41,379	$ 39,
Foodservice	2,617	6,406	10,505	18,
Franchise	1,482	581	3,903	2,
Corporate	(2,850)	(4,460)	(11,866)	(14,
(Loss) gain on property and equipment, net	(55)	885	6,009	3,
Restructuring costs	--	--	--	(12,
Total	$ 17,781	$ 19,497	$ 49,930	$ 37,
Interest expense, net	$ 6,464	$ 7,594	$ 20,967	$ 23,
Depreciation and amortization:				
Restaurant	$ 4,618	$ 5,052	$ 14,277	$ 15,
Foodservice	834	825	2,529	2,
Franchise	62	90	183	
Corporate	1,523	1,459	4,697	4,
Total	$ 7,037	$ 7,426	$ 21,686	$ 23,
Other non-cash expenses:				
Corporate	$ 67	$ 142	$ 235	$
Write-downs of property and equipment	35	664	103	19,
Total	$ 102	$ 806	$ 338	$ 19,

Income (loss) before (provision for)

benefit from income taxes and extraordinary item:				
Restaurant............................	$ 11,969	$ 11,033	$ 27,102	$ 23,
Foodservice...........................	1,783	5,581	7,976	16,
Franchise.............................	1,420	491	3,720	1,
Corporate.............................	(10,904)	(13,655)	(37,765)	(42,
(Loss) gain on property and equipment, net................................	(90)	221	5,906	(16,
Restructuring Costs...................	--	--	--	(12,
Total...............................	$ 4,178	$ 3,671	$ 6,939	$ (29,

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FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

3. SEGMENT REPORTING (CONTINUED)

	FOR THE THREE MONTHS ENDED		FOR THE NINE MONTHS EN	
	SEPTEMBER 30, 2001	OCTOBER 1, 2000	SEPTEMBER 30, 2001	OCTOBER 2000
	(IN THOUSANDS)			
Capital expenditures, including capitalized leases:				
Restaurant............................	$ 2,198	$ 5,824	$ 6,215	$ 12,
Foodservice...........................	268	44	1,483	1,
Corporate.............................	248	659	742	1,
Total...............................	$ 2,714	$ 6,527	$ 8,440	$ 15,

	SEPTEMBER 30, 2001	DECEMBER 31, 2000
Total assets:		
Restaurant..	$171,257	$199,223
Foodservice...	40,468	33,880
Franchise...	6,196	3,745
Corporate...	51,534	60,838
Total...	$269,455	$297,686

4. NEW ACCOUNTING PRONOUNCEMENTS

In September 2001, the Emerging Issues Task Force ("EITF") issued EITF Issue

No. 01-10, "Accounting for the Impact of the September 11, 2001 Terrorist Acts," which provides guidance on how the costs related to the terrorist acts should be classified, how to determine whether an asset impairment should be recognized and how liabilities for losses and other costs should be recognized. The impact of adopting EITF Issue No. 01-10 did not have any effect on the Company's consolidated financial statements.

In August 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 modifies the rules for accounting for the impairment or disposal of long-lived assets. The new rules become effective for fiscal years beginning after December 15, 2001, with earlier application encouraged. The Company has not yet quantified the impact of implementing SFAS No. 144 on the Company's consolidated financial statements.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangibles." SFAS No. 142 modifies the rules for accounting for goodwill and other intangible assets. The new rules become effective on January 1, 2002. The impact of adopting SFAS No. 142 will not have a material effect on the Company's consolidated financial statements and the Company will continue to amortize its license agreement related to certain trademarked products.

4. NEW ACCOUNTING PRONOUNCEMENTS (CONTINUED)

In April 2001, the FASB reached consensus on EITF Issue No. 00-25, "Accounting for Consideration from a Vendor to a Retailer in Connection with the Purchase or Promotion of the Vendor's Products," which is effective for quarters beginning after December 15, 2001, with prior financial statements restated if practicable. EITF Issue No. 00-25 requires that consideration from a vendor to a retailer be recorded as a reduction in revenue unless certain criteria are met. Arrangements within the scope of this Issue include slotting fees, cooperative advertising arrangements and buy-downs. As a result of EITF Issue No. 00-25, certain costs previously recorded as expense will be reclassified and offset against revenue. The Company's consolidated financial statements will be reclassified to conform with the consensus in the fourth quarter of 2001.

In May 2000, the Emerging Issues Task Force issued EITF Issue No. 00-14, "Accounting for Certain Sales Incentives," which provides guidance on the recognition, measurement and income statement classification for sales incentives offered voluntarily by a vendor without charge to customers that can be used in, or that are exercisable by a customer as a result of, a single exchange transaction. The Company adopted EITF Issue No. 00-14 on July 3, 2000. As a result, the Company has reclassified certain retail selling expenses against retail revenue for the three and nine months ended October 1, 2000 to conform with the current period presentation.

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 established accounting and reporting standards requiring that each derivative instrument (including certain derivative instruments embedded in other contracts) be recorded in the balance sheet as either an asset or liability measured at its fair value. The statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the statement of operations, and requires that a Company formally document, designate and assess the effectiveness of transactions that receive hedge accounting. Since the Company's commodity option contracts do not meet the criteria for hedge accounting, changes in the value of the commodity option contracts are recognized monthly in earnings. The cumulative effect upon adoption of approximately $77,000 has been recorded as income in the accompanying Condensed Consolidated Statement of Operations. It is not separately reported as a cumulative effect since the amount is not significant. Additionally, net losses of approximately $113,000 were recorded during the nine months ended September 30, 2001 related to the change in fair value for the period. The fair market value of derivatives at September 30, 2001 was approximately $19,000.

5. RESTRUCTURING PLAN

In March 2000, the Company's Board of Directors approved a restructuring plan that provided for the immediate closing of 81 restaurants at the end of March 2000 and the disposition of an additional 70 restaurants over the following 24 months. The 70 locations will remain in operation until they are sold, subleased or closed. In connection with the restructuring plan, the Company eliminated approximately 150 management and administrative positions in the field organization and at corporate headquarters. As a result of this plan, the Company reported a pre-tax restructuring charge of approximately $12,056,000 for severance pay, rent, utilities and real estate taxes, demarking, lease termination costs and certain other costs associated with the closing of the locations, along with a

5. RESTRUCTURING PLAN (CONTINUED)

pre-tax write-down of property and equipment for these locations of approximately $17,008,000 in the first quarter ended April 2, 2000.

The following represents the restructuring reserve activity (in thousands):

	BALANCE AS OF DECEMBER 31, 2000	COSTS PAID DURING THE NINE MONTHS ENDED SEPTEMBER 30, 2001	BALANCE AS OF SEPTEMBER 30, 2001
Severance pay	$ 74	$ (74)	$ --
Rent	3,585	(900)	2,685
Utilities and real estate taxes	1,105	(519)	586
Demarking	138	(126)	12
Lease termination costs	120	(120)	--
Inventory	5	(5)	--
Other	544	(169)	375
Total	$5,571	$(1,913)	$3,658

The write-down of property and equipment consisted of $7.8 million for the 81 locations closed at the end of March 2000 and $9.2 million for the 70 locations to be disposed of over the following 24 months. As of September 30, 2001, the Company had sold 60 of the 151 restructuring properties, of which 36 were included in the 81 restaurants that were closed in March 2000. The Company had also terminated its lease obligations at 49 restructuring properties, of which 33 were included in the list of 81 restaurants that were closed in March 2000. In addition, the Company has made a decision to continue to operate 25 of the 70 properties that were originally listed as locations to be disposed of. No amounts were included in the restructuring reserve related to these properties. These 25 properties are no longer being marketed and are now being depreciated. At September 30, 2001, the aggregate carrying amount of the remaining two operating restaurants and 15 closed properties to be disposed of was $1.3 million. At December 31, 2000, the aggregate carrying value of the 73 properties to be disposed of was $7.0 million. The amounts related to properties held for sale are reflected in the condensed consolidated balance sheets as property and equipment, net.

6. SALES OF RESTAURANT OPERATIONS AND PROPERTIES TO FRANCHISEES

On September 14, 2001, the Company entered into an agreement granting Revere Restaurant Group, Inc. ("Revere") certain limited exclusive rights to operate and develop Friendly's full-service restaurants in designated areas within Lehigh and Northampton counties, Pennsylvania (the "Revere Agreement"). Pursuant to the Revere Agreement, Revere purchased certain assets and rights in six existing Friendly's restaurants and committed to open an additional four restaurants over the next seven years. The president of Revere is a former employee of the Company. Gross proceeds from the sale were approximately $3.4 million of which approximately $0.2 million was for franchise fees for the initial six restaurants. The $0.2 million was recorded as revenue in the third quarter ended September 30, 2001. The Company also recognized a gain of approximately $0.3 million related to the sale of the assets for the six locations in the third quarter ended September 30, 2001.

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FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

6. SALES OF RESTAURANT OPERATIONS AND PROPERTIES TO FRANCHISEES (CONTINUED)

On April 13, 2001, the Company entered into an agreement granting J&B Restaurants Partners of Long Island Holding Co., LLC ("J&B") certain limited exclusive rights to operate and develop Friendly's full-service restaurants in the franchising regions of Nassau and Suffolk Counties in Long Island, New York (the "J&B Agreement"). Pursuant to the J&B Agreement, J&B purchased certain assets and rights in 31 existing Friendly's restaurants and committed to open an additional 29 restaurants over the next 12 years. Gross proceeds from the sale were approximately $19,950,000, of which approximately $4,250,000 was received in a note and $940,000 was for franchise fees for the initial 31 restaurants. The $940,000 was recorded as revenue in the second quarter ended July 1, 2001. The Company recognized a gain of approximately $3,955,000 related to the sale of the assets for the 31 locations in the second quarter ended July 1, 2001. The cash proceeds were used to prepay approximately $4,711,000 on the term loans with the remaining balance being applied to the revolving credit facility. The 5-year note bears interest at an annual rate of 11% using a 20-year amortization schedule. Payments are due monthly through the five years with a balloon payment due at the end of five years. The Company also sold certain assets and rights in two other restaurants to an additional franchisee resulting in a loss of $16,000.

On January 19, 2000, the Company entered into an agreement granting Kessler Family LLC ("Kessler") non-exclusive rights to operate and develop Friendly's full-service restaurants in the franchising region of Rochester, Buffalo and Syracuse, New York (the "Kessler Agreement"). Pursuant to the Kessler Agreement, Kessler purchased certain assets and rights in 29 existing Friendly's restaurants and committed to open an additional 15 restaurants over the next seven years. Gross proceeds from the sale were approximately $13,300,000 of which $735,000 was for franchise fees for the initial 29 restaurants. The $735,000 was recorded as revenue in the first quarter ended April 2, 2000. The Company recognized a gain of approximately $1,400,000 related to the sale of the assets for the 29 locations in the first quarter ended April 2, 2000. The Company also sold certain assets and rights in six other restaurants to two additional franchisees resulting in a gain of $687,000.

Effective August 6, 2001, the Company's largest franchisee, Davco Restaurants, Inc. ("Davco") refranchised three Newark, Delaware units, transferring it's rights to R.R.C. Restaurants, Inc. In addition, Davco closed two units during the quarter ended September 30, 2001. Currently, Davco is seeking to refranchise an additional 25 to 28 units.

7. EXTRAORDINARY ITEM

The Company recognized $0.2 million of expense, net of the related income tax benefit of $0.2 million, in 2001 related to previously deferred financing costs associated with Tranche A of the term loans, which was prepaid and extinguished in full during the quarter ended September 30, 2001.

8. SUBSEQUENT EVENT

On October 10, 2001, the Company eliminated approximately 70 positions at corporate headquarters. The purpose of the reduction was to streamline functions and reduce redundancy amongst its business segments. In addition, approximately 30 positions in the restaurant construction and fabrication areas will be eliminated by December 30, 2001. The Company believes the outsourcing of such activities will be more cost effective in the future. Annual salaries and fringe benefits associated with these 100 positions is approximately $5.6 million. As a result of the elimination of the positions and the outsourcing of certain functions, the Company will be reporting a pre-tax restructuring charge of approximately $2.5-$3.0 million for severance pay, rent and inventory in the fourth quarter ending December 30, 2001.

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION

FICC's obligation related to the $200 million Senior Notes is guaranteed fully and unconditionally by one of FICC's wholly- owned subsidiaries. There are no restrictions on FICC's ability to obtain dividends or other distributions of funds from this subsidiary, except those imposed by applicable law. The following supplemental financial information sets forth, on a condensed consolidating basis, balance sheets, statements of operations and statements of cash flows for Friendly Ice Cream Corporation (the "Parent Company"), Friendly's Restaurants Franchise, Inc. (the "Guarantor Subsidiary") and Friendly's International, Inc. and Restaurant Insurance Corporation (together, the "Non-guarantor Subsidiaries"). Separate complete financial statements and other disclosures of the Guarantor Subsidiary as of September 30, 2001 and October 1, 2000, and for the periods ended September 30, 2001 and October 1, 2000, are not presented because management has determined that such information is not material to investors.

Investments in subsidiaries are accounted for by the Parent Company on the equity method for purposes of the supplemental consolidating presentation. Earnings of the subsidiaries are, therefore, reflected in the Parent Company's investment accounts and earnings. The principal elimination entries eliminate the Parent Company's investments in subsidiaries and intercompany balances and transactions.

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING BALANCE SHEET
AS OF SEPTEMBER 30, 2001
(Unaudited)
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONS
Assets					
Current assets:					
Cash and cash equivalents.........	$ 6,661	$ 18	$ 878	$ --	$
Restricted cash..................	--	--	--	--	
Accounts receivable, net..........	7,848	646	--	--	
Inventories.......................	15,394	--	--	--	
Deferred income taxes............	10,258	43	--	94	
Prepaid expenses and other current assets.........................	8,537	983	3,504	(9,672)	
Total current assets................	48,698	1,690	4,382	(9,578)	
Deferred income taxes...............	--	506	1,327	(1,833)	
Property and equipment, net.........	194,219	--	--	--	1
Intangibles and deferred costs, net.............................	19,783	--	--	--	
Investments in subsidiaries.........	5,327	--	--	(5,327)	
Other assets........................	9,347	4,520	6,229	(9,835)	
Total assets........................	$277,374	$6,716	$11,938	$(26,573)	$2
Liabilities and Stockholders' Equity (Deficit)					
Current liabilities:					
Current maturities of long-term obligations.....................	$ 9,375	$ --	$ --	$ (3,500)	$
Accounts payable..................	21,622	--	--	--	
Accrued expenses..................	46,167	1,026	7,682	(5,987)	
Total current liabilities...........	77,164	1,026	7,682	(9,487)	

Deferred income taxes..............	17,407	--	--	(1,739)	
Long-term obligations, less current maturities.......................	263,386	--	--	(5,314)	2
Other long-term liabilities.........	14,992	1,080	3,539	(4,706)	
Stockholders' (deficit) equity......	(95,575)	4,610	717	(5,327)	(
Total liabilities and stockholders' (deficit) equity.................	$277,374	$6,716	$11,938	$(26,573)	$2

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FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2001
(Unaudited)
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONS
Revenues...........................	$149,941	$2,074	$ --	$ --	$1
Costs and expenses:					
Cost of sales....................	54,840	--	--	--	
Labor and benefits...............	39,674	--	--	--	
Operating expenses and write-downs of property and equipment.......	31,964	--	1	--	
General and administrative expenses.......................	7,224	1,169	--	--	
Depreciation and amortization.....	7,037	--	--	--	
Gain on franchise sales of restaurant operations and properties.......................	(219)	--	--	--	
Gain on dispositions of other property and equipment............	(317)	--	--	--	
Interest expense (income)...........	6,640	--	(176)	--	
Income before provision for income taxes, extraordinary item and equity in net income of consolidated subsidiaries.........	3,098	905	175	--	
Provision for income taxes..........	(1,180)	(372)	(61)	--	
Income before extraordinary item and equity in net income of consolidated subsidiaries.........	1,918	533	114	--	
Extraordinary item, net of income tax benefit......................	(221)	--	--	--	

Income before equity in net income of consolidated subsidiaries......	1,697	533	114	--	
Equity in net income of consolidated subsidiaries.....................	647	--	--	(647)	
Net income.........................	$ 2,344	$ 533	$ 114	$(647)	$

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001
(Unaudited)
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONS
Revenues...........................	$424,304	$ 5,991	$ --	$ --	$4
Costs and expenses:					
Cost of sales....................	149,757	--	--	--	1
Labor and benefits...............	120,684	--	--	--	1
Operating expenses and write-downs of property and equipment.......	89,803	--	(10)	--	
General and administrative expenses.......................	23,585	3,485	--	--	
Depreciation and amortization.....	21,686	--	--	--	
Gain on franchise sales of restaurant operations and properties.......................	(4,042)	--	--	--	
Gain on dispositions of other property and equipment............	(2,559)	--	--	--	
Interest expense (income)...........	21,540	--	(573)	--	
Income before provision for income taxes, extraordinary item and equity in net income of consolidated subsidiaries.........	3,850	2,506	583	--	
Provision for income taxes..........	(1,312)	(1,028)	(205)	--	
Income before extraordinary item and equity in net income of consolidated subsidiaries.........	2,538	1,478	378	--	

Extraordinary item, net of income tax benefit......................	(221)	--	--	--	--
Income before equity in net income of consolidated subsidiaries......	2,317	1,478	378	--	
Equity in net income of consolidated subsidiaries.....................	1,856	--	--	(1,856)	--
Net income.........................	$ 4,173	$ 1,478	$ 378	$(1,856)	$

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FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
FOR THE NINE MONTHS ENDED SEPTEMBER 30, 2001
(Unaudited)
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CON
Net cash provided by (used in) operating activities..............	$ 12,639	$(15)	$ 2,240	$(2,294)	$
Cash flows from investing activities:					
Purchases of property and equipment.......................	(8,440)	--	--	--	
Proceeds from sales of property and equipment.......................	23,556	--	--	--	
Net cash provided by investing activities........................	15,116	--	--	--	
Cash flows from financing activities:					
Proceeds from borrowings...........	51,405	--	--	--	
Repayments of obligations..........	(86,118)	--	--	--	
Reinsurance deposits received......	--	--	505	(505)	
Reinsurance payments made from deposits........................	--	--	(2,799)	2,799	
Net cash used in financing activities........................	(34,713)	--	(2,294)	2,294	

Net decrease in cash and cash

equivalents........................	(6,958)	(15)	(54)	--	
Cash and cash equivalents, beginning of period.........................	13,619	33	932	--	
Cash and cash equivalents, end of period............................	$ 6,661	$ 18	$ 878	$ --	$
Supplemental disclosures:					
Interest paid (received)...........	$ 17,273	$ --	$ (574)	$ --	$
Income taxes paid..................	1	2	--	--	
Capital lease obligations terminated.......................	170	--	--	--	
Note received from the sale of property and equipment...........	4,250	--	--	--	

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FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING BALANCE SHEET
AS OF DECEMBER 31, 2000
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONS
Assets					
Current assets:					
Cash and cash equivalents.........	$ 13,619	$ 33	$ 932	$ --	$
Restricted cash...................	--	--	1,737	--	
Accounts receivable, net..........	5,649	508	--	--	
Inventories.......................	11,570	--	--	--	
Deferred income taxes.............	10,258	43	--	94	
Prepaid expenses and other current assets.........................	7,435	551	4,057	(9,244)	
Total current assets................	48,531	1,135	6,726	(9,150)	
Deferred income taxes...............	--	506	1,327	(1,833)	
Property and equipment, net.........	226,865	--	--	--	2
Intangible assets and deferred costs, net.......................	21,529	--	--	--	
Investments in subsidiaries.........	3,500	--	--	(3,500)	
Other assets........................	1,135	3,614	5,729	(8,428)	
Total assets........................	$301,560	$5,255	$13,782	$(22,911)	$2

Liabilities and Stockholders' (Deficit) Equity

Current liabilities:					
Current maturities of long-term obligations....................	$ 19,172	$ --	$ --	$ (4,000)	$
Accounts payable.................	20,100	--	--	--	
Accrued expenses.................	43,683	648	8,082	(5,014)	
Total current liabilities..........	82,955	648	8,082	(9,014)	
Deferred income taxes..............	15,015	--	--	(1,739)	
Long-term obligations, less current maturities......................	288,472	--	--	(4,814)	2
Other liabilities..................	15,101	1,475	5,332	(3,844)	
Stockholders' (deficit) equity......	(99,983)	3,132	368	(3,500)	(
Total liabilities and stockholders' (deficit) equity.................	$301,560	$5,255	$13,782	$(22,911)	$2

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
FOR THE THREE MONTHS ENDED OCTOBER 1, 2000
(Unaudited)
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CON
Revenues............................	$160,511	$1,330	$ --	$ --	$
Costs and expenses:					
Cost of sales......................	54,081	--	--	--	
Labor and benefits.................	47,822	--	--	--	
Operating expenses and write-downs of property and equipment.........	33,319	--	(44)	--	
General and administrative expenses.........................	7,177	1,680	--	--	
Depreciation and amortization.......	7,426	--	--	--	
Loss on franchise sales of restaurant operations and properties..........	75	--	--	--	
Gain on dispositions of other property and equipment......................	(960)	--	--	--	
Interest expense (income)............	7,768	--	(174)	--	
Income (loss) before (provision for) benefit from income taxes and equity in net loss of consolidated subsidiaries.......................	3,803	(350)	218	--	
(Provision for) benefit from income taxes.............................	(493)	144	(76)	--	

Income (loss) before equity in net loss of consolidated subsidiaries...	3,310	(206)	142	--	
Equity in net loss of consolidated subsidiaries.......................	(64)	--	--	64	
Net income (loss)....................	$ 3,246	$ (206)	$142	$ 64	$

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF OPERATIONS
FOR THE NINE MONTHS ENDED OCTOBER 1, 2000
(Unaudited)
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CONS
Revenues............................	$460,751	$4,510	$ --	$ --	$4
Costs and expenses:					
Cost of sales....................	149,146	--	--	--	1
Labor and benefits...............	145,397	--	--	--	1
Operating expenses and write-downs of property and equipment.......	113,713	--	(159)	--	1
General and administrative expenses.......................	27,473	2,951	--	--	
Restructuring costs..............	12,056	--	--	--	
Depreciation and amortization.....	23,166	--	--	--	
Gain on franchise sales of restaurant operations and properties.......................	(1,923)	--	--	--	
Gain on dispositions of other property and equipment............	(1,005)	--	--	--	
Interest expense (income)...........	24,014	--	(519)	--	
(Loss) income before benefit from (provision for) income taxes and equity in net income of consolidated subsidiaries.........	(31,286)	1,559	678	--	(
Benefit from (provision for) income taxes............................	17,666	(639)	(237)	--	
(Loss) income before equity in net income of consolidated					

subsidiaries.....................	(13,620)	920	441	--	(
Equity in net income of consolidated subsidiaries.....................	1,361	--	--	(1,361)	
Net (loss) income..................	$(12,259)	$ 920	$441	$(1,361)	$(

FRIENDLY ICE CREAM CORPORATION AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(UNAUDITED)

9. SUPPLEMENTAL CONDENSED CONSOLIDATING FINANCIAL INFORMATION (CONTINUED)

SUPPLEMENTAL CONDENSED CONSOLIDATING STATEMENT OF CASH FLOWS
FOR THE NINE MONTHS ENDED OCTOBER 1, 2000
(Unaudited)
(In thousands)

	PARENT COMPANY	GUARANTOR SUBSIDIARY	NON-GUARANTOR SUBSIDIARIES	ELIMINATIONS	CON
Net cash provided by (used in) operating activities.............	$ 7,780	$ (3)	$ (105)	$(1,478)	$
Cash flows from investing activities:					
Purchases of property and equipment......................	(12,808)	--	--	--	
Proceeds from sales of property and equipment..................	32,594	--	--	--	
Net cash provided by investing activities.......................	19,786	--	--	--	
Cash flows from financing activities:					
Proceeds from borrowings..........	74,000	--	--	--	
Repayments of obligations.........	(103,022)	--	--	--	
Reinsurance deposits received.....	--	--	2,133	(2,133)	
Reinsurance payments made from deposits.......................	--	--	(3,611)	3,611	
Net cash used in financing activities.......................	(29,022)	--	(1,478)	1,478	
Net decrease in cash and cash equivalents......................	(1,456)	(3)	(1,583)	--	
Cash and cash equivalents, beginning of period........................	9,674	14	2,374	--	

Cash and cash equivalents, end of period	$ 8,218	$ 11	$ 791	$ --	$
Supplemental disclosures:					
Interest paid (received)	$ 18,805	$ --	$ (704)	$ --	$
Income taxes (refunded) paid	(1,075)	891	246	--	
Capital lease obligations incurred	2,891	--	--	--	
Capital lease obligations terminated	711	--	--	--	
Note received from the sale of property and equipment	577	--	--	--	

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

THE FOLLOWING DISCUSSION SHOULD BE READ IN CONJUNCTION WITH THE CONDENSED CONSOLIDATED FINANCIAL STATEMENTS OF THE COMPANY AND THE NOTES THERETO INCLUDED ELSEWHERE HEREIN.

FORWARD LOOKING STATEMENTS

Statements contained herein that are not historical facts constitute "forward looking statements" as that term is defined in the Private Securities Litigation Reform Act of 1995. All forward looking statements are subject to risks and uncertainties which could cause results to differ materially from those anticipated. These factors include the Company's highly competitive business environment, uncertainty with respect to the Company's ongoing compliance with covenants in its existing debt facilities and its ability to refinance its existing debt facilities, exposure to commodity prices, risks associated with the foodservice industry, the ability to retain and attract new employees, government regulations, the Company's high geographic concentration in the Northeast and its attendant weather patterns, conditions needed to meet re-imaging and new opening and franchising targets and risks associated with improved service and other initiatives. Other factors that may cause actual results to differ from the forward looking statements contained herein and that may affect the Company's prospects in general are included in the Company's other filings with the Securities and Exchange Commission.

OVERVIEW

As of September 30, 2001, the Company owned and operated 394 restaurants and franchised 160 restaurants and 6 cafes. The Company manufactures and distributes a full line of frozen dessert products, which are distributed to Friendly's restaurants and through more than 3,500 supermarkets and other retail locations in 17 states. The restaurants offer a wide variety of reasonably- priced breakfast, lunch and dinner menu items as well as the frozen dessert products.

	FOR THE THREE MONTHS ENDED		FOR THE NINE MONTHS ENDED	
	SEPTEMBER 30, 2001	OCTOBER 1, 2000	SEPTEMBER 30, 2001	OCTOBER 1, 2000

COMPANY UNITS:				
Beginning of period.............	403	486	449	618
Openings........................	--	--	--	2
Re-franchised closings..........	(6)	--	(39)	(37)
Closings........................	(3)	(15)	(16)	(112)
End of period...................	394	471	394	471
FRANCHISED UNITS:				
Beginning of period.............	163	114	127	69
Re-franchised openings..........	6	--	39	37
Openings........................	1	3	4	13
Closings........................	(4)	(2)	(4)	(4)
End of period...................	166	115	166	115

REVENUES:

Total revenues decreased $9.8 million, or 6.1%, to $152.0 million for the third quarter ended September 30, 2001 from $161.8 million for the same quarter in 2000. Restaurant revenues decreased $18.6 million, or 13.5%, to $118.9 million for the third quarter of 2001 from $137.5 million for the same quarter in 2000. Restaurant revenues decreased by $19.8 million due to the closing of 41 under-performing restaurants and the re-franchising of 51 additional locations over the past 15 months. Closing of restaurants accounted for $5.6 million of the restaurant revenue decline and re-franchising reduced restaurant revenues by an additional $14.2 million. Partially offsetting this decrease was a 1.5% increase in comparable restaurant revenues. Foodservice (product sales to franchisees, retail and institutional) revenues increased by $7.9 million, or 35.0%, to $30.5 million for the third quarter of 2001 from $22.6 million for the same quarter in 2000. The increase in the number of franchised units accounted for $4.1 million of the increase, sales to foodservice retail supermarket customers increased by $3.5 million and sales to outside distributors increased by $0.3 million. On May 1, 2001, foodservice decreased its ice cream pricing to all restaurants. This resulted in decreased foodservice revenues of 4.7% for the third quarter ended September 30, 2001. The Company's foodservice division sells a variety of products to the Company's franchisees and ice cream products to supermarkets and other retail locations. Franchise revenues increased $0.7 million, or 38.9%, to $2.5 million for the three months ended September 30, 2001 compared to $1.8 million for the three months ended October 1, 2000. The increase is largely the result of the difference in the number of franchised locations operating during both periods. There were 166 franchise units open at the end of the third quarter ended September 30, 2001 compared to 115 franchise units open at the end of the third quarter ended October 1, 2000.

Total revenues decreased $35.0 million, or 7.5%, to $430.3 million for the nine months ended September 30, 2001 from $465.3 million for the same period in 2000. Restaurant revenues decreased $54.7 million, or 13.7%, to $345.0 million for the first nine months of 2001 from $399.7 million for the same period in 2000. Restaurant revenues decreased by $59.1 million due to the closing of 138 under-performing restaurants and the re-franchising of 88 additional locations over the past 21 months. Closing of restaurants accounted for $27.0 million of the restaurant revenue decline and re-franchising reduced restaurant revenues by an additional $32.1 million. Partially offsetting this decrease was a 1.3% increase in comparable restaurant revenues. Revenues from the one location open less than one year were $0.5 million. Foodservice (product sales to franchisees, retail and institutional) and other revenues increased by $18.3 million, or 30.6%, to $78.1 million for the nine months ended September 30, 2001 from $59.8 million for the same period in 2000. The increase in the number of franchised units accounted for $9.6 million of the increase, sales to foodservice retail supermarket customers increased by $7.6 million and sales to outside distributors increased by $1.1 million. On May 1, 2001, foodservice decreased its ice cream pricing to all restaurants. This resulted in decreased foodservice revenues of 3.0% for the nine months ended September 30, 2001. Franchise revenue increased $1.4 million, or 24.1%, to $7.2 million for the nine months ended September 30, 2001 compared to $5.8 million for the nine months ended October 1, 2000. The increase is largely the result of the difference in the number of franchised locations operating during both periods. There were 166 franchise units open at the end of the nine months ended September 30, 2001 compared to 115 franchise units open at the end of the nine months ended October 1, 2000.

COST OF SALES:

Cost of sales increased $0.7 million, or 1.4%, to $54.8 million for the third quarter ended September 30, 2001 from $54.1 million for the same quarter in 2000. Cost of sales as a percentage of total revenues increased to 36.1% for the third quarter of 2001 from 33.4% for the third quarter of 2000. The higher food cost as a percentage of total revenue was mainly due to a shift in sales mix from Company-owned restaurant sales to foodservice sales. Foodservice sales to franchisees and retail

customers have a higher food cost as a percentage of revenue than sales in Company-owned restaurants to restaurant patrons. The cost of cream, the principal ingredient used in making ice cream, was higher in the third quarter of 2001 when compared to the third quarter of 2000 and partially contributed to the rise in cost of sales as a percentage of total revenues, especially in foodservice's retail supermarket business. The Company believes that cream prices will be higher in the fourth quarter of 2001 when compared to those prices experienced during the fourth quarter of 2000. To minimize risk, alternative supply sources continue to be pursued.

Cost of sales increased $0.6 million, or 0.4%, to $149.7 million for the nine months ended September 30, 2001 from $149.1 million for the same period in 2000. Cost of sales as a percentage of total revenues increased to 34.8% for the nine months in 2001 from 32.0% for the same period in 2000. The higher food cost as a percentage of total revenue was partially due to a shift in sales mix from Company-owned restaurant sales to foodservice sales. Foodservice sales to franchisees and retail customers have a higher food cost as a percentage of revenue than sales in Company-owned restaurants to restaurant patrons. The cost of cream, the principal ingredient used in making ice cream, was higher in the first nine months of 2001 when compared to the first nine months of 2000 and contributed to the rise in cost of sales as a percentage of total revenues, especially in foodservice's retail supermarket business. In May 2001, the Company raised prices to its retail customers.

LABOR AND BENEFITS:

Labor and benefits decreased $8.1 million, or 17.0%, to $39.7 million for the third quarter ended September 30, 2001 from $47.8 million for the same quarter in 2000. Labor and benefits as a percentage of total revenues decreased to 26.1% for the third quarter of 2001 from 29.5% for the same quarter in 2000. The lower labor cost as a percentage of total revenue is partially the result of revenue increases derived from additional franchised locations and higher sales to foodservice retail supermarket customers, which do not have any associated restaurant labor and benefits. In addition, the closing of 41 under-performing

Company-owned units over the past 15 months improved the relationship of restaurant labor and benefits to restaurant sales as well as to total revenues.

Labor and benefits decreased $24.7 million, or 17.0%, to $120.7 million for the nine months ended September 30, 2001 from $145.4 million for the same period in 2000. Labor and benefits as a percentage of total revenues decreased to 28.0% for the nine months of 2001 from 31.3% for the same period in 2000. The lower labor cost as a percentage of total revenue is partially the result of revenue increases derived from additional franchised locations and higher sales to foodservice retail supermarket customers, which do not have any associated restaurant labor and benefits. In addition, the closing of 138 under-performing Company-owned units over the past 21 months improved the relationship of restaurant labor and benefits to restaurant sales as well as to total revenues.

OPERATING EXPENSES:

Operating expenses decreased $0.7 million, or 2.1%, to $31.9 million for the third quarter ended September 30, 2001 from $32.6 million for the same quarter in 2000. Operating expenses as a percentage of total revenues were 21.0% and 20.2% for the third quarters ended September 30, 2001 and October 1, 2000, respectively. The increase as a percentage of total revenues resulted from higher costs for foodservice retail promotions and restaurant utilities in the 2001 quarter when compared to the 2000 quarter.

Operating expenses decreased $4.8 million, or 5.1%, to $89.7 million for the nine months ended September 30, 2001 from $94.5 million for the same period in 2000. Operating expenses as a percentage of total revenues were 20.8% and 20.3% for the nine months ended September 30, 2001 and October 1, 2000, respectively. The increase as a percentage of total revenues resulted from higher

costs for foodservice retail promotions and restaurant advertising and utilities in the 2001 period when compared to the 2000 period.

GENERAL AND ADMINISTRATIVE EXPENSES:

General and administrative expenses were $8.4 million for the third quarter ended September 30, 2001 and $8.9 million for the same period in 2000. General and administrative expenses as a percentage of total revenues were 5.5% in the third quarters of 2001 and 2000. In the 2001 period, bonus expense increased $1.1 million when compared to the same period in 2000.

General and administrative expenses were $27.1 million and $30.4 million for the nine months ended September 30, 2001 and October 1, 2000, respectively. General and administrative expenses as a percentage of total revenues decreased to 6.3% in the nine months ended September 30, 2001 from 6.5% for the same period in 2000. The decrease is primarily the result of the elimination of certain management and administrative positions associated with the Company's announcement of the immediate closing of 81 restaurants and the planned closing of 70 additional restaurants in March 2000 and an on-going hiring freeze. In the 2001 period, bonus expense increased $0.8 million when compared to the same period in 2000.

EBITDA:

As a result of the above, EBITDA (EBITDA represents net income (loss) before (i) benefit from (provision for) income taxes, (ii) interest expense, net, (iii) depreciation and amortization, (iv) extraordinary item and (v) write-downs and all other non-cash items plus cash distributions from unconsolidated subsidiaries) decreased $1.7 million, or 8.8%, to $17.8 million for the third quarter ended September 30, 2001 from $19.5 million for the same quarter in 2000. EBITDA as a percentage of total revenues was 11.7% and 12.0% for the third quarters of 2001 and 2000, respectively.

EBITDA increased $12.8 million, or 34.7%, to $49.9 million for the nine months ended September 30, 2001 from $37.1 million for the same period in 2000. EBITDA as a percentage of total revenues was 11.6% and 8.0% for the nine months ended September 30, 2001 and October 1, 2000, respectively.

RESTRUCTURING COSTS:

Restructuring costs were $12.1 million for the nine months ended October 1, 2000 as a result of the costs associated with the Company's decision to reorganize its restaurant field and headquarters organizations in conjunction with the closing of 81 under-performing restaurants and the planned closing of an additional 70 restaurants over the following 24 months. Included in these costs are severance, rent on closed units until lease termination, utilities and real estate taxes, demarking, lease termination, environmental and other miscellaneous costs.

WRITE-DOWNS OF PROPERTY AND EQUIPMENT:

Write-downs of property and equipment were $0.7 million for the three months ended October 1, 2000. Write-downs of property and equipment were $0.1 million and $19.0 million for the nine months ended September 30, 2001 and October 1, 2000, respectively. The decrease in write-downs is primarily the result of the non-cash write-down of the 81 under-performing restaurants which were closed at the end of March 2000 and the non-cash write-down of the additional 70 restaurants which were to be closed over the following 24 months to their estimated net realizable value. During the nine months ended September 30, 2001, the Company made the decision to continue to operate 25 of these properties. As of September 30, 2001, 27 of these 70 restaurants are still operating.

DEPRECIATION AND AMORTIZATION:

Depreciation and amortization decreased $0.4 million, or 5.2%, to $7.0 million for the third quarter ended September 30, 2001 from $7.4 million for the same quarter in 2000. Depreciation and amortization as a percentage of total revenues was 4.6% for the third quarters of 2001 and 2000.

Depreciation and amortization decreased $1.5 million, or 6.4%, to $21.7 million for the nine months ended September 30, 2001 from $23.2 million for the same period in 2000. Depreciation and amortization as a percentage of total revenues was 5.0% for the nine months ended September 30, 2001 and October 1, 2000.

(GAIN) LOSS ON FRANCHISE SALES OF RESTAURANT OPERATIONS AND PROPERTIES:

Gain on franchise sales of restaurant operations and properties was $0.2 million for the third quarter ended September 30, 2001 compared to a loss of $0.1 million for the third quarter ended October 1, 2000. The gain on franchise sales of restaurant operations and properties was $4.0 million and $1.9 million for the nine months ended September 30, 2001 and October 1, 2000, respectively. The increase was primarily the result of the gain of $4.3 million associated with the sale of 37 restaurants to a franchisee during the nine months ended September 30, 2001 as compared to the gain of $1.4 million associated with the sale of 29 restaurants to a franchisee on January 19, 2000. The Company also sold certain assets and rights in eight other restaurants to three additional franchisees resulting in a gain of $0.7 million during the nine months ended October 1, 2000.

GAIN ON DISPOSITION OF OTHER PROPERTY AND EQUIPMENT:

The gain on disposition of other property and equipment for the quarters ended September 30, 2001 and October 1, 2000 was $0.3 million and $1.0 million, respectively. The gain on disposition of other property and equipment was $2.6 million and $1.0 million for the nine months ended September 30, 2001 and October 1, 2000, respectively. The gain in the 2001 period resulted from the sale of 21 closed locations during the nine month period ended September 30, 2001 compared to the sale of 20 closed locations during the nine month period ended October 1, 2000.

INTEREST EXPENSE, NET:

Interest expense, net of capitalized interest and interest income, decreased by $1.1 million, or 14.9%, to $6.5 million for the third quarter ended September 30, 2001 from $7.6 million for the same quarter in 2000. The decrease is primarily due to a reduction in the average outstanding debt.

Interest expense, net of capitalized interest and interest income, decreased by $2.5 million, or 10.8%, to $21.0 million for the nine months ended September 30, 2001 from $23.5 million for the same period in 2000. The decrease is primarily impacted by the decrease in the average outstanding balance on the term loans for the nine months ended September 30, 2001 compared to the nine months ended October 1, 2000. Total outstanding debt, including capital lease obligations, was reduced from $288.9 million at October 1, 2000 to $263.9 million at September 30, 2001.

(PROVISION FOR) BENEFIT FROM INCOME TAXES:

The provision for income taxes was $1.6 million, or 38.6%, for the third quarter ended September 30, 2001 compared to $0.4 million, or 11.6%, for the third quarter ended October 1, 2000. The provision for income taxes was $2.5 million, or 36.7%, for the nine months ended September 30, 2001 compared to a benefit from taxes of $16.8 million, or 57.8%, for the nine months ended October 1, 2000. The Company records income taxes based on the effective rate expected for the year with any changes in the valuation allowance reflected in the period of change. The sales of the land and buildings to franchisees during the nine months ended October 1, 2000 favorably impacted the

provision for income taxes as it triggered built-in gains, which allowed for a reduction in the valuation allowance on certain net operating loss carryforwards.

EXTRAORDINARY ITEM:

The Company recognized $0.2 million of expense, net of the related income tax benefit of $0.2 million, in 2001 related to previously deferred financing costs associated with Tranche A of the term loans, which was prepaid and extinguished during the quarter ended September 30, 2001.

NET INCOME (LOSS):

Net income was $2.3 million and $3.2 million for the third quarters ended September 30, 2001 and October 1, 2000, respectively. Net income was $4.2 million for the nine months ended September 30, 2001 compared to a net loss of $12.3 million for the nine months ended October 1, 2000.

LIQUIDITY AND CAPITAL RESOURCES

The Company's primary sources of liquidity and capital resources are cash generated from operations and borrowings under its revolving credit facility. Net cash provided by operating activities was $12.6 million and $6.2 million for the nine months ended September 30, 2001 and October 1, 2000, respectively. During the nine months ended September 30, 2001, inventories increased $3.8 million as a result of increased retail promotional activity expected for the fourth quarter. Accounts payable increased $1.5 million primarily as a result of increased inventory purchases. Accounts receivable increased $2.3 million primarily due to increased retail supermarket sales along with the increase in volume of foodservice product sales to franchisees. Accrued expenses and other long- term liabilities decreased $1.8 million as a result of $2.3 million of payments made against the captive insurance company's reserves for workers compensation claims and $1.9 million of payments made against the restructuring reserve. These decreases were offset by an increase in accrued interest of $3.6 million related to the timing of interest payment dates. Available borrowings under the revolving credit facility were $18 million as of September 30, 2001.

Additional sources of liquidity consist of capital and operating leases for financing leased restaurant locations (in malls and shopping centers and land or building leases), restaurant equipment, manufacturing equipment, distribution vehicles and computer equipment. Additionally, sales of under-performing existing restaurant properties and other assets (to the extent the Company's and its subsidiaries' debt instruments, if any, permit) are sources of cash. The amounts of debt financing that the Company will be able to incur under capital leases and for property and casualty insurance financing and the amount of asset sales by the Company are limited by the terms of its credit facility and Senior Notes.

Net cash provided by investing activities was $15.1 million and $19.8 million in the nine months ended September 30, 2001 and October 1, 2000, respectively. Capital expenditures for restaurant operations were approximately $5.8 million and $12.7 million for the nine months ended September 30, 2001 and October 1, 2000, respectively. Other capital expenditures were $2.6 million and $3.0 million for the nine months ended September 30, 2001 and October 1, 2000, respectively. The decrease in capital expenditures was primarily due to the reduction in new units, replacements and re-imaging projects. Cash proceeds from the sale of property and equipment were $23.6 million and $32.6 million in the nine months ended September 30, 2001 and October 1, 2000, respectively. The decrease in proceeds was primarily due to the receipt of $7.4 million in 2001 compared to $15.2 million in 2000 related to the disposal of properties in connection with the March 2000 restructuring.

Net cash used in financing activities was $34.7 million and $29.0 million in the nine months ended September 30, 2001 and October 1, 2000, respectively.

The Company had a working capital deficit of $31.2 million as of September 30, 2001. The Company is able to operate with a substantial working capital deficit because: (i) restaurant operations are conducted primarily on a cash (and cash equivalent) basis with a low level of accounts receivable; (ii) rapid turnover allows a limited investment in inventories and (iii) cash from sales is usually received before related expenses for food, supplies and payroll are paid.

The Company's credit facility imposes significant operating and financial restrictions on the Company's ability to, among other things, incur indebtedness, create liens, sell assets, engage in mergers or consolidations, pay dividends and engage in certain transactions with affiliates. The credit facility limits the amount which the Company may spend on capital expenditures and requires the Company to comply with certain financial covenants. The Company's credit facility also restricts the use of proceeds from asset sales.

Proceeds, as defined in the credit agreement and subject to certain exceptions, in excess of stated maximum allowable amounts must be used to permanently reduce outstanding obligations under the credit facility. During the nine months ended September 30, 2001, the Company received $11.5 million of asset sale proceeds which were used to reduce the amount outstanding on the term loans.

The Company entered into its existing credit facility in November 1997. The credit facility includes the revolving credit loan, term loans and letters of credit. Since 1997, the Company has executed several amendments to the credit facility. The most recent amendment occurred on March 19, 2001. All of the existing financial covenants were amended and a new financial covenant was added requiring minimum cumulative Consolidated EBITDA, as defined, on a monthly basis. Interest rates on term loans, borrowings under the revolving credit facility and issued letters of credit increased 0.25%. In addition, automatic increases in the interest rates will occur on August 2, 2001, January 2, 2002, April 1, 2002, September 30, 2002 and October 1, 2002 of 0.25%, 0.50%, 0.25%, 0.25% and 0.25%, respectively. Interest payments on all ABR loans, Eurodollar loans and issued letters of credit are required on a monthly basis rather than quarterly.

Also due to the March 19, 2001 amendment, the maturity dates of Tranche B and Tranche C of the term loans were changed to November 15, 2002 from their original maturity dates of November 15, 2004 and November 15, 2005, respectively. Annual scheduled principal payments due through October 15, 2002 did not change. However, the amendment requires additional minimum cumulative prepayments on the term loans, excluding prepayments made pursuant to the J&B Agreement, by the dates specified below as follows:

October 15, 2001...	$6,000,000
January 15, 2002...	7,500,000
April 15, 2002...	8,500,000
July 15, 2002..	10,000,000

As of October 15, 2001, the Company has paid additional minimum cumulative prepayments of $6,793,000 on the term loans, which exceed the minimum cumulative prepayment requirement.

Tranche A of the term loans was prepaid and extinguished during the third quarter ended September 30, 2001. Any remaining unpaid balances due on Tranches B and C of the term loans will be paid on November 15, 2002.

FICC paid an amendment fee of approximately $256,000 to the lenders contemporaneous with the execution of the seventh amendment. FICC paid an additional amendment fee (the "Additional Fee") of $441,459 on October 1, 2001 pursuant to the seventh amendment, which will be expensed over the remaining term of the credit facility using the effective yield method. If all obligations under the credit facility were satisfied before September 30, 2001, the Additional Fee would have been reduced to approximately $128,000. The Company believes that based on the terms of the seventh amendment, the Company has adequate cash and availability on its revolving credit facility to meet its obligations

through September 30, 2002. Additionally, the Company believes that it can comply with the revised covenant requirements under the amendment through December 30, 2001.

The Company is undertaking a refinancing plan (collectively, the

"Refinancing Plan"), which has the following three principal components:

(i) obtaining a new revolving credit facility from one or more financial institutions for $35 million;

(ii) obtaining $55 million in loans from GE Capital Franchise Finance Corporation which will be secured by first mortgage liens upon 75 of the Company's restaurants; and

(iii) entering into a sale and leaseback arrangement with one or more financial institutions involving 45 of the Company's restaurants that is expected to provide the Company up to $37.5 million in cash.

The Company would use the proceeds of these financings to repay the amounts outstanding on its existing credit facility ($55,114,000 as of September 30, 2001), to increase working capital and, to the extent the proceeds of the financings are sufficient, after giving effect to the foregoing, to finance a tender offer for a portion of the Company's senior notes (the "Notes"). The Company has obtained a commitment letter from GE Capital Franchise Finance Corporation relating to the mortgage financing, but the Company does not have any commitments or other agreements from any financial institutions relating to the new revolving credit facility or the sale and leaseback arrangements described above. The commitment letter received is contingent upon obtaining a new revolving credit facility. The closing of each of the three financings described above will be subject, among other things, to the negotiation of definitive agreements and other definitive documentation. There can be no assurance that the Company will be able to successfully implement any of the components of the Refinancing Plan. The availability of funds from the closing of these transactions will be a condition to the Company's ability to purchase any Notes.

The Company anticipates requiring capital in the future principally to maintain existing restaurant and plant facilities and to continue to renovate and re-image existing restaurants. Capital expenditures for 2001 are anticipated to be $13.5 million in the aggregate, of which $10.0 million is expected to be spent on restaurant operations. The Company's actual 2001 capital expenditures may vary from these estimated amounts. The Company believes that the combination of the funds anticipated to be generated from operating activities and borrowing availability under the credit facility will be sufficient to meet the Company's anticipated operating requirements, capital requirements and obligations associated with the restructuring.

On September 14, 2001, the Company entered into an agreement granting Revere Restaurant Group, Inc. ("Revere") certain limited exclusive rights to operate and develop Friendly's full-service restaurants in designated areas within Lehigh and Northampton counties, Pennsylvania (the "Revere Agreement"). Pursuant to the Revere Agreement, Revere purchased certain assets and rights in six existing Friendly's restaurants and committed to open an additional four restaurants over the next seven years. Gross proceeds from the sale were approximately $3.4 million of which approximately $0.2 million was for franchise fees for the initial six restaurants. The cash proceeds were used to fund operating activities of the Company.

On April 13, 2001, the Company executed an agreement granting J&B Restaurants Partners of Long Island Holding Co., LLC ("J&B") certain limited exclusive rights to operate and develop Friendly's full-service restaurants in the franchising regions of Nassau and Suffolk Counties in Long Island, New York (the "J&B Agreement"). Pursuant to the J&B Agreement, J&B purchased certain assets and rights in 31 existing Friendly's restaurants and committed to open an additional 29 restaurants over the next 12 years. The transaction price was approximately $19,950,000, of which approximately $4,250,000 was received in a note. The cash proceeds were used to prepay approximately

$4.7 million on the term loans with the remaining balance being applied to the revolving credit facility. The 5-year note bears interest at an annual rate of 11% using a 20-year amortization schedule. Payments are due monthly through the five years with a balloon payment due at the end of five years.

RECENT DEVELOPMENTS

Effective August 6, 2001, the Company's largest franchisee, Davco Restaurants, Inc. ("Davco") refranchised three Newark, DE units, transferring it's rights to R.R.C. Restaurants, Inc. In addition, Davco closed two units during the quarter ended September 30, 2001. Currently, Davco is seeking to refranchise an additional 25 to 28 units.

SEASONALITY

Due to the seasonality of frozen dessert consumption and the effect from time to time of weather on patronage in its restaurants, the Company's revenues and EBITDA are typically higher in its second and third quarters.

GEOGRAPHIC CONCENTRATION

Approximately 89% of the Company-owned restaurants are located, and substantially all of its retail sales are generated, in the Northeast. As a result, a severe or prolonged economic recession or changes in demographic mix, employment levels, population density, weather, real estate market conditions or other factors specific to this geographic region may adversely affect the Company more than certain of its competitors which are more geographically diverse.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In September 2001, the Emerging Issues Task Force ("EITF") issued EITF Issue No. 01-10, "Accounting for the Impact of the September 11, 2001 Terrorist Acts," which provides guidance on how the costs related to the terrorist acts should be classified, how to determine whether an asset impairment should be recognized and how liabilities for losses and other costs should be recognized. The impact of adopting EITF Issue No. 01-10 did not have any effect on the Company's consolidated financial statements.

In August 2001, the Financial Accounting Standards Board ("FASB") issued Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." SFAS No. 144 modifies the rules for accounting for the impairment or disposal of long-lived assets. The new rules become effective for fiscal years beginning after December 15, 2001, with earlier application encouraged. The Company has not yet quantified the impact of implementing SFAS No. 144 on the Company's consolidated financial statements.

In June 2001, the FASB issued SFAS No. 142, "Goodwill and Other Intangibles." SFAS No. 142 modifies the rules for accounting for goodwill and other intangible assets. The new rules become effective on January 1, 2002. The impact of adopting SFAS No. 142 will not have a material effect on the Company's consolidated financial statements and the Company will continue to amortize its license agreement related to certain trademarked products.

In April 2001, the FASB reached consensus on EITF Issue No. 00-25, "Accounting for Consideration from a Vendor to a Retailer in Connection with the Purchase or Promotion of the Vendor's Products," which is effective for quarters beginning after December 15, 2001, with prior financial statements restated if practicable. EITF Issue No. 00-25 requires that consideration from a vendor to a retailer be recorded as a reduction in revenue unless certain criteria are met. Arrangements within the scope of this Issue include slotting fees, cooperative advertising arrangements and buy-downs. As a result of EITF Issue No. 00-25, certain costs previously recorded as expense will

be reclassified and offset against revenue. The Company's consolidated financial statements will be reclassified to conform with the consensus in the fourth quarter of 2001.

In May 2000, the Emerging Issues Task Force issued EITF Issue No. 00-14, "Accounting for Certain Sales Incentives," which provides guidance on the recognition, measurement and income statement classification for sales incentives offered voluntarily by a vendor without charge to customers that can be used in, or that are exercisable by a customer as a result of, a single exchange transaction. The Company adopted EITF Issue No. 00-14 on July 3, 2000. As a result, the Company has reclassified certain retail selling expenses against retail revenue for the three and nine months ended October 1, 2000 to conform with the current period presentation.

In June 1998, the FASB issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 established accounting and reporting standards requiring that each derivative instrument (including certain derivative instruments embedded in other contracts) be recorded in the balance sheet as either an asset or liability measured at its fair value. The statement requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the statement of operations, and requires that a Company formally document, designate and assess the effectiveness of transactions that receive hedge accounting. Since the Company's commodity option contracts do not meet the criteria for hedge accounting, changes in the value of the commodity option contracts are recognized monthly in earnings. The cumulative effect upon adoption of approximately $77,000 has been recorded as income in the accompanying Condensed Consolidated Statement of Operations. It is not separately reported as a cumulative effect since the amount is not significant. Additionally, net losses of approximately $113,000 were recorded during the nine months ended September 30, 2001 related to the change in fair value for the period. The fair market value of derivatives at September 30, 2001 was approximately $19,000.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There has been no material change in the Company's market risk exposure since the filing of the Annual Report on Form 10K.

PART II--OTHER INFORMATION

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

(a) An annual meeting of the Company's shareholders was held on May 16, 2001.

(b) Not applicable.

(c) The election of two nominees for directors of the Company was voted upon at the meeting. The number of affirmative votes and the number of votes withheld with respect to such approvals were as follows:

NOMINEE	AFFIRMATIVE VOTES	VOTES WITHHELD
Michael J. Daly......................	5,521,075	1,356,041
Burton J. Manning...................	5,531,600	1,345,516

The results of the voting to approve the appointment of Arthur Andersen LLP to audit the accounts of the Company and its subsidiaries for 2001 were as follows:

FOR	AGAINST	ABSTAIN
6,767,341	104,375	5,400

There were no matters voted upon at the Company's annual meeting to which broker non-votes applied.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

None

(b) No report on Form 8-K was filed during the three months and nine months ended September 30, 2001.

SIGNATURES

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

FRIENDLY ICE CREAM CORPORATION

By: /s/ PAUL V. HOAGLAND

Name: Paul V. Hoagland
Title: Senior Vice President, Chief Financial
Officer, Treasurer and Assistant Cler