

FINANCIAL HIGHLIGHTS
(in thousands, except per share amounts)

	Years ended December 31,		
	2003	2002	2001
Revenue	\$113,245	\$97,156	\$81,402
Net income available to common stockholders	7,375	7,312	4,195
Net income per share	5.30	5.19	2.95
Total assets	83,554	69,548	77,567
Total debt*	31,508	24,755	38,427
Stockholders' equity	29,829	23,136	15,883

* Includes subordinated debentures and redeemable preferred stock

BUSINESS SEGMENTS

The Hallwood Group Incorporated (the "Company") (AMEX:HWG) is a holding company that classifies its primary business operations into two segments; real estate and textile products.

At the direction of the board of directors of the Company's Hallwood Realty, LLC subsidiary, the investment banking firm of Morgan Stanley is actively engaged in a process that may result in the disposition of the Company's entire investment in Hallwood Realty Partners, L.P. There can be no assurance that such a transaction will be consummated.

FINANCING ACTIVITIES

In August 2003, the Company closed an \$8.0 million credit facility with First Bank & Trust, of which \$5.0 million was used to pay a substantial portion of the judgment on remand in the Gotham litigation matter and \$3.0 million was reserved to satisfy a settlement obligation. The facility is expected to be amended in 2004 to fully satisfy the Gotham judgment.

In January 2004, the Company's Brookwood subsidiary amended and restated its credit agreement with Key Bank, which increased the facility to \$22,000,000 and extended the maturity to January 2007.

ENERGY INVESTMENTS

Through March 2004, the Company has invested \$6.1 million in an affiliated, privately-held energy company referred to as Hallwood Energy Corporation ("HEC"). As of the date of this letter, HEC had drilled thirty-six wells in the Barnett Shale Formation of Johnson County, Texas. After constructing an extensive gas gathering system, HEC commenced commercial production in February 2003. Additionally, HEC has completed a commercial salt water disposal well and facility, which went into operation in March 2004 and will serve HEC's disposal needs as well as accommodate disposed water of third parties. HEC anticipates that it could drill in excess of fifty additional wells during 2004. The Company owns approximately 28% of HEC and accounts for its investment using the equity method of accounting.

In January 2004, the Company committed to invest \$1.3 million for an approximate 20% interest in a newly-formed, privately-held partnership, Hallwood Exploration, L.P. Expected activities include 3-D seismic testing and gas exploration in South Louisiana. The Company will account for its investment using the equity method of accounting.

TO OUR STOCKHOLDERS

We are pleased to present the Company's 2003 Annual Report, which includes results for the years ended December 31, 2003, 2002 and 2001. This has been a very successful year for our Company. Our share price increased from approximately \$6 to \$21 per share and reached a high of \$39 per share in February 2004. In addition, the Company withstood the Gotham lawsuit, refinanced its realty investments and improved cash flow from operations. Although the last few years were very difficult, we believe the Company has turned the corner as we prepare to launch additional new business ventures in 2004.

Results of Operations

For the 2003 year, net income was \$7.4 million, or \$5.30 per share (assuming dilution), compared to net income of \$7.4 million, or \$5.19 per share, in 2002 and net income of \$4.2 million, or \$2.95 per share, in 2001. Net income for 2002 and 2001 included \$3.4 million and \$9.8 million, or \$2.41 and \$6.87 per share, respectively, from the discontinued hotel and energy operations.

Income from continuing operations was \$7.4 million, or \$5.30 per share in 2003, compared to income of \$3.4 million, or \$2.38 per share in 2002, and a loss of \$5.5 million, or \$3.89 per share in 2001, on revenue of \$113.2 million, \$97.2 million and \$81.4 million, respectively.

Real Estate

The Company's Hallwood Realty, LLC ("Hallwood Realty") subsidiary is the 1% sole general partner of Dallas-based and AMEX-listed, Hallwood Realty Partners, L.P. ("HRP"), a real estate master limited partnership. The Company's HWG, LLC subsidiary holds a 21% limited partnership interest in HRP.

HRP is engaged in the acquisition, ownership and operation of commercial real estate, and owns fourteen real estate properties in six states containing 5.2 million net rentable square feet. Hallwood Realty is responsible for asset management of HRP and its properties, including the decisions regarding financing, refinancing, acquiring and disposing of properties. In addition, Hallwood Realty provides general operating and administrative services to HRP.

The Company's Hallwood Commercial Real Estate, LLC subsidiary is responsible for property management, leasing and construction supervision for all HRP properties and other properties it manages for third parties.

For calendar year 2003, the real estate segment posted revenues of \$4.6 million, compared to \$7.1 million in 2002 and \$8.5 million in 2001. This business segment reported a loss before taxes of \$855,000 in 2003, compared to income of \$4.6 million in 2002 and income of \$3.2 million in 2001. The 2003 results included litigation expense of \$3.4 million related to the Gotham litigation that was effectively ended in December 2003.

Textile Products

The Company's Brookwood Companies Incorporated subsidiary ("Brookwood") is an integrated textile company focused on woven nylon products. Converting and design operations are conducted at its New York City offices. Through its Rhode Island dyeing and finishing plant and nearby laminating plant, Brookwood develops and produces innovative woven fabrics and related products through specialized finishing, treating and coating processes.

Brookwood is a market leader in its industry, and is seeking to expand its high tech textile businesses to drive sales and profits. It produces laminated fabrics, using its own branded breathable film, including "Storm-Tech®," "Assault®" and "Batt™". In addition, Brookwood markets other consumer branded fibers and fabrics such as "Cordura®" and "Supplex®." During 2003 Brookwood increased its volume as a supplier of specialized fabric to United States military contractors.

Brookwood enjoyed its most profitable year in calendar 2003. The textile products segment posted revenues of \$104.7 million, compared to \$85.9 million in 2002 and \$69.6 million in 2001. This business segment reported income before taxes of \$6.0 million in 2003, compared to \$2.7 million in 2002 and a loss of \$2.1 million in 2001.

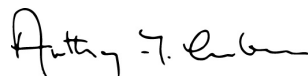
Business Plan

Our goal continues to be to increase stockholder value over the long term by seeking opportunistic investment opportunities.

Acknowledgments

Once again I wish to thank our employees for their continued efforts, and our stockholders, lenders and debentureholders for their continued support.

Sincerely,



Anthony J. Gumbiner
Chairman, President and Chief Executive Officer

April 5, 2004