CNF INC
Form 10-Q
August 05, 2004

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

FORM 10-Q

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

For the quarterly period ended June 30, 2004

OR

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

For the transition period from N/A to N/A

COMMISSION FILE NUMBER 1-5046

CNF Inc.

Incorporated in the State of Delaware
I.R.S. Employer Identification No. 94-1444798

3240 Hillview Avenue, Palo Alto, California 94304
Telephone Number (650) 494-2900

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

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

Number of shares of Common Stock, $.625 par value,
outstanding as of July 30, 2004: 50,939,112

CNF INC.

FORM 10-Q
Quarter Ended June 30, 2004

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements

CNF INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands)

ASSETS	June 30, 2004 (Unaudited)	December 31, 2003

Current Assets		
Cash and cash equivalents	$605,622	$321,460
Trade accounts receivable, net	809,308	769,707
Other accounts receivable	95,217	68,611
Operating supplies, at lower of average cost or market	18,392	14,333
Prepaid expenses	55,085	53,144
Deferred income taxes	100,035	89,440
Total Current Assets	1,683,659	1,316,695
Property, Plant and Equipment, at Cost		
Land	159,709	159,645
Buildings and leasehold improvements	808,892	792,289
Revenue equipment	648,309	652,818
Other equipment	374,080	373,034
	1,990,990	1,977,786
Accumulated depreciation and amortization	(1,009,162)	(980,331)
	981,828	997,455
Other Assets		
Deferred charges and other assets (Note 3)	69,322	130,324
Capitalized software, net	65,461	68,589
Goodwill, net	240,673	240,671
	375,456	439,584
Total Assets	$3,040,943	$2,753,734

The accompanying notes are an integral part of these statements.

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CNF INC.
CONSOLIDATED BALANCE SHEETS
(Dollars in thousands except per share amounts)

LIABILITIES AND SHAREHOLDERS' EQUITY	June 30, 2004 (Unaudited)	December 31, 2003
Current Liabilities		
Accounts payable	$406,457	$354,401
Accrued liabilities (Note 7)	331,560	320,250
Accrued claims costs	124,527	120,730
Current maturities of long-term debt		

and capital leases (Note 6)	112,902	14,230
Total Current Liabilities	975,446	809,611
Long-Term Liabilities		
Long-term debt and guarantees (Note 6)	603,681	554,981
Long-term obligations under capital leases	110,112	110,199
Accrued claims costs	105,625	114,793
Employee benefits (Note 4)	269,101	269,318
Other liabilities and deferred credits	40,780	38,149
Deferred income taxes	37,806	37,875
Total Liabilities	2,142,551	1,934,926
Commitments and Contingencies (Note 8)		
Shareholders' Equity		
Preferred stock, no par value; authorized 5,000,000 shares: Series B, 8.5% cumulative, convertible, $.01 stated value; designated 1,100,000 shares; issued 751,849 and 763,674 shares, respectively	8	8
Additional paid-in capital, preferred stock	114,349	116,147
Deferred compensation, Thrift and Stock Plan	(53,427)	(57,687)
Total Preferred Shareholders' Equity	60,930	58,468
Common stock, $.625 par value; authorized 100,000,000 shares; issued 57,207,901 and 56,436,981 shares, respectively	35,755	35,273
Additional paid-in capital, common stock	373,899	356,700
Retained earnings	620,591	570,751
Deferred compensation, restricted stock	(4,067)	(6,188)
Cost of repurchased common stock (6,402,718 and 6,459,732 shares, respectively)	(157,867)	(159,273)
	868,311	797,263
Accumulated Other Comprehensive Loss (Note 5)	(30,849)	(36,923)
Total Common Shareholders' Equity	837,462	760,340
Total Shareholders' Equity	898,392	818,808
Total Liabilities and Shareholders' Equity	$3,040,943	$2,753,734

The accompanying notes are an integral part of these statements.

CNF INC.
STATEMENTS OF CONSOLIDATED INCOME
(Unaudited)
(Dollars in thousands except per share amounts)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
REVENUES	$1,441,726	$1,236,905	$2,790,131	$2,443,146
Costs and Expenses				
Operating expenses (Note 3)	1,207,450	1,042,036	2,345,954	2,055,707
Selling, general and administrative expenses	128,853	124,053	253,927	242,343
Depreciation	32,031	33,496	64,116	66,728
	1,368,334	1,199,585	2,663,997	2,364,778
OPERATING INCOME	73,392	37,320	126,134	78,368
Other Income (Expense)				
Investment income	1,408	630	2,135	1,216
Interest expense (Note 6)	(11,847)	(8,974)	(20,887)	(18,246)
Miscellaneous, net	(1,469)	1,137	(2,572)	(1,790)
	(11,908)	(7,207)	(21,324)	(18,820)
Income Before Taxes	61,484	30,113	104,810	59,548
Income Tax Provision	23,979	11,744	40,876	23,224
Net Income	37,505	18,369	63,934	36,324
Preferred Stock Dividends	2,022	2,069	4,044	4,095
NET INCOME AVAILABLE TO COMMON SHAREHOLDERS	$35,483	$16,300	$59,890	$32,229
Weighted-Average Common Shares Outstanding (Note 1)				
Basic	50,319,659	49,494,145	50,075,246	49,445,348
Diluted	56,883,738	57,127,187	56,981,429	54,004,772

Earnings per Common Share (Note 1)				
Basic	$0.71	$0.33	$1.20	$0.65
Diluted	$0.64	$0.31	$1.09	$0.61

The accompanying notes are an integral part of these statements.

CNF INC.
STATEMENTS OF CONSOLIDATED CASH FLOWS
(Unaudited)
(Dollars in thousands)

	Six Months Ended June 30,	
	2004	2003
Cash and Cash Equivalents, Beginning of Period	$321,460	$270,404
Operating Activities		
Net income	63,934	36,324
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization, net of accretion	73,586	74,730
Increase in deferred income taxes	59	16,295
Amortization of deferred compensation	6,569	4,953
Provision for uncollectible accounts	5,650	6,092
Equity in earnings of Vector joint venture	(5,380)	(6,548)
Loss (Gain) on sales of property and equipment, net	(330)	1,782
Loss from equity ventures	-	2,223
Changes in assets and liabilities:		
Receivables	(40,567)	36,838
Prepaid expenses	(1,941)	(7,504)
Accounts payable	56,688	(6,592)
Accrued liabilities, excluding accrued incentive compensation	(16,139)	15,834
Accrued incentive compensation	33,406	(43,713)
Accrued claims costs	(5,371)	(19,614)
Income taxes	7,271	38,293
Employee benefits	(5,166)	(510)
Accrued aircraft lease return provision	(5,002)	(29,186)
Deferred charges and credits	15,419	20,636
Other	(1,824)	8,084
Net Cash Provided by Operating Activities	180,862	148,417
Investing Activities		
Capital expenditures	(47,963)	(65,305)
Software expenditures	(7,143)	(7,665)
Proceeds from sales of property and equipment, net	7,771	4,554
Net Cash Used in Investing Activities	(47,335)	(68,416)

Financing Activities		
Net proceeds from issuance of long-term debt	292,587	2,156
Net repayment of long-term debt, guarantees and capital leases	(142,998)	(12,219)
Proceeds from exercise of stock options	17,055	1,805
Payments of common dividends	(10,050)	(9,911)
Payments of preferred dividends	(5,004)	(5,124)
Net Cash Provided by (Used in) Financing Activities	151,590	(23,293)
Net Cash Provided by Continuing Operations	285,117	56,708
Net Cash Provided by (Used in) Discontinued Operations	(955)	206
Increase in Cash and Cash Equivalents	284,162	56,914
Cash and Cash Equivalents, End of Period	$605,622	$327,318
Supplemental Disclosure		
Cash Paid (Refunded) for income taxes, net	$31,813	$(32,275)
Cash Paid for interest, net of amounts capitalized	18,377	18,285

The accompanying notes are an integral part of these statements.

CNF INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Principal Accounting Policies

Basis of Presentation

Pursuant to the rules and regulations of the Securities and Exchange Commission, the accompanying consolidated financial statements of CNF Inc. and its wholly owned subsidiaries ("CNF") have been prepared by CNF, without audit by independent public accountants. In the opinion of management, the consolidated financial statements include all normal recurring adjustments necessary to present fairly the information required to be set forth therein. Certain information and note disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted from these statements pursuant to such rules and regulations and, accordingly, should be read in conjunction with the consolidated financial statements included in CNF's 2003 Annual Report on Form 10-K.

Earnings per Share ("EPS")

Basic EPS is computed by dividing reported net income available to common shareholders by the weighted-average common shares outstanding. Diluted EPS is calculated as follows:

(Dollars in thousands except per share data)	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Earnings:				
Net income available to common shareholders	$ 35,483	$ 16,300	$ 59,890	$ 32,229
Add-backs:				
Dividends on Series B preferred stock, net of replacement funding	343	367	651	691
Interest expense on convertible subordinated debentures, net of trust dividend income (Note 6)	636	954	1,590	--
	$ 36,462	$ 17,621	$ 62,131	$ 32,920
Shares:				
Weighted-average common shares outstanding	50,319,659	49,494,145	50,075,246	49,445,348
Stock options	941,041	386,228	762,311	437,610
Series B preferred stock	3,539,705	4,121,814	3,539,705	4,121,814
Convertible subordinated debentures (Note 6)	2,083,333	3,125,000	2,604,167	--
	56,883,738	57,127,187	56,981,429	54,004,772
Diluted earnings per share	$ 0.64	$ 0.31	$ 1.09	$ 0.61

For the three and six months ended June 30, 2004, diluted shares reflect the effect of CNF's redemption in June 2004 of its convertible subordinated debentures, as more fully discussed in Note 6, "Debt."

For the six months ended June 30, 2003, the convertible subordinated debentures were anti-dilutive. As a result, the assumed shares and related add-back to net income available to common shareholders under the if-converted method have been excluded from the calculation of diluted EPS. If the securities had been dilutive, the assumed shares from the convertible subordinated debentures under the if-converted method would have been 3,125,000 shares for the six months ended June 30, 2003.

Stock-Based Compensation

Officers and non-employee directors have been granted options under CNF's stock option plans to purchase common stock of CNF at prices equal to the market value of the stock on the date of grant. CNF accounts for stock-based compensation utilizing the intrinsic value method in accordance with the provisions of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees." Accordingly, no compensation expense is recognized for fixed option plans because the exercise prices of employee stock options equal or exceed the market prices of the underlying stock on the dates of grant.

The following table sets forth the effect on net income and earnings per share if CNF had applied the fair-value based method and recognition provisions of SFAS 123, " Accounting for Stock-Based Compensation," to stock-based compensation:

(Dollars in thousands except per share data)	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Net income available to common shareholders, as reported	$ 35,483	$ 16,300	$ 59,890	$ 32,229
Additional compensation cost, net of tax, that would have been included in net income if the fair-value method had been applied	(1,927)	(2,238)	(3,934)	(4,452)
Adjusted net income available to common shareholders as if the fair-value method had been applied	$ 33,556	$ 14,062	$ 55,956	$ 27,777
Earnings per share:				
Basic:				
As reported	$ 0.71	$ 0.33	$ 1.20	$ 0.65
Adjusted	$ 0.67	$ 0.28	$ 1.12	$ 0.56
Diluted:				
As reported	$ 0.64	$ 0.31	$ 1.09	$ 0.61
Adjusted	$ 0.61	$ 0.27	$ 1.02	$ 0.53

These effects of applying SFAS 123 may not be indicative of future amounts.

Foreign Currency

CNF recognizes deferred taxes to reflect the effect of temporary differences between tax and book accounting on the translation of foreign subsidiary financial statements. Based on expectations in certain tax jurisdictions, CNF re-evaluated its assumptions regarding the repatriation of foreign earnings in the first quarter of 2004. CNF will no longer assume that past and future earnings of foreign subsidiaries are indefinitely reinvested. Accordingly, CNF in the first quarter of 2004 recorded a deferred tax asset of $9.4 million to recognize the associated tax effect of the accumulated foreign currency translation adjustment.

New Accounting Standards

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 that all special-purpose entities be designated as either a voting-interest entity or a variable-interest entity

("VIE"). A VIE is an entity for which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the VIE to finance its activities without additional subordinated financial support from other parties. A VIE is required to be consolidated by its primary beneficiary if it does not effectively disperse risks among parties involved. The primary beneficiary of a VIE is the party that absorbs a majority of the VIE's expected losses or receives a majority of its expected residual returns.

The implementation of FIN 46 was required for periods beginning after June 15, 2003. However, in October 2003, the FASB deferred the effective date for applying FIN 46 to VIEs created before February 1, 2003 until the end of the first interim period ending after December 15, 2003. In December 2003, the FASB revised FIN 46 ("FIN 46R") to incorporate certain revisions, including the requirement to disregard certain rights in determining whether an entity is the primary beneficiary in a VIE. Under FIN 46R, CNF was not the primary beneficiary of CNF Trust 1 (the "Trust"), a wholly owned subsidiary,

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and CNF was therefore required to deconsolidate the Trust effective in the quarter ended March 31, 2004. Accordingly, CNF's 5% convertible subordinated debentures held by the Trust, which were redeemed by CNF on June 1, 2004, were included in long-term debt at March 31, 2004, and prior periods were restated to reflect adoption of FIN 46R, as more fully discussed in Note 6, "Debt."

Reclassification

Certain amounts in the prior-period financial statements have been reclassified to conform to the current-period presentation.

2. Reporting Segments

CNF discloses segment information in the manner in which the components are organized for making operating decisions, assessing performance and allocating resources. CNF's principal businesses consist of Con-Way Transportation Services ("Con-Way") and Menlo Worldwide. For financial reporting purposes, CNF is divided into five reporting segments. The operating results of Con-Way are reported as one reporting segment while Menlo Worldwide is divided into three reporting segments: Menlo Worldwide Forwarding, Menlo Worldwide Logistics ("Logistics"), and Menlo Worldwide Other. Also, certain corporate activities and the results of Road Systems, a trailer manufacturer, are reported in the CNF Other reporting segment.

The Menlo Worldwide Forwarding ("Forwarding") segment consists of the combined operating results of Menlo Worldwide Forwarding, Inc. ("MWF") and its subsidiaries, Menlo Worldwide Expedite!, Inc. and a portion of the operations of Emery Worldwide Airlines, Inc. ("EWA"), which ceased air carrier operations in December 2001.

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Financial Data

Management evaluates segment performance primarily based on revenue

and operating income (loss); therefore, other non-operating items, consisting primarily of interest income or expense, are not reported in segment results. Corporate expenses are generally allocated based on measurable services provided to each segment or, for general corporate expenses, based on segment revenue or capital employed. Inter-segment revenue and related operating income have been eliminated to reconcile to consolidated revenue and operating income.

(Dollars in thousands)	Three Months Ended June 30, 2004	Three Months Ended June 30, 2003	Six Months Ended June 30, 2004	Six Months Ended June 30, 2003
Revenues				
Con-Way Transportation Services	$ 657,541	$ 541,446	$ 1,251,385	$ 1,060,554
Menlo Worldwide				
Forwarding	517,376	442,421	1,018,893	888,043
Logistics	265,857	253,012	518,647	494,514
	783,233	695,433	1,537,540	1,382,557
CNF Other	952	26	1,206	35
	$ 1,441,726	$ 1,236,905	$ 2,790,131	$ 2,443,146
Intersegment Revenue Eliminations by Segment				
Con-Way Transportation Services	$ 1,429	$ 146	$ 2,723	$ 256
Menlo Worldwide				
Forwarding	3,324	48	5,871	120
Logistics	--	1,300	--	2,975
	3,324	1,348	5,871	3,095
CNF Other	6,564	5,595	12,664	10,736
	$ 11,317	$ 7,089	$ 21,258	$ 14,087
Revenues before Intersegment Eliminations				
Con-Way Transportation Services	$ 658,970	$ 541,592	$ 1,254,108	$ 1,060,810
Menlo Worldwide				
Forwarding	520,700	442,469	1,024,764	888,163
Logistics	265,857	254,312	518,647	497,489
	786,557	696,781	1,543,411	1,385,652
CNF Other	7,516	5,621	13,870	10,771
Intersegment Revenue Eliminations	(11,317)	(7,089)	(21,258)	(14,087)
	$ 1,441,726	$ 1,236,905	$ 2,790,131	$ 2,443,146
Operating Income (Loss)				
Con-Way Transportation Services	$ 67,136	$ 43,575	$ 118,241	$ 80,767
Menlo Worldwide				
Forwarding	(2,355)	(13,818)	(8,764)	(19,249)
Logistics	6,549	6,303	13,055	12,339
Other	2,988	3,572	5,380	6,548

	7,182	(3,943)	9,671	(362)
CNF Other	(926)	(2,312)	(1,778)	(2,037)
	$ 73,392	$ 37,320	$ 126,134	$ 78,368

Terrorist Attacks

In response to the September 11, 2001 terrorist attacks, the U.S. Congress passed the Air Transportation Safety and System Stabilization Act (the "Act"), a $15 billion emergency economic assistance package intended to mitigate financial losses in the air carrier industry. The legislation provided for $5 billion in direct loss reimbursement and other financial assistance. In March 2002, Forwarding received an initial $11.9 million payment under the Act, resulting in a $9.9 million first-quarter net gain in 2002. In March 2003, Forwarding received a final payment of $7.5 million, resulting in a $7.2 million first-quarter net gain in 2003.

3. Investment in Unconsolidated Joint Venture

Vector SCM ("Vector") is a joint venture formed with General Motors ("GM") in December 2000 for the purpose of providing logistics management services on a global basis for GM, and ultimately for customers in addition to GM. Although Menlo Worldwide, LLC ("MW") owns a majority interest in Vector, MW's portion of Vector's operating results are reported in the Menlo Worldwide Other reporting segment as an equity-method investment based on GM's ability to control certain operating decisions. Vector is organized as a limited liability company that has elected to be taxed as a partnership. Therefore, the joint venture partners are responsible for income taxes applicable to their share of Vector's taxable income. MW's portion of Vector's net income, which is reported as a reduction of operating expenses in the accompanying Statements of Consolidated Income, does not include any provision for income taxes that will be incurred by CNF. MW's undistributed earnings from Vector at June 30, 2004 and December 31, 2003, before provision for CNF's related parent income taxes, was $28.0 million and $22.6 million, respectively.

Vector participates in CNF's centralized cash management system, and, consequently, Vector's domestic trade accounts payable are paid by CNF and settled through Vector's affiliate accounts with CNF. In addition, excess cash balances in Vector's bank accounts, if any, are invested by CNF and settled through affiliate accounts, which earn interest income based on a rate earned by CNF's cash-equivalent investments. As a result of Vector's excess cash invested by CNF, Vector's affiliate receivable from CNF as of June 30, 2004 and December 31, 2003 was $21.0 million and $16.0 million, respectively.

As required by the Vector Agreements, CNF provides Vector with a $20 million line of credit for Vector's working capital and capital expenditure requirements. Under the credit facility, which matures on December 13, 2005, Vector may obtain loans with an annual interest rate based on the rate CNF pays under its $385 million revolving credit facility. CNF provides a portion of its $20 million credit commitment to Vector through CNF's guarantee of $7.5 million of uncommitted local currency overdraft facilities available to Vector by international banks. At June 30, 2004, there was no balance outstanding under Vector's uncommitted local currency overdraft facilities and no

borrowings were directly payable to CNF. At December 31, 2003, Vector owed $5.8 million under the uncommitted local currency overdraft facilities and no borrowings were directly payable to CNF.

CNF's capital transactions with Vector, including cash advances to and from Vector under CNF's centralized cash management system and credit facility described above, are reported as adjustments to MW's investment in Vector in Deferred Charges and Other Assets in CNF's Consolidated Balance Sheets.

4. Employee Benefit Plans

Effective in 2004, CNF adopted the interim disclosure provisions of SFAS No. 132R, "Employers' Disclosure about Pensions and Other Postretirement Benefits, an Amendment of FASB Statements No. 87, 88 and 106 and a Revision of FASB Statement No. 132." The revised statement requires the disclosure of the components of the net periodic benefit expense recognized in interim periods, which is summarized in the tables below.

	Defined Benefit Pension Plans			
	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2004	2003	2004	2003
Service cost - benefits earned during the quarter	$ 12,083	$ 10,966	$ 27,474	$ 21,931
Interest cost on benefit obligation	12,445	12,495	28,297	24,989
Expected return on plan assets	(12,227)	(10,391)	(27,802)	(20,782)
Net amortization and deferral	1,677	2,268	3,814	4,539
Net periodic benefit expense	$ 13,978	$ 15,338	$ 31,783	$ 30,677

CNF previously disclosed in its financial statements for the quarter ended March 31, 2004, that it expects to contribute $90.0 million to its defined benefit pension plans in 2004. As of June 30, 2004, CNF has contributed $40.0 million to those plans.

	Postretirement Medical Plan			
	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2004	2003	2004	2003
Service cost - benefits earned during the quarter	$ 550	$ 457	$ 1,037	$ 913
Interest cost on benefit obligation	1,666	1,384	3,143	2,768
Net amortization and deferral	79	65	149	131

Net periodic benefit expense	$ 2,295	$ 1,906	$ 4,329	$ 3,812

In December 2003, the Medicare Prescription Drug Improvement and Modernization Act of 2003 (the "Act") was enacted in the U.S. The Act introduced a prescription drug benefit under Medicare, as well as a federal subsidy to sponsors of retiree health benefit plans that provide a prescription drug benefit that is at least actuarially equivalent to Medicare's prescription drug benefit. In January and May 2004, the FASB issued FASB Staff Position No. 106-1 and 106-2, "Accounting and Disclosure Requirements Related to the Medicare Prescription Drug, Improvement and Modernization Act of 2003" ("FSP 106-1" and "FSP 106-2").

Under FSP 106-2, CNF concluded that its postretirement medical plan provided an actuarially equivalent benefit and recognized the Act's effect retrospectively to the date of enactment. CNF's adoption of FSP 106-2 resulted in a $4.9 million reduction to its projected postretirement benefit obligation, which will be recognized as a reduction to its net periodic postretirement benefit expense in future periods when costs are subsidized under the Act. The effect of adoption of FSP 106-2 on CNF's financial condition, results of operations and cash flows for the three and six months ended June 30, 2004 was not significant.

5. Comprehensive Income

Comprehensive income, which is a measure of all changes in equity except those resulting from investments by owners and distributions to owners, was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands)	2004	2003	2004	2003
Net income	$ 37,505	$ 18,369	$ 63,934	$ 36,324
Other comprehensive income (loss):				
Realized gain on marketable securities	(1,833)	--	(2,044)	--
Change in fair value of cash flow hedge	--	101	--	194
Foreign currency translation adjustment (Note 1)	(1,741)	3,420	8,118	3,438
	(3,574)	3,521	6,074	3,632
Comprehensive income	$ 33,931	21,890	70,008	39,956

The following is a summary of the components of Accumulated Other Comprehensive Loss, net of tax:

June 30, December 31,

(Dollars in thousands)	2004	2003
Unrealized gain on marketable securities	$ --	$ 2,044
Accumulated foreign currency translation adjustments (Note 1)	(11,221)	(19,339)
Minimum pension liability adjustment	(19,628)	(19,628)
Accumulated other comprehensive loss	$ (30,849)	(36,923)

6. Debt

Convertible Subordinated Debentures

On June 1, 2004, CNF redeemed $128.9 million aggregate principal amount of its 5% Convertible Subordinated Debentures due 2012 (the "Convertible Debentures"). The Convertible Debentures were redeemable for cash on or after June 1, 2000 at a price equal to 103.125% of the principal amount, declining annually to par if redeemed on or after June 1, 2005. CNF Trust 1 (the "Trust"), a trust wholly owned by CNF, applied the proceeds from the redemption of the Convertible Debentures to redeem CNF's $3.9 million interest in the common stock of the Trust and $125 million of Term Convertible Securities, Series A ("TECONS"), which the Trust issued to the public in June 1997. In connection with the redemption of the Convertible Debentures, CNF recognized $2.7 million of expenses in the second quarter of 2004 for an early redemption call premium and for the write-off of the unamortized cost of issuing the Convertible Debentures.

Prior to their redemption in June 2004, the Convertible Debentures were reported in long-term debt as the result of CNF's adoption in the first quarter of 2004 of the revised FASB Interpretation No. 46 "Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51" ("FIN 46R"). Under FIN 46R, CNF was not deemed to be the primary beneficiary of the Trust and CNF was therefore required to deconsolidate the Trust effective in the quarter ended March 31, 2004. Prior to adoption of FIN 46R, CNF reported the TECONS as a mezzanine security with cash distributions reported as a non-operating expense. Under FIN 46R, CNF's consolidated financial statements, for all periods presented, reflect the deconsolidation of the Trust. Accordingly, long-term debt and interest expense reflect the obligation and interest cost, respectively, of the Convertible Debentures prior to their redemption. Also, prior to redemption of the Convertible Debentures, CNF's $3.9 million interest in the common securities of the Trust is reported as an investment in Deferred Charges and Other Assets while dividend income on the common securities are reported by CNF as non-operating income.

The TECONS, the Trust, and the Convertible Debentures are more fully discussed in Note 9, "Preferred Securities of Subsidiary Trust," of Item 8, "Financial Statements and Supplementary Data," in CNF's 2003 Annual Report on Form 10-K.

Senior Debentures due 2034

On April 27, 2004, CNF issued $300 million of 6.70% Senior Debentures due 2034 in a private placement with exchange rights for proceeds of $292.6 million, net of a $7.4 million discount. In connection with the

issuance of the Senior Debentures, CNF capitalized $2.6 million of underwriting fees and $0.3 million of related debt costs in the second quarter, which will be amortized until maturity in 2034. CNF used a portion of the proceeds to redeem $128.9 million of CNF's Convertible Debentures on June 1, 2004, as discussed above. CNF intends to use the remaining proceeds to repurchase from time to time or pay at maturity, $100 million of 7.35% Notes due in June 2005, and for working capital and general corporate purposes.

On July 27, 2004, CNF completed the exchange of registered senior debentures (the "Senior Debentures") for the debentures issued in the private placement. The Senior Debentures bear interest at the rate of 6.70% per year, payable semi-annually on May 1 and November 1 of each year, beginning on November 1, 2004. CNF may redeem the Senior Debentures, in whole or in part, on not less than 30 nor more than 60 days' notice, at a redemption price equal to the greater of (1) the principal amount being redeemed, or (2) the sum of the present values of the remaining scheduled payments of principal and interest on the Senior Debentures being redeemed, discounted at the redemption date on a semiannual basis at the Treasury rate payable on an equivalent debenture plus 35 basis points. The Senior Debentures were issued under an indenture that restricts CNF's ability, with certain exceptions, to incur debt secured by liens.

Thrift and Stock Plan Notes

CNF guarantees the notes issued by CNF's Thrift and Stock Plan ("TASP"), as more fully discussed in Note 6, "Debt and Other Financing Arrangements," of Item 8, "Financial Statements and Supplementary Data," included in CNF's 2003 Annual Report on Form 10-K.

As of June 30, 2004, there was $27.7 million aggregate principal amount of Series A TASP 6.00% notes outstanding and $62.0 million of Series B TASP 8.54% notes outstanding. Holders of the Series B notes issued by CNF's TASP have the right to require CNF to repurchase those notes if, among other things, both Moody's and Standard & Poor's have publicly rated CNF's long-term senior debt at less than investment grade unless, within 45 days, CNF shall have obtained, through a guarantee, letter of credit or other permitted credit enhancement or otherwise, a credit rating for such notes of at least "A" from Moody's or Standard & Poor's (or another nationally recognized rating agency selected by the holders of such notes) and shall maintain a rating on such notes of "A" or better thereafter.

Following CNF's issuance of debentures in April 2004, as described above, Moody's and Standard & Poors affirmed their investment-grade ratings on CNF's senior unsecured debt. Also, Moody's upgraded its outlook to "stable" from "negative."

7. Restructuring Plans

2001 Restructuring Plan

In June 2001, Forwarding began an operational restructuring to align it with management's estimates of future business prospects for domestic heavy air freight and address changes in market conditions. CNF announced in December 2001 that Forwarding would utilize aircraft

operated by other air carriers instead of EWA operating its own fleet of aircraft, and that EWA would permanently cease air carrier operations. As a result, EWA terminated the employment of all of its pilots and crew members. Those pilots and crew members are represented by the Air Line Pilots Association ("ALPA") union under a collective bargaining agreement. Subsequently, ALPA filed a grievance on behalf of the pilots and crew members protesting the cessation of EWA's air carrier operations and Forwarding's use of other air carriers. The ALPA matters are the subject of litigation in U.S. District Court and, depending on the outcome of that litigation, may be subject to binding arbitration. Based on CNF's current evaluation, management believes that it has provided for its estimated exposure related to the ALPA matters. However, there can be no assurance in this regard as CNF cannot predict with certainty the ultimate outcome of these matters.

Forwarding's restructuring reserves decreased to $34.7 million at June 30, 2004 from $34.8 million at December 31, 2003, primarily due to payments of restructuring-related obligations, partially offset by proceeds from sales of aircraft equipment. No aircraft remained under lease as of June 30, 2004. Restructuring reserves at June 30, 2004 consisted primarily of CNF's estimated exposure related to the labor matters described above, as well as other estimated remaining restructuring-related obligations.

Refer to Note 3, "Restructuring Plans," of Item 8, "Financial Statements and Supplementary Data," included in CNF's 2003 Annual Report on Form 10-K for a more detailed discussion of Forwarding's 2001 restructuring plan.

2003 Restructuring Plan

In response to continued declines in North American air freight revenue, Forwarding continued restructuring its operations in the fourth quarter of 2003, primarily to reduce the costs of its North American freight service center network. Under the restructuring plan, nine service centers were closed in markets for which Forwarding believes it can utilize cartage agents to transport customer shipments more cost effectively. In connection with the restructuring plan, Forwarding recognized a $7.8 million charge in the fourth quarter of 2003, primarily for the accrual of future lease payments on closed facilities and employee termination costs. Forwarding's reserves related to the 2003 restructuring plan declined to $2.9 million at June 30, 2004, from $6.6 million at December 31, 2003, due to cash payments related to employee terminations and lease payments on closed facilities. These payments are reflected in Forwarding's cash flows when paid but are not included in Forwarding's operating expenses as these costs were accrued in connection with the restructuring charge. In addition to actions taken in connection with the restructuring charge, Forwarding's restructuring plan also included the renegotiation of contracts with third-party cartage agents and other service providers.

8. Commitments and Contingencies

Spin-Off of CFC

On December 2, 1996, CNF completed the spin-off of Consolidated Freightways Corporation ("CFC") to CNF's shareholders. CFC was, at the

time of the spin-off, and remains a party to certain multiemployer pension plans covering some of its current and former employees. The cessation of its U.S. operations will result in CFC's "complete withdrawal" (within the meaning of applicable federal law) from these multiemployer plans, at which point it will become obligated, under federal law, to pay its share of any unfunded vested benefits under those plans.

It is possible that the trustees of CFC's multiemployer pension plans may assert claims that CNF is liable for amounts owing to the plans as a result of CFC's withdrawal from those plans and, if so, there can be no assurance that those claims would not be material. CNF has received requests for information regarding the spin-off of CFC from representatives from some of the pension funds, and, in accordance with federal law, CNF has responded to those requests. Under federal law, representatives of CFC's multiemployer plans are entitled to request such information to assist them in determining whether they believe any basis exists for asserting a claim against CNF.

Based on advice of legal counsel and its knowledge of the facts, CNF believes that it would ultimately prevail if any such claims were made, although there can be no assurance in this regard. CNF believes that the amount of those claims, if asserted, could be material, and a judgment against CNF for all or a significant part of these claims could have a material adverse effect on CNF's financial condition, cash flow and results of operations.

Prior to the enactment in April 2004 of the Pension Funding Equity Act of 2004, if the multiemployer funds had asserted such claims against CNF, CNF would have had a statutory obligation to make cash payments to the funds prior to any arbitral or judicial decisions on the funds' determinations. Under the facts related to the CFC withdrawals and the law in effect after enactment of the Pension Funding Equity Act of 2004, CNF would no longer be required to make such payments to the multiemployer funds unless and until final decisions in arbitration proceedings, or in court, upheld the funds' determinations.

As a result of the matters discussed above, CNF can provide no assurance that matters relating to the spin-off of CFC and CFC's bankruptcy will not have a material adverse effect on CNF's financial condition, cash flows or results of operations.

Other

CNF is a defendant in various lawsuits incidental to its businesses. It is the opinion of management that the ultimate outcome of these actions will not have a material impact on CNF's financial condition, cash flows, or results of operations.

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

Management's Discussion and Analysis of Financial Condition and Results of Operations (referred to as "Management's Discussion and Analysis") is intended to assist in the understanding and assessment of the principal factors affecting the results of operations, liquidity and capital resources, as well as the critical accounting policies of CNF and its subsidiaries. This discussion and analysis should be read in

conjunction with the information included in CNF's 2003 Annual Report on Form 10-K.

CNF provides supply chain management services for commercial and industrial shipments by land, air and sea throughout the world. CNF's principal businesses consist of Con-Way and the Menlo Worldwide group of businesses. However, for financial reporting purposes, CNF is divided into five reporting segments. The operating results of Con-Way, primarily a provider of regional less-than-truckload ("LTL") freight services, are reported as one reporting segment while Menlo Worldwide is divided into three reporting segments: Forwarding, primarily a global provider of air freight and ocean forwarding services; Logistics, a provider of integrated contract logistics solutions; and Menlo Worldwide Other, which consists of Vector, a joint venture with General Motors ("GM") that serves as the lead logistics manager for GM. Also, certain corporate activities and the results of Road Systems, a trailer manufacturer, are reported in the separate CNF Other reporting segment.

CNF's operating results are generally expected to depend on the number and weight of shipments transported, the prices received on those shipments, and the mix of services provided to customers, as well as the fixed and variable costs incurred by CNF in providing the services and the ability to manage those costs under changing shipment levels. Con-Way and Forwarding primarily transport shipments through freight service center networks while Logistics and Vector manage the logistics functions of their customers and primarily utilize third-party transportation providers for the movement of customer shipments.

RESULTS OF OPERATIONS

CONSOLIDATED RESULTS

CNF in the second quarter of 2004 earned net income available to common shareholders of $35.5 million ($0.64 per diluted share), more than double the $16.3 million ($0.31 per diluted share) earned in last year's second quarter. Net income available to common shareholders in the first half of 2004 was $59.9 million ($1.09 per diluted share), an 85.8% increase from $32.2 million ($0.61 per diluted share) earned in the first half of 2003, which included a $7.2 million pre-tax net gain ($4.4 million after-tax or $0.08 per diluted share) from a payment under the Air Transportation Safety and System Stabilization Act. CNF's improved second-quarter and first-half net income in 2004 was primarily due to higher operating income, partially offset by an increase in other net non-operating expenses.

The following table compares operating results (dollars in thousands, except per share amounts) for the three and six months ended June 30:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Revenues	$ 1,441,726	$ 1,236,905	$ 2,790,131	$ 2,443,146
Operating Income	73,392	37,320	126,134	78,368
Net Income Available to Common Shareholders	35,483	16,300	59,890	32,229
Diluted Earnings per Share	$ 0.64	$ 0.31	$ 1.09	$ 0.61

Amid improved global economic conditions, CNF's revenue and operating income in the second quarter and first half of 2004 increased from the same prior-year periods as both Con-Way and the Menlo Worldwide group of businesses achieved improved operating results on continued revenue growth. CNF's second-quarter operating income rose 96.7% on a 16.6% increase in revenue while consolidated operating income in the first half of 2004 grew 61.0% on a 14.2% increase in revenue. Significantly higher operating income at Con-Way was due principally to operating leverage and revenue growth while improvement in the collective operating results of the Menlo Worldwide companies was primarily due to reduced operating losses from Forwarding.

Con-Way's operating income grew 54.1% in the second quarter of 2004 to a record $67.1 million and rose 46.4% to $118.2 million in the first half of the year. In 2004, the Menlo Worldwide companies reported second-quarter and first-half operating income of $7.2 million and $9.7 million, respectively, compared to operating losses of $3.9 million and $0.4 million, respectively, in the same periods of 2003. The prior-year first quarter benefited from Forwarding's $7.2 million net gain from a payment under the Stabilization Act. Forwarding accounted for substantially all of the improvement in Menlo Worldwide's operating results in 2004, as it reduced operating losses on growth in both international and North American air freight revenue. In 2004, Logistics reported a 3.9% increase in second-quarter operating income, and in the first half of the year, reported a 5.8% improvement in operating income. Vector's operating income of $3.0 million in the second quarter of 2004 and $5.4 million in the first half of 2004, which declined 16.3% and 17.8% from the respective periods last year, reflects compensation earned under amended agreements with GM, its joint venture partner and customer.

Other net expense increased $4.7 million in the second quarter of 2004 and rose $2.5 million in the first half of 2004, due primarily to increases in interest expense and other net miscellaneous non-operating expenses, partially offset by higher interest income on cash-equivalent investments. Interest expense in the second quarter and first half of 2004 rose $2.9 million and $2.7 million, respectively, due largely to the net effect of financing transactions, including the issuance in May 2004 of 6.7% Senior Debentures and the redemption in June 2004 of 5% Convertible Debentures, as more fully discussed, in Note 6, "Debt" of Item 1, "Financial Statements." In 2004, second-quarter and first-half net increases in other miscellaneous non-operating expenses primarily reflect $2.7 million of costs associated with the redemption of the Convertible Debentures as well as declines in income from the cash-surrender value of corporate-owned life insurance policies, partially offset by a $2.0 million net gain from the sale of securities in the second quarter of 2004 and equity venture losses included in the prior year. In 2003, CNF recognized second-quarter and first-half losses from equity ventures of $0.9 million and $2.2 million, respectively.

CON-WAY TRANSPORTATION SERVICES

The following table compares operating results (dollars in thousands), operating margins, and the percentage increase in selected operating statistics of the Con-Way reporting segment:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Summary of Operating Results				
Revenues	$ 657,541	$ 541,446	$ 1,251,385	$ 1,060,554
Operating Income	67,136	43,575	118,241	80,767
Operating Margin	10.2%	8.0%	9.4%	7.6%

	2004 vs. 2003	2004 vs. 2003
Selected Regional-Carrier Operating Statistics		
Revenue per day	+19.1%	+15.2%
Yield	+2.8	+1.7
Weight per day:		
Less-than-truckload	+13.9	+12.0
Total	+15.8	+13.3

Con-Way's revenue in the second quarter and first half of 2004 rose 21.4% and 18.0%, respectively, from the same periods in 2003 due to higher revenue from Con-Way's regional carriers and continued growth from Con-Way's asset-light businesses, which include Con-Way NOW, Con-Way Logistics, and Con-Way Air Express. Revenue per day from the regional carriers rose 19.1% and 15.2% from the second quarter and

first half of 2003 on a 15.8% and 13.3% increase in weight per day ("weight"), respectively, and a 2.8% and 1.7% increase in revenue per hundredweight ("yield"), respectively. Weight improvement in the second quarter and first half of 2004 was due primarily to comparatively better economic conditions in the U.S., and to a lesser extent, continued consolidation of the LTL industry. Second-quarter and first-half yield in 2004 reflects higher rates, an increase in fuel surcharges and continued growth in higher-rated interregional joint services. Yields in 2004 were adversely affected by a 4.6% and 3.7% increase in second-quarter and first-half weight per shipment, respectively. Rates typically decline when weight per shipment increases, as freight with a higher weight per shipment typically has a lower transportation cost per unit of weight. In the second quarter and first half of 2004, Con-Way's asset-light businesses increased revenue by 62.7% and 76.4%, respectively, from the same periods in 2003. Con-Way defines "asset-light" businesses as those that require a comparatively smaller capital investment than its LTL operations.

Con-Way's second-quarter and first-half operating income in 2004 increased 54.1% and 46.4%, respectively, due primarily to higher revenue from the regional carriers, as well as revenue growth from Con-Way's asset-light businesses, which reduced their collective net operating loss in the second quarter and first half of 2004 by $2.8 million and $5.5 million, respectively, over the same periods in 2003. The improvement in Con-Way's operating margin in the second quarter and first half of 2004 reflects operating leverage, as Con-Way's regional carrier service center network accommodated additional shipments with proportionally smaller cost increases. Second-quarter and first-half operating income in 2004 was affected by employee costs, which rose

9.8% and 12.9%, respectively, due primarily to increases in base salaries, variable compensation, employee headcount and employee benefits.

In June 2004, Con-Way announced the formation of a new operating company, Con-Way Truckload ("CTL"), that is scheduled to begin operations in the first quarter of 2005. The new company will serve Con-Way's three regional LTL carriers by providing linehaul service on full loads of LTL shipments moving in transcontinental lanes and eventually offer the services to other customers. The formation of CTL is expected to allow Con-Way to reduce linehaul expense, and protect service with inter-company operations that operate in tandem with current truckload vendors. CTL will utilize Con-Way's existing infrastructure and administrative support services to minimize the required investment. Con-Way's management expects the new company will allow Con-Way to build a potential truckload revenue base by providing truckload services to its customers, and does not expect that the new operation will have a material effect on CNF's financial condition, results of operations or cash flows as of and for the year ending December 31, 2004.

MENLO WORLDWIDE

For financial reporting purposes, the Menlo Worldwide group is divided into three reporting segments: Forwarding, Logistics, and Menlo Worldwide Other. Vector SCM, a joint venture with GM, is reported in the Menlo Worldwide Other segment as an equity-method investment. In 2004, the Menlo Worldwide group of businesses reported second-quarter operating income of $7.2 million on revenue of $783.2 million, and in the first half of the year, reported operating income of $9.7 million on revenue of $1.54 billion.

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FORWARDING

The following table compares operating results (dollars in thousands), operating margins, and the percentage increase (decrease) in selected operating statistics of the Forwarding reporting segment:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Summary of Operating Results				
Revenues	$ 517,376	$ 442,421	$1,018,893	$ 888,043
Operating Loss (1)	(2,355)	(13,818)	(8,764)	(19,249)
Operating Margin	-0.5%	-3.1%	-0.9%	-2.2%

	2004 vs. 2003	2004 vs. 2003
Selected Air Freight Operating Statistics		
International		
Revenue per day	+22.8%	+18.6%
Weight per day	+20.6	+20.5
Yield	+1.8	-1.6

North America		
Revenue per day	+6.6	+3.6
Weight per day	+7.5	+7.3
Yield	-0.8	-3.5

(1) The six months ended June 30, 2003 included a $7.2 million net gain from a payment under the Air Transportation Safety and System Stabilization Act.

Forwarding's revenue in the second quarter and first half of 2004 rose 16.9% and 14.7% over the respective periods last year, as improved global economic conditions contributed to growth in both international and domestic air freight revenue.
International air freight revenue per day in the second quarter and first half of 2004 increased 22.8% and 18.6%, respectively, over the same periods last year, while domestic airfreight revenue per day grew 6.6% and 3.6% from the same periods of 2003. Forwarding's first quarter of 2004 included one more working day than the same quarter of last year.

International air freight revenue in the second quarter and first half of 2004 rose considerably over the same periods last year due largely to growth in average pounds transported ("weight") per day, which reflects stronger business levels in the Asian, European, and Latin American markets. International yield in the second quarter and first half of 2004 was positively affected by higher fuel-surcharge revenue, but was adversely affected by an increase in the percentage of lower-yield delivery services. The decline in international yield in the first half of 2004 was also due in part to reduced volumes of higher-yield military supply business, which benefited the first quarter of last year. Excluding fuel surcharges, second-quarter international yield in 2004 rose 0.5% over last year while international yield in the first half of the year fell 2.7% from the same period in 2003.

North American air freight revenue in the second quarter and first half of 2004 increased over the same prior-year periods due primarily to an increase in weight, partially offset by a decline in yield. North American yield in the second quarter of 2004 fell 0.8% including the fuel-surcharge revenue and declined 0.6% excluding the effect of fuel surcharges. In the first half of the year, North American yield fell 3.5% with fuel surcharges and declined 4.2% excluding the fuel-surcharge impact.

In 2004, Forwarding reduced its second-quarter operating loss by $11.5 million from last year's second quarter and, in the first half of 2004, reduced its operating loss by $10.5 million from the same period of 2003, which benefited from a $7.2 million net gain from a Stabilization Act payment, as more fully discussed below under " - Terrorist Attacks." Improved second-quarter and first-half operating results in 2004 were achieved principally from growth in air freight revenue. Forwarding's international gross margin as a percentage of international air freight revenue in the second quarter of 2004 was essentially flat compared to the same period last year, but declined in the first half of 2004 compared to the first half of last year. Lower international gross margin percentage in the first half of 2004 was due primarily to reduced volumes of higher-yield military supply business, which benefited gross margins in the first quarter of last year. Second-quarter and first-half operating results in 2004 also reflect higher fuel costs and employee-related expenses. In the second quarter of 2004, Forwarding's fuel surcharge revenue was insufficient to

recover higher fuel costs. Employee costs in the second quarter and first half of 2004 rose 9.5% and 9.6%, respectively, due primarily to increases in employee compensation (including variable compensation and the effect of foreign currency fluctuations) and employee benefits, partially offset by a reduction in employee headcount.

Restructuring Plans

2001 Restructuring Plan

In June 2001, Forwarding began an operational restructuring to align it with management's estimates of future business prospects for domestic heavy air freight and address changes in market conditions. CNF announced in December 2001 that Forwarding would utilize aircraft operated by other air carriers instead of EWA operating its own fleet of aircraft, and that EWA would permanently cease air carrier operations. As a result, EWA terminated the employment of all of its pilots and crew members. Those pilots and crew members are represented by the Air Line Pilots Association ("ALPA") union under a collective bargaining agreement. Subsequently, ALPA filed a grievance on behalf of the pilots and crew members protesting the cessation of EWA's air carrier operations and Forwarding's use of other air carriers. The ALPA matters are the subject of litigation in U.S. District Court and, depending on the outcome of that litigation, may be subject to binding arbitration. Based on CNF's current evaluation, management believes that it has provided for its estimated exposure related to the ALPA matters. However, there can be no assurance in this regard as CNF cannot predict with certainty the ultimate outcome of these matters.

Forwarding's restructuring reserves decreased to $34.7 million at June 30, 2004 from $34.8 million at December 31, 2003, primarily due to payments of restructuring-related obligations, partially offset by proceeds from sales of aircraft and equipment. No aircraft remained under lease as of June 30, 2004. Restructuring reserves at June 30, 2004 consisted primarily of CNF's estimated exposure related to the labor matters described above, as well as other estimated remaining restructuring-related obligations.

Refer to Note 3, "Restructuring Plans," of Item 8, "Financial Statements and Supplementary Data," included in CNF's 2003 Annual Report on Form 10-K for a more detailed discussion of Forwarding's 2001 restructuring plan.

2003 Restructuring Plan

In response to continued declines in North American air freight revenue, Forwarding continued restructuring its operations in the fourth quarter of 2003, primarily to reduce the costs of its North American freight service center network. Under the restructuring plan, nine service centers were closed in markets for which Forwarding believes it can utilize cartage agents to transport customer shipments more cost effectively. In connection with the restructuring plan, Forwarding recognized a $7.8 million charge in the fourth quarter of 2003, primarily for the accrual of future lease payments on closed facilities and employee termination costs. Forwarding's reserves related to the 2003 restructuring plan declined to $2.9 million at June 30, 2004, from $6.6 million at December 31, 2003, due to cash payments related to employee terminations and lease payments on closed facilities. These payments are reflected in Forwarding's cash flows when paid but are not included in Forwarding's operating expenses as

these costs were accrued in connection with the restructuring charge. In addition to actions taken in connection with the restructuring charge, Forwarding's restructuring plan also included the renegotiation of contracts with third-party cartage agents and other service providers.

Forwarding's restructuring charges recognized during 2001 and 2003 reflect CNF's estimate of the costs of the related restructuring activities. CNF believes that these estimates are adequate to cover these costs based on information currently available and assumptions management believes are reasonable under the circumstances. However, there can be no assurance that actual costs will not differ from this estimate, and that difference would be recognized as additional expense or income in the period when and if that determination can be made.

Terrorist Attacks

In response to the September 11, 2001 terrorist attacks, the U.S. Congress passed the Air Transportation Safety and System Stabilization Act (the "Act"), a $15 billion emergency economic assistance package intended to mitigate financial losses in the air carrier industry. The legislation provided for $5 billion in direct loss reimbursement and other financial assistance. In March 2002, Forwarding received an $11.9 million payment under the Act, resulting in a $9.9 million first-quarter net gain in 2002. In March 2003, Forwarding received a final payment of $7.5 million, resulting in a $7.2 million first-quarter net gain in 2003.

Forwarding is not able to accurately quantify how the events of September 11, or any subsequent terrorist activities, will affect the global economy, governmental regulation, the air transportation industry, Forwarding's costs of providing air freight services and the demand for Forwarding's air freight services. However, Forwarding believes that any additional security measures that may be required by future regulations could result in additional costs and could have an adverse effect on its operations and service.

LOGISTICS

The following table compares operating results (dollars in thousands) and operating margins of the Logistics reporting segment:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2004	2003	2004	2003
Summary of Operating Results				
Revenues	$ 265,857	$ 253,012	$ 518,647	$ 494,514
Operating Income	6,549	6,303	13,055	12,339
Operating Margin	2.5%	2.5%	2.5%	2.5%

Logistics' revenue in the second quarter and first half of 2004 increased 5.1% and 4.9%, respectively, from the same periods in 2003, due principally to an increase in warehouse management services and a slight increase in carrier management services, partially offset by

lower revenue from contract carriage services. Revenue from carrier management services in the second quarter and first half of 2004 increased slightly despite the loss of a significant customer in the fourth quarter of 2003, a division of a large company that terminated the logistics outsourcing arrangements at many of its divisions. The customer accounted for 7.5% and 8.3% of Logistics' revenue in the second quarter and first half of 2003, respectively, but was among Logistics' lowest-margin accounts. Logistics' operating income in the second quarter and first half of 2004 grew 3.9% and 5.8%, respectively, due largely to higher revenue.

Logistics' carrier-management revenue is attributable to contracts for which Logistics manages the transportation of freight but subcontracts the actual transportation and delivery of products to third parties, which Logistics refers to as purchased transportation. Logistics' net revenue (revenue less purchased transportation) in the second quarter and first half of 2004 was $76.4 million and $152.7 million, respectively, and $73.2 million and $143.4 million in the comparative periods of 2003, respectively.

MENLO WORLDWIDE OTHER

The Menlo Worldwide Other reporting segment consists of the results of Vector, a joint venture formed with GM in December 2000 for the purpose of providing logistics management services on a global basis for GM, and ultimately for customers in addition to GM. Prior to the amendments described below, agreements pertaining to Vector (collectively, "Vector Agreements") provided that Vector would be compensated by sharing in efficiency gains and cost savings achieved through the implementation of Approved Business Cases ("ABCs") and other special projects in GM's North America region and GM's three international regions. An ABC is a project, developed with and approved by GM, aimed at reducing costs, assuming operational responsibilities, and/or achieving operational changes.

In August 2003, the Vector Agreements were amended, primarily to expedite the transition of logistics management services in the North America region from GM to Vector. The amendments changed the compensation principles for GM's North American logistics operations, revised the allocation of Vector's profit between GM and Menlo Worldwide, LLC ("MW"), and modified the formula for the valuation of Vector in the event that MW exercises its Put Right, as described below.

The amendments to the Vector Agreements provide for Vector to be compensated for its management of logistics for all of GM's North America operations rather than through its sharing in efficiency gains and cost savings under individual and separately approved ABCs in North America. In each year of a five-year period retroactive to January 1, 2003, Vector will be compensated with a management fee based on shipment volumes and can earn additional compensation if certain performance criteria are achieved. In accordance with GAAP, compensation under the volume-based management fee will be recognized as vehicles are shipped while performance-based compensation will not be recognized until specified levels of cost savings are achieved,

which will generally not be determinable until the fourth quarter of each contract year. Vector will also be compensated by GM for its

direct and administrative costs in North America, subject to certain limitations.

The amended Vector Agreements also increase MW's allocation of profit and loss from 80% to 85%. Although MW owns a majority equity interest, the operating results of Vector are reported as an equity-method investment based on GM's ability to control certain operating decisions.

Under the Vector Agreements, GM has the right to purchase MW's membership interest in Vector ("Call Right") and MW has the right to require GM to purchase MW's membership interest in Vector ("Put Right"). The Call Right and Put Right are exercisable at the sole discretion of GM and MW, respectively. Under the amended Vector Agreements, the amount payable by GM to MW under the Put Right is based on a mutually agreed-upon estimated value for MW's membership interest as of the contract amendment date and will decline on a straight-line basis over an 8-year period beginning January 1, 2004. Exercise of MW's Put Right or GM's Call Right would result in MW retaining commercialization contracts involving customers other than GM.

Operating income reported by the Menlo Worldwide Other segment declined 16.3% to $3.0 million in the second quarter of 2004 and fell 17.8% to $5.4 million in the first half of 2004. Vector began recognizing compensation in accordance with the amended Vector Agreements in the third quarter of 2003. As a result, operating income in the second quarter and first half of 2004 reflects the recognition of Vector's compensation in accordance with the amended Vector Agreements while operating income in the same periods of the prior year was determined under the compensation principles of the original Vector Agreements, as described above.

In each successive year covered by the amended Vector agreements, management anticipates that performance-based compensation will represent a growing percentage of compensation earned in GM's North America region. Management believes that Vector's long-term profitability growth depends on its ability to grow compensation earned from commercialization activities and from GM's international regions and aftermarket parts-supply operations, which are unaffected by the amended Vector Agreements.

CNF OTHER

The CNF Other segment consists of the results of Road Systems and certain corporate activities. A majority of the revenue from Road Systems was from sales to other CNF subsidiaries. The CNF Other second-quarter operating loss decreased to $0.9 million in 2004 from $2.3 million in 2003, while the $1.8 million operating loss in the first half of 2004 decreased from $2.0 million in 2003. Operating results for the CNF Other segment were affected by the sales of corporate properties, which resulted in a $0.7 million first-quarter net loss in 2004 and a $1.1 million second-quarter net loss in 2003.

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LIQUIDITY AND CAPITAL RESOURCES

In the first six months of 2004, cash and cash equivalents rose to $605.6 million at June 30, 2004, as $180.9 million provided by operating activities and $151.6 million provided by financing

activities significantly exceeded $47.3 million used in investing activities. The excess cash flow from operating and financing activities increased cash and cash equivalents by $284.2 million. Cash provided by financing activities primarily reflects net proceeds of $292.6 million received from the issuance of $300 million of Senior Debentures in May 2004, partially offset by the redemption in June 2004 of its $128.9 million of Convertible Debentures, as more fully discussed below and in Note 6, "Debt" of Item 1, "Financial Statements." CNF's cash flows (dollars in thousands) are summarized in the table below.

	Six Months Ended June 30,	
	2004	2003
Operating Activities		
Net income	$ 63,934	$ 36,324
Non-cash adjustments (1)	80,154	99,527
	144,088	135,851
Changes in assets and liabilities		
Receivables	(40,567)	36,838
Accounts payable and accrued liabilities, excluding accrued incentive compensation	40,549	9,242
Accrued incentive compensation	33,406	(43,713)
Accrued aircraft leases and return provision	(5,002)	(29,186)
Income taxes	7,271	38,293
Employee benefits	(5,166)	(510)
Other	6,283	1,602
	36,774	12,566
Net Cash Provided by Operating Activities	180,862	148,417
Net Cash Used in Investing Activities	(47,335)	(68,416)
Net Cash Provided by (Used in) Financing Activities	151,590	(23,293)
Net Cash Provided by Continuing Operations	285,117	56,708
Net Cash Provided by (Used in) Discontinued Operations	(955)	206
Increase in Cash and Cash Equivalents	$ 284,162	$ 56,914

(1) "Non-cash adjustments" refer to depreciation, amortization, deferred income taxes, provision for uncollectible accounts, equity in earnings of joint venture, and non-cash gains and losses.

CONTINUING OPERATIONS

First-half cash flow from operations in 2004 was $180.9 million compared to $148.4 million in 2003. In the first half of 2004, an increase in receivables used $40.6 million while the collective increase in accounts payable and accrued liabilities (excluding accrued incentive compensation) provided $40.5 million. In the first half of 2004, accrued incentive compensation increased by $33.4 million while the first half of the prior year reflects a $43.7 million reduction. Changes in accrued incentive compensation reflect CNF's payment schedule for its employee incentive plans, under which total incentive compensation earned in an award year is paid to employees with a partial payment in December of the award year and a final payment in February of the next award year. In the first half of 2004, incentive compensation expense accruals exceeded payments, while in the first half of last year, payments for incentive compensation exceeded expense accruals. Cash flow from operations in the first half of 2004 also reflects $5.0 million in payments for restructuring-related aircraft lease payments and return costs while the first half of 2003 includes $29.2 million for that same purpose. Changes in employee benefits in

the first half of 2004 and 2003 reflect the net effect of defined benefit pension plan funding contributions of $40.0 million and $25.0 million, respectively, as described below under "-Defined Benefit Pension Plans," partially offset by expense accruals for CNF's defined benefit plan obligation.

In June and July of 2004, CNF fully liquidated its corporate-owned life insurance policies based on the volatility and insufficiency of returns on the investments. The cash-surrender value of policies liquidated in the second quarter was $40.4 million and the remaining $14.1 million was liquidated subsequent to the second quarter. Prior to June 30, 2004, the cash-surrender value of liquidated policies was reported in Other Assets in CNF's Consolidated Balance Sheets. As of June 30, 2004, the $40.4 million cash-surrender value of policies liquidated in the second quarter was recorded in Other Receivables to reflect amounts receivable by CNF in connection with the liquidation. Since all cash payments for settlement of the investments were received by CNF subsequent to the second quarter of 2004, cash proceeds from the liquidation of the policies are not reflected in CNF's Consolidated Statement of Cash Flows for the six months ended June 30, 2004.

Investing activities in the first half of 2004 used $47.3 million, a decline from $68.4 million used in the first half of last year, due primarily to $17.3 million of capital expenditure reductions, including $12.0 million at Con-Way, $1.9 million at Forwarding, and $1.8 million at Logistics. In the first half of last year, Con-Way invested in $54.7 million of capital acquisitions, primarily for revenue equipment. In 2004, CNF anticipates capital expenditures of between $200 to $215 million, including an estimated $181 million for the acquisition of additional tractor and trailer equipment at Con-Way to accommodate the previously described increase in business levels.

Financing activities in the first six months of 2004 provided cash of $151.6 million compared to cash used in financing activities of $23.3 million in 2003. In April 2004, CNF issued $300 million of 6.70% Senior Debentures due 2034 in a private placement with exchange rights for net proceeds of $292.6 million. CNF used a portion of the proceeds to redeem $128.9 million of CNF's Convertible Debentures on June 1,

2004, as more fully discussed in Note 6, "Debt," of Item 1, "Financial Statements." CNF expects the remaining portion of the proceeds from issuance of the Senior Debentures to pay from time to time or at maturity its $100 million of 7.35% Notes due in June 2005, and for working capital and general corporate purposes. Financing activities in the first six months of 2004 and 2003 also reflect dividend payments and scheduled principal payments for the Thrift and Stock Plan notes guaranteed by CNF.

CNF has a $385 million revolving credit facility that matures on July 3, 2006. The revolving credit facility is available for cash borrowings and for the issuance of letters of credit up to $385 million. At June 30, 2004, no borrowings were outstanding under the facility and $215.1 million of letters of credit were outstanding, leaving $169.9 million of available capacity for additional letters of credit or cash borrowings, subject to compliance with financial covenants and other customary conditions to borrowing. CNF had other uncommitted unsecured credit facilities totaling $134.8 million at June 30, 2004, which are available to support letters of credit, bank guarantees, and overdraft facilities; at that date, a total of $105.1 million was outstanding under these facilities. Of the total letters of credit outstanding at June 30, 2004, $242.7 million provided collateral for CNF workers' compensation and vehicular self-insurance programs. See "Other Matters - Forward-Looking Statements" below, and Note 6, "Debt and Other Financing Arrangements," in Item 8, "Financial Statements and Supplementary Data," of CNF's 2003 Annual Report on Form 10-K for additional information concerning CNF's $385 million credit facility and some of its other debt instruments.

Defined Benefit Pension Plans

CNF periodically reviews the funding status of its defined benefit pension plans for non-contractual employees, and makes contributions from time to time as necessary in order to comply with the funding requirements of the Employee Retirement Income Security Act ("ERISA"). Funding of CNF's defined benefit pensions is based on ERISA-defined measurements rather than the recognition and measurement criteria prescribed by accounting principles generally accepted in the United States ("GAAP").

CNF currently estimates it will contribute $90 million to its defined benefit pension plans in 2004, composed of $40 million paid in the second quarter and $50 million of payments in the third quarter. CNF also made defined benefit pension plan contributions of $75.0 million in 2003 (including $25.0 million in the first half of 2003), $76.2 million in 2002 and $13.1 million in 2001, but made no contributions from 1996 through 2000, due in part to the high rate of return realized on plan assets and for the lack of tax deductibility of funding during that period. There can be no assurance that CNF will not be required to make further cash contributions, which could be substantial, to its defined benefit pension plans in the future.

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Contractual Cash Obligations

CNF's contractual cash obligations as of December 31, 2003 are summarized in CNF's 2003 Annual Report on Form 10-K under Item 7, "Management's Discussion and Analysis - Liquidity and Capital Resources - Contractual Cash Obligations." In the first half of 2004, there have been no material changes in CNF's contractual cash obligations outside

the ordinary course of business, except for CNF's issuance of the Senior Debentures in April 2004 and the redemption of its Convertible Debentures in June 2004. These financing transactions, as well as the effect of CNF's adoption of FIN 46R, are more fully discussed above and in Note 6, "Debt," of Item 1, "Financial Statements."

Other

CNF's debt-to-capital ratio increased to 47.9% at June 30, 2004 from 45.3% at December 31, 2003 due primarily to the net effect of the second-quarter financing transactions described above, partially offset by growth in retained earnings resulting from net income.

DISCONTINUED OPERATIONS

On December 2, 1996, CNF completed the spin-off of Consolidated Freightways Corporation ("CFC") to CNF's shareholders. CFC withdrew in 2002 from certain multiemployer pension funds, thereby incurring withdrawal liabilities to such funds. Prior to enactment in April 2004 of the Pension Funding Equity Act of 2004, if the multiemployer funds had asserted claims against CNF for such liabilities, CNF would have had a statutory obligation to make cash payments to the funds prior to any arbitral or judicial decisions on the funds' determinations. Under the facts relating to the CFC withdrawals and the law in effect after enactment of the Pension Funding Equity Act of 2004, CNF would no longer be required to make such payments to the multiemployer funds unless and until final decisions in arbitration proceedings, or in court, upheld the funds' determination. Refer to Note 8, "Commitments and Contingencies," of Item 1, "Financial Statements."

OTHER MATTERS

ESTIMATES AND CRITICAL ACCOUNTING POLICIES

CNF makes estimates and assumptions when preparing its financial statements in conformity with accounting principles generally accepted in the United States. These estimates and assumptions affect the amounts reported in the accompanying financial statements and notes thereto. Actual results could differ from those estimates. CNF's most critical accounting policies upon which management bases estimates are described below.

Self-Insurance Reserves

CNF uses a combination of insurance and self-insurance programs to provide for the potential liabilities for medical, casualty, liability, vehicular, cargo and workers' compensation claims. Liabilities associated with the risks that are retained by CNF are estimated, in part, by considering historical claims experience, medical costs, demographic factors, severity factors and other assumptions. The undiscounted estimated accruals for these liabilities could be significantly affected if actual costs differ from these assumptions and historical trends.

Income Taxes

In establishing its deferred income tax assets and liabilities, CNF makes judgments and interpretations based on the enacted tax laws and published tax guidance that are applicable to its operations. CNF records deferred tax assets and liabilities and periodically evaluates the need for a valuation allowance to reduce deferred tax assets to realizable amounts. The likelihood of a material change in CNF's expected realization of these assets is dependent on future taxable income, its ability to use foreign tax credit carry forwards and carry backs, final U.S. and foreign tax settlements, and the effectiveness of its tax planning strategies in the various relevant jurisdictions. CNF is also subject to examination of its income tax returns for multiple years by the IRS and other tax authorities. CNF periodically assesses the likelihood of adverse outcomes resulting from these examinations to determine the adequacy of its provision and related accruals for income taxes.

Restructuring Reserves

The restructuring charges recognized in 2003 and 2001 were based on significant estimates and assumptions made by management. Refer to the "Menlo Worldwide - Forwarding - Restructuring Plans" section under "Results of Operations" above for a description of the significant assumptions used.

Uncollectible Accounts Receivable

CNF and its subsidiaries report accounts receivable at net realizable value and provide an allowance for uncollectible accounts when collection is considered doubtful. Con-Way and Forwarding provide for uncollectible accounts based on various judgments and assumptions, including revenue levels, historical loss experience, and composition of outstanding accounts receivable. Logistics, based on the size and nature of its client base, performs a frequent and periodic evaluation of its customers' creditworthiness and accounts receivable portfolio and recognizes expense from uncollectible accounts when losses are both probable and estimable.

Defined Benefit Pension Plans

CNF has defined benefit pension plans that cover non-contractual employees in the United States. The amount recognized as pension expense and the accrued pension liability depend upon a number of assumptions and factors, the most significant being the discount rate used to measure the present value of pension obligations, the assumed rate of return on plan assets, which are both affected by economic conditions, market fluctuations, and rate of compensation increase. CNF adjusts its discount rate periodically by taking into account changes in high-quality corporate bond yields and the guidance of its outside actuaries. CNF adjusts its assumed rate of return on plan assets based on historic returns of the plan assets and current market expectations.

CNF used a 6.75% discount rate for purposes of calculating its 2003 pension expense, but used a 6.25% discount rate for calculating its 2003 year-end pension liability and its 2004 pension expense, due primarily to declines in high-quality corporate bond yields in 2003.

By way of example, if all other factors were held constant, a 0.5% decline in the discount rate would have an estimated $6 million

increase in 2004 annual pension expense. CNF used an assumed rate of return on plan assets of 9.0% in 2003 and will assume the same rate for 2004. Using year-end plan asset values, a 0.5% decline in the assumed rate of return on plan assets would have an estimated $3 million increase in 2004 annual pension expense.

The determination of CNF's accrued pension benefit cost includes an unrecognized actuarial loss that results from the cumulative difference between estimated and actual values for the year-end projected pension benefit obligation and the fair value of plan assets. Under GAAP, any portion of the unrecognized actuarial loss or gain that exceeds ten percent of the greater of the projected benefit obligation or fair value of plan assets must be amortized as an expense over the average service period for employees, approximately thirteen years for CNF. Lower amortization of the unrecognized actuarial loss decreases the annual pension expense in 2004 by approximately $1 million from annual pension expense in 2003.

Goodwill and Other Long-Lived Assets

SFAS 142, "Goodwill and Other Intangible Assets" specifies that goodwill and indefinite-lived intangible assets will not be amortized but instead will be subject to an annual impairment test. On an annual basis in the fourth quarter and between annual tests in certain circumstances, CNF utilizes a third-party independent valuation consultant to perform an impairment test of goodwill associated with the Forwarding reporting segment. Based on an impairment test as of December 31, 2003, which assumed improving cash flows, CNF was not required to record a charge for goodwill impairment.

Consistent with SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets," CNF performs an impairment analysis of long-lived assets (other than goodwill or intangible assets) whenever circumstances indicate that the carrying amount may not be recoverable.

In assessing the recoverability of goodwill and other long-lived assets, CNF must make various assumptions regarding estimated future cash flows and other factors in determining the fair values of the respective assets. If these estimates or their related assumptions change in the future, CNF may be required to record impairment charges for goodwill or other long-lived assets in future periods. Any such resulting impairment charges could have a material adverse effect on CNF's financial condition or results of operations, including potentially triggering downgrades of debt instruments. See "- Forward-Looking Statements" below, and Note 6, "Debt and Other Financing Arrangements," in Item 8, "Financial Statements and Supplementary Data" of CNF's 2003 Annual Report on Form 10-K."

CYCLICALITY AND SEASONALITY

CNF's businesses operate in industries that are affected directly by general economic conditions and seasonal fluctuations, both of which affect demand for transportation services. In the trucking and air freight industries, for a typical year, the months of September and October usually have the highest business levels while the months of December, January and February usually have the lowest business levels.

BUSINESS INTERRUPTION

Although the operations of CNF's subsidiaries are largely decentralized, Forwarding maintains a major hub operation at the Dayton International Airport in Dayton, Ohio. While CNF currently maintains

property and business interruption insurance covering Forwarding's operations at the Dayton hub, its insurance policies contain limits for certain causes of loss, including but not limited to earthquake and flood. Such policies do not insure against property loss or business interruption resulting from a terrorist act. Accordingly, there can be no assurance that this insurance coverage will be sufficient. As a result, a major property loss or sustained interruption in the business operations at the Dayton hub, whether due to terrorist activities or otherwise, could have a material adverse effect on CNF's financial condition, cash flows, and results of operations.

In addition, CNF and its subsidiaries rely on CNF Service Company for the performance of shared administrative and technology services in the conduct of their businesses. CNF's centralized computer facilities and its administrative and technology employees are located at the Administrative and Technology ("AdTech") Center in Portland, Oregon. Although CNF maintains backup systems and has disaster recovery processes and procedures in place, a sustained interruption in the operation of these facilities, whether due to terrorist activities, earthquakes, floods or otherwise, could have a material adverse effect on CNF's financial condition, cash flows, and results of operations.

HOMELAND SECURITY

CNF is subject to compliance with cargo security and transportation regulations issued by the Transportation Security Administration and by the Department of Homeland Security. CNF is not able to accurately predict how new governmental regulation will affect the transportation industry. However, CNF believes that any additional security measures that may be required by future regulations could result in additional costs and could have an adverse effect on its ability to serve customers and on its financial condition, cash flows and results of operations.

EMPLOYEES

Most of the workforce of CNF and its subsidiaries is not affiliated with labor unions. Consequently, CNF believes that the operations of its subsidiaries have significant advantages over comparable unionized competitors (particularly in the trucking industry) in providing reliable and cost-competitive customer services, including greater efficiency and flexibility. There can be no assurance that CNF's subsidiaries will be able to maintain their current advantages over certain of their competitors.

NEW ACCOUNTING STANDARDS

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 that all special-purpose entities be designated as either a voting-interest entity or a variable-interest entity ("VIE"). A VIE is an entity for which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the VIE to finance its activities without additional subordinated financial support from other parties. A VIE is required to be consolidated by its primary beneficiary if it does not effectively disperse risks among parties involved. The primary beneficiary of a VIE is the party that absorbs a majority of the VIE's

expected losses or receives a majority of its expected residual returns.

The implementation of FIN 46 was required for periods beginning after June 15, 2003. However, in October 2003, the FASB deferred the effective date for applying FIN 46 to VIEs created before February 1, 2003 until the end of the first interim period ending after December 15, 2003. In December 2003, the FASB revised FIN 46 ("FIN 46R") to incorporate certain revisions, including the requirement to disregard certain rights in determining whether an entity is the primary beneficiary in a VIE. Under FIN 46R, CNF was not the primary beneficiary of CNF Trust 1 (the "Trust"), a wholly owned subsidiary, and CNF was therefore required to deconsolidate the Trust effective in the quarter ended March 31, 2004. Accordingly, CNF's 5% Convertible Debentures held by the Trust, which were redeemed by CNF on June 1, 2004, were included in long-term debt at March 31, 2004, and prior periods were restated to reflect adoption of FIN 46R, as more fully discussed in Note 6, "Debt" of Item 1, "Financial Statements."

FORWARD-LOOKING STATEMENTS

Certain statements included herein constitute "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended, and are subject to a number of risks and uncertainties, and should not be relied upon as predictions of future events. All statements other than statements of historical fact are forward-looking statements, including any projections of earnings, revenues, weight, yield, volumes, income or other financial or operating items, any statements of the plans, strategies, expectations or objectives of CNF or its management for future operations or other future items, any statements concerning proposed new products or services, any statements regarding CNF's estimated future contributions to pension plans, any statements as to the adequacy of reserves, any statements regarding the outcome of any claims that may be brought against CNF by CFC's multi-employer pension plans or any statements regarding future economic conditions or performance, any statements regarding the outcome of legal and other claims and proceedings against CNF; any statements of estimates or belief and any statements or assumptions underlying the foregoing.

Certain such forward-looking statements can be identified by the use of forward-looking terminology such as "believes," "expects," "may," "will," "should," "seeks," "approximately," "intends," "plans," "estimates" or "anticipates" or the negative of those terms or other variations of those terms or comparable terminology or by discussions of strategy, plans or intentions. Such forward-looking statements are necessarily dependent on assumptions, data and methods that may be incorrect or imprecise and there can be no assurance that they will be realized. In that regard, the following factors, among others and in addition to the matters discussed elsewhere in this document and other reports and documents filed by CNF with the Securities and Exchange

Commission, could cause actual results and other matters to differ materially from those discussed in such forward-looking statements:

- changes in general business and economic conditions, including the global economy;

- the creditworthiness of CNF's customers and their ability to pay

for services rendered;

- increasing competition and pricing pressure;
- changes in fuel prices;
- the effects of the cessation of EWA's air carrier operations; the possibility of additional unusual charges and other costs and expenses relating to Forwarding's operations;
- the possibility that CNF may, from time to time, be required to record impairment charges for goodwill and other long-lived assets;
- the possibility of defaults under CNF's $385 million credit agreement and other debt instruments, including defaults resulting from additional unusual charges or from any costs or expenses that CNF may incur, and the possibility that CNF may be required to repay certain indebtedness in the event that the ratings assigned to its long-term senior debt by credit rating agencies are reduced;
- labor matters, including the grievance by furloughed pilots and crew members, renegotiations of labor contracts, labor organizing activities, work stoppages or strikes; enforcement of and changes in governmental regulations, including the effects of new regulations issued by the Department of Homeland Security;
- environmental and tax matters;
- the February 2000 crash of an EWA aircraft and related litigation;
- and matters relating to CNF's 1996 spin-off of CFC, including the possibility that CFC's multi-employer pension plans may assert claims against CNF, that CNF may not prevail in those proceedings and may not have the financial resources necessary to satisfy amounts payable to those plans, and matters relating to CNF's defined benefit pension plans.

As a result of the foregoing, no assurance can be given as to future financial condition, cash flows, or results of operations. See Note 8, "Commitments and Contingencies" in Item 1, "Financial Statements."

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

CNF is exposed to a variety of market risks, including the effects of interest rates, commodity prices, foreign currency exchange rates and credit risk. CNF enters into derivative financial instruments only in circumstances that warrant the hedge of an underlying asset, liability or future cash flow against exposure to some form of interest rate, commodity or currency-related risk. Additionally, the designated hedges should have high correlation to the underlying exposure such that fluctuations in the value of the derivatives offset reciprocal changes in the underlying exposure.

CNF is subject to the effect of interest rate fluctuations in the fair value of its long-term debt and capital lease obligations, as summarized in Item 8, "Financial Statements and Supplementary Data," under Note 6, "Debt and Other Financing Arrangements," and Note 7, "Leases" of CNF's 2003 Annual Report on Form 10-K. In April 2004, CNF

issued $300 million of 6.70% Senior Debentures in a private placement with exchange rights for net proceeds of $292.6 million. CNF used a portion of the proceeds to redeem $128.9 million of CNF's Convertible Debentures on June 1, 2004 as more fully discussed in Note 6, "Debt" of Item 1, "Financial Statements." Given a hypothetical 10% change in interest rates, the increase in fair value of CNF's long-term debt and guarantees at June 30, 2004 would be approximately $36 million.

CNF held two freestanding interest rate swap derivatives at June 30, 2004 that were initially entered into as cash flow hedges to mitigate the effects of interest rate volatility on floating-rate lease payments. In connection with Forwarding's 2001 restructuring plan, hedge accounting was discontinued for these interest rate swaps when EWA settled floating-rate operating leases hedged with the interest rate swaps. At June 30, 2004, CNF had not entered into any material derivative contracts to hedge exposure to commodity prices or foreign currency.

ITEM 4. CONTROLS AND PROCEDURES

(a) Disclosure Controls and Procedures. CNF's management, with the participation of CNF's Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of CNF's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. Based on such evaluation, CNF's Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, CNF's disclosure controls and procedures are effective.

(b) Internal Control Over Financial Reporting. There have not been any changes in CNF's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, CNF's internal control over financial reporting.

PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

Certain legal proceedings of CNF are also discussed in Note 8, "Commitments and Contingencies," of Part 1, Item 1, "Financial Statements."

In 2001, EWA received subpoenas issued by federal grand juries in Massachusetts and the District of Columbia and the USPS Inspector General for documents relating to the Priority Mail contract. EWA cooperated fully and provided the documents requested in those subpoenas. In September 2003, CNF received notice from the United States Attorney's Office for the District of Columbia that EWA is being considered for possible civil action under the False Claims Act for allegedly submitting false invoices to the USPS for payment under the Priority Mail contract. EWA has entered into a tolling agreement with

the government in order to give the parties more time to investigate the allegations. EWA is in the process of conducting its own investigation of the allegations and as a result CNF is currently unable to predict the outcome of this matter. Under the False Claims Act, the government would be entitled to recover treble damages, plus penalties, if a court was to ultimately conclude that EWA knowingly submitted false invoices to the USPS.

On February 16, 2000, a DC-8 cargo aircraft operated by EWA personnel crashed shortly after take-off from Mather Field, near Sacramento, California. The crew of three was killed. The National Transportation Safety Board subsequently determined that the probable cause of the crash was the disconnection of the right elevator control tab due to improper maintenance, but was not able to determine whether the maintenance errors occurred during the most recent heavy maintenance "D" check by an outside vendor or during subsequent maintenance of the aircraft. MWF, EWA and CNF Inc. have been named as defendants in wrongful death lawsuits brought by the families of the three deceased crew members, seeking compensatory and punitive damages. MWF, EWA and CNF Inc. also may be subject to other claims and proceedings relating to the crash, which could include other private lawsuits seeking monetary damages and governmental proceedings. Although MWF, EWA and CNF Inc. maintain insurance that is intended to cover claims that may arise in connection with an airplane crash, there can be no assurance that the insurance will in fact be adequate to cover all possible types of claims. In particular, any claims for punitive damages or any sanctions resulting from possible governmental proceedings would not be covered by insurance.

On December 5, 2001, EWA announced that it would cease operating as an air carrier, and in connection therewith terminated the employment of all pilots and crew members, bringing the total number of terminated employees in 2001 to 800. Those pilots and crew members are represented by the Air Line Pilots Association ("ALPA") under a collective bargaining agreement. Subsequently, ALPA filed a grievance on behalf of the pilots and crew members protesting the cessation of EWA's air carrier operations and Forwarding's use of other air carriers. The ALPA matters are the subject of litigation in U.S. District Court and, depending on the outcome of that litigation, may be subject to binding arbitration. Based on CNF's current evaluation, management believes that it has provided for its estimated exposure related to the ALPA matters. However, CNF cannot predict with certainty the ultimate outcome of these matters.

EWA, MWF, Menlo Worldwide, LLC and CNF Inc. are named as defendants in a lawsuit filed in state court in California by approximately 140 former EWA pilots and crew members. The lawsuit alleges wrongful termination in connection with the termination of EWA's air carrier operations, and seeks $500 million and certain other unspecified damages. CNF believes that the lawsuit's claims are without merit, and intends to vigorously defend the lawsuit.

CNF has become aware of information that Emery Transnational, a Philippines-based joint venture in which MWF may be deemed to be a controlling partner, may be in violation of the Foreign Corrupt Practices Act. CNF is conducting an internal investigation and has notified the Department of Justice and the Securities and Exchange Commission of this matter. CNF will share the results of its internal investigation, when completed, with the appropriate regulatory agencies, and will fully cooperate with any investigations that may be conducted by such regulatory agencies.

Certain current and former officers of CNF, EWA and Forwarding and certain current and former directors of CNF have been named as defendants in a purported shareholder derivative suit filed in September 2003 in California Superior Court for the County of San Mateo. The complaint alleges breach of fiduciary duty, gross mismanagement, waste and abuse of control relating to the management, control and operation of EWA and Forwarding. CNF is named only as a nominal defendant and no relief is sought against it. CNF maintains insurance for the benefit of its officers and directors, and the applicable insurance carriers have been notified of the claims asserted in the lawsuit.

ITEM 6. Exhibits and Reports on Form 8-K

(a) Exhibits

31 Certification of Officers pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32 Certification of Officers pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K

On April 20, 2004, CNF filed a current report on Form 8-K to furnish under Item 12 CNF's press release presenting CNF's results for the three months ended March 31, 2004.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Company (Registrant) has duly caused this Form 10-Q Quarterly Report to be signed on its behalf by the undersigned, thereunto duly authorized.

..

CNF Inc

(Registrant)

August 5, 2004

/s/Chutta Ratnathicam

Chutta Ratnathicam
Senior Vice President and
Chief Financial Officer