

HORIZON ORGANIC HOLDING CORP
Form 10-Q
May 14, 2003

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

Form 10-Q

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

For the quarterly period ended March 31, 2003

Commission File No. 000-24337

Horizon Organic Holding Corporation

(a Delaware Corporation)

I.R.S. Employer Identification Number **84-1405007**

6311 Horizon Lane

Longmont, Colorado 80503

(303) 530-2711

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

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

As of April 30, 2003, the registrant had outstanding 10,327,976 shares of its common stock, \$.001 par value per share.

HORIZON ORGANIC HOLDING CORPORATION

Form 10-Q

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

HORIZON ORGANIC HOLDING CORPORATION AND SUBSIDIARIES

Consolidated Balance Sheets

(In thousands, except share amounts)

As of March 31, 2003 (unaudited) and December 31, 2002

| | 2003 | 2002 |
|---|--------|--------|
| Assets | | |
| Current Assets: | | |
| Cash and cash equivalents | \$ 348 | 1,382 |
| Trade accounts receivable, less allowances of \$2,581 in 2003 and \$2,260 in 2002 | 22,954 | 19,978 |
| Inventories | 11,933 | 12,124 |
| Assets held for sale | 28,737 | 29,911 |
| Deferred income tax assets | 277 | 277 |
| Prepaid and other current assets | 4,336 | 5,124 |
| Total current assets | 68,585 | 68,796 |
| Long-term assets held for sale | 1,851 | 1,851 |
| Property, Equipment and Cattle: | | |
| Cattle, net | 1,284 | 1,211 |
| Property and equipment, net | 13,731 | 13,578 |
| Total property, equipment and cattle | 15,015 | 14,789 |
| Other Assets: | | |
| Goodwill, net of accumulated amortization of \$3,054 in 2003 and \$3,054 in 2002 | 26,551 | 27,040 |
| Other intangible assets, net of accumulated amortization of \$5,457 in 2003 and \$5,136 in 2002 | 12,714 | 13,046 |
| Other assets, net | 2,628 | 2,685 |

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| | | | |
|--|----|---------|---------|
| Total other assets | | 41,893 | 42,771 |
| Total Assets | \$ | 127,344 | 128,207 |
| Liabilities and Stockholders Equity | | | |
| Current Liabilities: | | | |
| Current portion of long-term debt | \$ | 26,531 | 26,703 |
| Trade accounts payable | | 11,563 | 10,100 |
| Other accrued expenses | | 8,307 | 8,743 |
| Total current liabilities | | 46,401 | 45,546 |
| Long-Term Liabilities: | | | |
| Long-term debt, less current portion | | 12,779 | 14,110 |
| Deferred income tax liabilities | | 2,887 | 2,898 |
| Total long-term liabilities | | 15,666 | 17,008 |
| Total liabilities | | 62,067 | 62,554 |
| Stockholders Equity: | | | |
| Preferred stock, \$.001 par value, authorized 5,000,000 shares; no shares issued or outstanding | | | |
| Common stock, \$.001 par value; authorized 30,000,000 shares; 10,306,601 and 10,293,127 shares issued and outstanding in 2003 and 2002, respectively | | 10 | 10 |
| Additional paid-in capital | | 61,920 | 61,866 |
| Accumulated other comprehensive income foreign currency translation adjustment | | 1,417 | 2,034 |
| Retained earnings | | 1,930 | 1,743 |
| Total stockholders equity | | 65,277 | 65,653 |
| Total Liabilities and Stockholders Equity | \$ | 127,344 | 128,207 |

See accompanying notes to the unaudited consolidated financial statements.

HORIZON ORGANIC HOLDING CORPORATION AND SUBSIDIARIES

Consolidated Statements of Operations and Comprehensive Income (Loss)

(In thousands, except per share amounts)

For the three months ended March 31, 2003 and 2002

(unaudited)

| | 2003 | 2002 |
|---|-----------|--------|
| Net sales | \$ 51,820 | 42,218 |
| Cost of sales | 35,305 | 28,368 |
| Gross profit | 16,515 | 13,850 |
| Operating expenses: | | |
| Selling | 11,309 | 9,431 |
| General and administrative | 3,196 | 2,520 |
| Intangible asset amortization | 329 | 325 |
| Total operating expenses | 14,834 | 12,276 |
| Operating income | 1,681 | 1,574 |
| Other income (expense), net: | | |
| Interest income | 13 | 11 |
| Interest expense | (6) | (130) |
| Other, net | (56) | (70) |
| Total other expense, net | (49) | (189) |
| Income from continuing operations before income taxes | 1,632 | 1,385 |
| Income tax expense | (637) | (540) |
| Income from continuing operations | 995 | 845 |

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Discontinued operations (Note 4):

| | | | |
|--|----|---------|---------|
| Loss from operations of discontinued Idaho Dairy and Colorado herd (including loss on disposal of \$750 in 2003 and \$2,250 in 2002) | | (1,325) | (3,120) |
| Income tax benefit from discontinued operations | | 517 | 601 |
| Loss from discontinued operations | | (808) | (2,519) |
| Net income (loss) | \$ | 187 | (1,674) |
| Income from continuing operations per basic share | \$ | .10 | .08 |
| Income from continuing operations per diluted share | \$ | .09 | .08 |
| Loss from discontinued operations per basic share | \$ | (.08) | (.25) |
| Loss from discontinued operations per diluted share | \$ | (.08) | (.24) |
| Net income (loss) per basic share | \$ | .02 | (.17) |
| Net income (loss) per diluted share | \$ | .02 | (.16) |
| Weighted average shares outstanding: | | | |
| Basic | | 10,304 | 10,143 |
| Diluted | | 10,575 | 10,545 |
| Comprehensive income (loss): | | | |
| Net income (loss) | \$ | 187 | (1,674) |
| Foreign currency translation adjustment | | (617) | (564) |
| Comprehensive loss | \$ | (430) | (2,238) |

See accompanying notes to the unaudited consolidated financial statements.

HORIZON ORGANIC HOLDING CORPORATION AND SUBSIDIARIES

Consolidated Statements of Cash Flows

(In thousands)

For the three months ended March 31, 2003 and 2002

(unaudited)

| | 2003 | 2002 |
|---|---------|---------|
| Cash flows from operating activities: | | |
| Net income (loss) | \$ 187 | (1,674) |
| Adjustments to reconcile net income (loss) to net cash from operating activities: | | |
| Loss from discontinued operations, net of income taxes | 351 | 531 |
| Loss from anticipated sale of Idaho Dairy and Colorado herd, net of income taxes | 458 | 1,988 |
| Depreciation and amortization | 984 | 939 |
| Loss on sale of cattle and equipment | 134 | 28 |
| Deferred income taxes | | 12 |
| Noncash payments for director services | 20 | 9 |
| Changes in operating assets and liabilities: | | |
| Trade accounts receivable | (3,058) | 875 |
| Inventories | 176 | 518 |
| Prepaid and other current assets | 743 | (1,014) |
| Other assets | (9) | 8 |
| Trade accounts payable | 1,517 | (227) |
| Other accrued expenses | (381) | (71) |
| Net cash provided by operating activities | 1,122 | 1,922 |
| Cash flows from investing activities: | | |
| Net cash generated by (used in) discontinued operations | 364 | (112) |
| Purchases of property and equipment | (851) | (435) |
| Proceeds from equipment sales | 29 | 21 |
| Purchases of cattle | (227) | (216) |
| Proceeds from cattle sales | 68 | 81 |
| Other assets | (45) | (28) |

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| | | |
|--|---------|---------|
| Net cash used in investing activities | (662) | (689) |
| Cash flows from financing activities: | | |
| Repayments of long-term line of credit | (300) | (1,550) |
| Repayments of long-term debt, other than line of credit | (1,197) | (232) |
| Proceeds from exercise of stock options | 34 | 143 |
| Net cash used in financing activities | (1,463) | (1,639) |
| Effect of exchange rate changes on cash | (31) | (53) |
| Net decrease in cash and cash equivalents | (1,034) | (459) |
| Cash and cash equivalents at beginning of period | 1,382 | 3,534 |
| Cash and cash equivalents at end of period | \$ 348 | 3,075 |
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the period for interest, including \$417 and \$431 included in/ allocated to discontinued operations for the three months ended March 31, 2003 and 2002, respectively | \$ 380 | 435 |
| Cash paid during the period for income taxes | \$ 22 | 185 |
| Noncash investing and financing activities: | | |
| Common stock issued to outside directors | \$ 20 | 9 |

See accompanying notes to the unaudited consolidated financial statements.

HORIZON ORGANIC HOLDING CORPORATION AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(unaudited)

1. Basis of Presentation

The accompanying consolidated financial statements have been prepared by Horizon Organic Holding Corporation (the Company) pursuant to the rules and regulations of the Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally accompanying financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such SEC rules and regulations. In management's opinion, all adjustments necessary for a fair presentation of the results of operations for the periods presented have been made and are of a normal and recurring nature. Operating results for the three months ended March 31, 2003 are not necessarily indicative of the results that may be expected for the year ended December 31, 2003.

These consolidated financial statements and accompanying notes should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended December 31, 2002. Certain reclassifications have been made to the 2002 financial statements to conform to the 2003 presentation.

2. Summary of Critical Accounting Policies

The critical accounting policies effective during the three months ended March 31, 2003 were consistent with the critical accounting policies reported in the Company's Form 10-K for the year ended December 31, 2002.

3. Translation of Foreign Currencies

The accounts of the Company's subsidiaries in the United Kingdom were measured using the local currency, which has been designated as the functional currency. Assets and liabilities were translated at the exchange rate in effect at the end of the period. Revenue and expenses were translated at the average exchange rate for the period. Translation adjustments arising from the use of differing exchange rates from period to period were included in comprehensive income (loss) in stockholders' equity.

4. Discontinued Operations

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On March 31, 2002, the Company determined that its Idaho Dairy and Colorado herd met the definition of a disposal group under Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, or SFAS 144. The Company has a plan in place to sell the assets of the Idaho Dairy. The remaining Colorado herd was transferred to the Idaho Dairy by September 30, 2002 in connection with the September 30, 2002 termination of the Dairy Herd Management and Supply Agreement with Aurora Dairy Corporation for the Colorado herd. The Company is negotiating for the sale of the Idaho Dairy, including the transferred Colorado herd, to an experienced dairy farmer and for a long-term supply agreement with the buyer for organic fluid milk at the expected fair market value. The Company is also currently marketing the Idaho Dairy to other prospective qualified buyers. The Company hopes to finalize a transaction by the end of the year, but at this time cannot accurately predict the timing of a closing. Additionally, there can be no assurance that the Company will enter into a definitive agreement with the current or other prospective buyers.

The terms of the anticipated Idaho Dairy sale agreement contemplate a sale price based on net book value, which assumes that depreciation of the cattle and fixed assets would continue from the time the terms were agreed to until the sale closes. Consequently, the resulting price of the Idaho Dairy continues to decrease over time. However, pursuant to SFAS 144, the Company ceased depreciating the related assets as of the measurement date, which was March 31, 2002. Therefore, the net book value of the assets held for sale does not decrease from an increase in accumulated depreciation since the measurement date; but it does decrease for the decrease in anticipated sale price under the contemplated sale agreement subsequent to the measurement date. Because of the resulting differences due to depreciation between the anticipated net book value and the anticipated selling price, the Company recognized an additional loss on disposal of discontinued operations consistent with an additional three months of depreciation of \$0.7 million for the three months ended March 31, 2003. If the Company is unable to finalize the transaction by June 30, 2003, an additional loss on disposal will be recognized by the Company equaling the amount of depreciation that would be expected up to the anticipated date of finalizing the transaction. The Company believes that the contemplated sales price approximates fair market value.

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The financial results from these operations for the current and prior periods are reported as discontinued operations consistent with a disposal group. Included in the loss from discontinued operations, before income taxes and including closing and transaction fees and the decrease in anticipated sale price due to depreciation, for the three months ended March 31, 2003 and March 31, 2002 was an estimated loss on disposal of the discontinued operations of \$0.8 million and \$2.3 million, respectively. The following unaudited financial data presents the combined results of operations for the discontinued operations for the three months ended March 31, 2003 and 2002 (in thousands, except per share amounts):

| | Three Months Ended March 31, | |
|---|---|-------------|
| | 2003 | 2002 |
| Sales | \$ 4,650 | 5,135 |
| Cost of sales excluding cattle depreciation | 3,192 | 3,260 |
| Cattle depreciation | | 494 |
| Gross profit | 1,458 | 1,381 |
| Operating expenses excluding fixed asset depreciation | 1,602 | 1,572 |
| Fixed asset depreciation | | 248 |
| Loss on disposal | 750 | 2,250 |
| Operating loss | (894) | (2,689) |
| Other expense, net | 431 | 431 |
| Loss before income taxes | (1,325) | (3,120) |
| Income tax benefit | 517 | 601 |
| Net loss | \$ (808) | (2,519) |

The following unaudited proforma financial data presents the results of operations for the discontinued operations for the three months ended March 31, 2003 and 2002, if the Company had concluded that its Idaho Dairy operation had not met the definition of a disposal group under SFAS 144 and if the Company had not determined to sell its Idaho Dairy:

| | Three Months Ended March 31, | |
|---|---|-------------|
| | 2003 | 2002 |
| Sales | \$ 4,650 | 5,135 |
| Cost of sales excluding cattle depreciation | 3,192 | 3,260 |
| Cattle depreciation | 476 | 494 |
| Gross profit | 982 | 1,381 |
| Operating expenses excluding fixed asset depreciation | 1,602 | 1,572 |
| Fixed asset depreciation | 247 | 248 |
| Loss on disposal | | |
| Operating loss | (867) | (439) |
| Other expense, net | 431 | 431 |
| Loss before income taxes | (1,298) | (870) |
| Income tax benefit | 506 | 340 |
| Net loss | \$ (792) | (530) |

Differences between the financial results from these operations and the unaudited proforma financial data presented above for the three months ended March 31, 2003 include \$476,000 and \$247,000 in depreciation charges for cattle and fixed assets, respectively, that are included in loss on disposal in the financial results that are instead shown as depreciation in their respective categories in the 2003 unaudited proforma financial data. The financial results include an additional \$27,000 loss on disposal for potential write downs to expected net realizable value as well as an additional income tax benefit of \$11,000. The differences between the financial results and the unaudited proforma financial data for the three months ended March 31, 2002 include a \$2,250,000 loss on disposal consisting of transaction costs and write downs to expected net realizable value, including charges equal to normal depreciation through June 30, 2002 which was the expected transaction close date at March 31, 2002. These costs are not in the unaudited proforma financial data because these costs would not have been incurred if the Company had not determined to sell the Idaho Dairy. In addition, the financial results include an additional income tax benefit of \$261,000, which is not included in the unaudited proforma financial data.

Additionally, approximately \$28.7 million of the Idaho Dairy assets expected to be disposed of, including the transferred Colorado herd, have been classified as current assets held for sale at March 31, 2003. This compares to \$29.9 million at December 31, 2002. Pursuant to SFAS 144, the Company wrote the assets down to the expected disposal value, less costs to sell. The Company expects to use a substantial portion of the proceeds from the sale of assets held for sale to repay outstanding debt.

5. Long-term Debt

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The Company has a \$25.0 million Senior Secured Term Loan with US Bank National Association with a due date of May 31, 2005 and quarterly principal payments. The note bears interest at LIBOR plus a varying margin spread of 1.65% to 3.75%. At March 31, 2003, the interest rate was 3.8% and the outstanding principal balance of this note was \$16.8 million. Interest payments are made in conjunction with LIBOR pricing maturity dates.

The Company has a \$25.0 million credit line facility with US Bank which has been extended for six months. The credit line is collateral-based, has a November 30, 2003 due date and bears interest primarily at LIBOR plus a varying margin spread of 1.65% to 3.75%. At March 31, 2003, the interest rate was 3.8% and the Company had borrowed \$15.9 million against the credit line facility in addition to letter of credit encumbrances of \$2.5 million. Of this \$15.9 million outstanding line of credit balance, \$14.4 million was at an interest rate of 3.8% and \$1.5 million was at an adjustable interest rate of prime plus 0.75%, or 5.0%. We may borrow additional amounts under the revolving line of credit, subject to the terms of the credit agreement, until the facility's maturity date. Total availability under the line of credit pursuant to the borrowing base as defined was \$5.5 million at March 31, 2003. This loan and the Senior Secured Term Loan with US Bank are secured by substantially all of the assets of the Company and contain certain covenants that, among other things, limit the Company's ability to incur additional debt, create liens, pay dividends or enter into certain other transactions, and which require the Company to meet certain financial covenants. The Company is in compliance with these financial covenants.

6. Reportable Segments

The Company has three segments of business, the marketing company, the dairy farm operations and international. The marketing company is responsible for acquiring, processing and marketing organic fluid milk, organic dairy products and organic non-dairy products. The dairy farm operations are responsible for producing farm milk for use by the marketing company in the production of its products. International is the United Kingdom entities responsible for acquiring, processing and marketing organic fluid milk and organic dairy products. The following table sets forth selected segment data for the three months ended March 31, 2003 and 2002 (in thousands):

| | For the three months ended March 31, 2003 | | | | | | | | |
|--|---|-----------------------|-------------------|------------------|---------------|---------------|---------------------------------|--------------------------------------|--------|
| | Marketing | Dairy farm operations | U.S. eliminations | U.S. adjustments | U.S. subtotal | International | U.S. and International subtotal | International eliminations with U.S. | Total |
| Net sales | \$ 42,516 | 717 | (717) | | 42,516 | 9,304 | 51,820 | | 51,820 |
| Cost of sales | 28,166 | 402 | (402) | 12 | 28,178 | 7,127 | 35,305 | | 35,305 |
| Gross profit | 14,350 | 315 | (315) | (12) | 14,338 | 2,177 | 16,515 | | 16,515 |
| Operating expenses excluding intangible asset amortization | 12,782 | 327 | (327) | | 12,782 | 1,723 | 14,505 | | 14,505 |
| Intangible asset amortization | 294 | | | | 294 | 35 | 329 | | 329 |
| Operating income (loss) | 1,274 | (12) | 12 | (12) | 1,262 | 419 | 1,681 | | 1,681 |
| Interest income | 468 | | (72) | (388) | 8 | 5 | 13 | | 13 |
| Interest expense | (43) | (83) | 72 | 388 | 334 | (340) | (6) | | (6) |
| Other, net | (56) | | | | (56) | | (56) | | (56) |
| Income (loss) from continuing operations before income taxes | 1,643 | (95) | 12 | (12) | 1,548 | 84 | 1,632 | | 1,632 |
| Income tax benefit (expense) | (641) | 37 | | | (604) | (33) | (637) | | (637) |
| Income (loss) from continuing operations | 1,002 | (58) | 12 | (12) | 944 | 51 | 995 | | 995 |
| Discontinued operations*: | | | | | | | | | |

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| | | | | | | | | | |
|--|----|---------|--------|----------|---------|---------|---------|---------|------------------|
| Loss from operations of discontinued Idaho Dairy and Colorado herd (including loss on disposal of \$750) | | (1,325) | | | (1,325) | | (1,325) | | (1,325) |
| Income tax benefit from discontinued operations | | 517 | | | 517 | | 517 | | 517 |
| Loss from discontinued operations | | (808) | | | (808) | | (808) | | (808) |
| Net income (loss) | \$ | 1,002 | (866) | 12 | (12) | 136 | 51 | 187 | 187 |
| Segment assets | \$ | 115,970 | 41,748 | (38,769) | | 118,949 | 41,318 | 160,267 | (32,923) 127,344 |

The following additional supplemental information is included above:

| | | | | | | | | | |
|--|----|-----|-------|--|--|-------|-----|-------|-------|
| Continuing Operations: | | | | | | | | | |
| Depreciation and amortization | \$ | 749 | 121 | | | 870 | 114 | 984 | 984 |
| Loss on sale of cattle and equipment | | | 31 | | | 31 | 103 | 134 | 134 |
| Discontinued Operations: | | | | | | | | | |
| Depreciation and amortization | \$ | | | | | | | | |
| Loss on sale of cattle and equipment including loss on sale of the Idaho Dairy | | | 1,260 | | | 1,260 | | 1,260 | 1,260 |
| Company Total: | | | | | | | | | |
| Depreciation and amortization | \$ | 749 | 121 | | | 870 | 114 | 984 | 984 |
| Loss on sale of cattle and equipment including loss on sale of the Idaho Dairy | | | 1,291 | | | 1,291 | 103 | 1,394 | 1,394 |

* Revenue and operating expenses (including loss on sale of the Idaho Dairy) associated with the discontinued dairy farm operations were \$4,650 and \$5,544, respectively.

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For the three months ended March 31, 2002

| | Marketing | Dairy farm operations | U.S. eliminations | U.S. adjustments | U.S. subtotal | International | U.S. and International subtotal | International eliminations with U.S. | Total |
|--|-----------|-----------------------|-------------------|------------------|---------------|---------------|---------------------------------|--------------------------------------|---------|
| Net sales | \$ 34,388 | 781 | (781) | | 34,388 | 7,830 | 42,218 | | 42,218 |
| Cost of sales | 22,522 | 410 | (410) | (140) | 22,382 | 5,986 | 28,368 | | 28,368 |
| Gross profit | 11,866 | 371 | (371) | 140 | 12,006 | 1,844 | 13,850 | | 13,850 |
| Operating expenses excluding intangible asset amortization | 10,616 | 231 | (231) | | 10,616 | 1,334 | 11,951 | | 11,951 |
| Intangible asset amortization | 294 | | | | 294 | 31 | 325 | | 325 |
| Operating income | 956 | 140 | (140) | 140 | 1,096 | 479 | 1,574 | | 1,574 |
| Interest income | 445 | 0 | (71) | (363) | 11 | | 11 | | 11 |
| Interest expense | (120) | (84) | 71 | 363 | 230 | (360) | (130) | | (130) |
| Other, net | (70) | | | | (70) | | (70) | | (70) |
| Income (loss) from continuing operations before income taxes | 1,211 | 57 | (140) | 140 | 1,267 | 119 | 1,385 | | 1,385 |
| Income tax benefit (expense) | (472) | (22) | | | (494) | (46) | (540) | | (540) |
| Income (loss) from continuing operations | 739 | 35 | (140) | 140 | 773 | 73 | 845 | | 845 |
| Discontinued operations: | | | | | | | | | |
| Loss from operations of discontinued Idaho dairy and Colorado herd (including loss on disposal of \$2,250) | | (3,120) | | | (3,120) | | (3,120) | | (3,120) |
| Income tax benefit from discontinued | | 601 | | | 601 | | 601 | | 601 |

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| | | | | | | | | | |
|-----------------------------------|------------|---------|----------|---------|---------|---------|----------|---------|--|
| operations | | | | | | | | | |
| Loss from discontinued operations | | (2,519) | | (2,519) | | (2,519) | | (2,519) | |
| Net income (loss) | \$ 739 | (2,484) | (140) | 140 | (1,746) | 73 | (1,674) | (1,674) | |
| Segment assets | \$ 117,641 | 42,103 | (37,109) | 122,635 | 37,020 | 159,655 | (33,326) | 126,330 | |

The following additional supplemental information is included above:

| | | | | | | | | | |
|--|--------|-------|--|-------|-----|-------|--|-------|--|
| Continuing Operations: | | | | | | | | | |
| Depreciation and amortization | \$ 712 | 113 | | 825 | 114 | 939 | | 939 | |
| Loss on sale of cattle and equipment | | 28 | | 28 | | 28 | | 28 | |
| Discontinued Operations: | | | | | | | | | |
| Depreciation and amortization | \$ | 755 | | 755 | | 755 | | 755 | |
| Loss on sale of cattle and equipment including loss on sale of the Idaho Dairy | | 2,635 | | 2,635 | | 2,635 | | 2,635 | |
| Company Total: | | | | | | | | | |
| Depreciation and amortization | \$ 712 | 868 | | 1,580 | 114 | 1,694 | | 1,694 | |
| Loss on sale of cattle and equipment including loss on sale of the Idaho Dairy | | 2,663 | | 2,663 | | 2,663 | | 2,663 | |

* **Revenue and operating expenses (including loss on sale of the Idaho Dairy) associated with the discontinued dairy farm operations were \$5,135 and \$7,825, respectively.**

7. **Earnings Per Share**

Earnings per share calculations were calculated as follows:

Income from continuing operations

Per basic share. Computed by dividing income from continuing operations by the weighted average number of common shares outstanding.

Per diluted share. Computed by dividing income from continuing operations by the weighted average number of common shares outstanding increased for potentially dilutive common shares outstanding during the period.

Loss from discontinued operations

Per basic share. Computed by dividing loss from discontinued operations by the weighted average number of common shares outstanding.

Per diluted share. Computed by dividing loss from discontinued operations by the weighted average number of common shares outstanding increased for potentially dilutive common shares outstanding during the period.

Net income (loss)

Per basic share. Computed by dividing net income (loss) by the weighted average number of common shares outstanding.

Per diluted share. Computed by dividing net income (loss) by the weighted average number of common shares outstanding increased for potentially dilutive common shares outstanding during the period.

The dilutive effect of stock options and their equivalents was calculated using the treasury stock method.

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Stock options to purchase 522,500 and 40,850 common shares were excluded from the treasury stock method calculations because they were antidilutive during the three months ended March 31, 2003 and March 31, 2002, respectively. The following table sets forth the calculation of earnings (loss) per share for the three months ended March 31, 2003 and 2002 (in thousands, except per share amounts):

| | Three months ended March 31, | |
|---|---------------------------------|---------|
| | 2003 | 2002 |
| Income from continuing operations | \$ 995 | 845 |
| Loss from discontinued operations | \$ (808) | (2,519) |
| Net income (loss) | \$ 187 | (1,674) |
| Common and common equivalent shares outstanding: | | |
| Historical common shares outstanding at beginning of period | 10,293 | 10,126 |
| Weighted average common equivalent shares issued during period | 11 | 17 |
| Weighted average common shares - basic | 10,304 | 10,143 |
| Weighted average common equivalent shares outstanding during period | 271 | 402 |
| Weighted average common shares - diluted | 10,575 | 10,545 |
| Income from continuing operations per basic share | \$.10 | .08 |
| Income from continuing operations per diluted share | \$.09 | .08 |
| Loss from discontinued operations per basic share | \$ (.08) | (.25) |
| Loss from discontinued operations per diluted share | \$ (.08) | (.24) |
| Net income (loss) per basic share | \$.02 | (.17) |
| Net income (loss) per diluted share | \$.02 | (.16) |

(8) Stock Option Plan and Stock Option Agreements

The per share weighted-average fair value of stock options granted during the three months ended March 31, 2003 was \$7.30 on the date of grant using the Black Scholes option-pricing model with the following weighted-average assumptions: no expected dividend yield, expected volatility of 66%, risk free rates ranging from 3.2% to 3.6%, and expected lives of 5 years.

The Company applies the principles in APB Opinion No. 25 in accounting for its Plan and stock option agreements and, accordingly, no compensation cost has been recognized for stock options granted to employees in the accompanying consolidated financial statements. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under SFAS No. 123, the Company's net income (loss) would have been reduced to the pro forma amounts indicated below (in thousands, except per share amounts):

| | Three Months Ended March 31, | |
|---|------------------------------|---------|
| | 2003 | 2002 |
| Net income (loss), as reported | \$ 187 | (1,674) |
| Net loss, pro forma | (481) | (2,291) |
| Net loss per basic and diluted share, pro forma | (.05) | (.23) |

The above pro forma disclosures are not necessarily representative of the effect on the reported net income for future periods because options vest over several years and additional awards are generally made each year.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis should be read in conjunction with our unaudited consolidated financial statements for the three months ended March 31, 2003, and accompanying notes included herein and our Annual Report on Form 10-K for the year ended December 31, 2002. Except for the historical information contained herein, the discussion in this Quarterly Report on Form 10-Q contains certain forward-looking statements that involve risks and uncertainties, such as statements about our plans, objectives, expectations and intentions. We use words such as anticipate, believe, expect, future and intend and similar expressions to identify forward-looking statements. Our actual results could differ materially from those anticipated in these forward-looking statements due to a number of factors. These factors are discussed more fully in our Annual Report on Form 10-K for the fiscal year ended December 31, 2002, in Part I Item 1 under the heading "Risk Factors".

Presentation Overview

We derive revenue primarily through product sales. Net sales include product sales, less product returns, if any, and allowances. Product sales are comprised primarily of sales of organic fluid milk, organic yogurts, organic butters, organic cheeses, organic desserts and organic juices. Revenue is recognized upon transfer of title at the time of shipment to or pickup by a customer.

Cost of sales includes the cost of raw materials including milk purchased from our Idaho Dairy and Colorado herd which are included in discontinued operations, processing fees, inbound freight costs, milk pooling charges and operating income or loss from our Maryland farm operations. The costs of our farm operations include all costs associated with the milk production from our Maryland organic dairy herd which is included in continuing operations. Such costs primarily include organic feed, cattle depreciation, cull losses, payroll, general operating expenses and fixed asset depreciation. We depreciate our Maryland farm assets using the straight-line method over the estimated useful lives, which range from 3 to 27 years. Cattle are depreciated using a straight-line method over five years commencing with their first milking and have a capitalized cost based on purchase price plus pre-production costs.

We purchase most of our fluid milk supply from various organic farmers and cooperatives throughout the U.S. and the U.K. In the U.S., we generally have contracts with our suppliers with terms of one to two years. In the U.K., terms generally range anywhere from three months to five years. Prices are set based on butterfat content and quality testing criteria and most contracts require that we purchase minimum quantities of organic farm milk. If we cannot use the minimum amounts of milk we are required to purchase under these contracts, either as organic milk or in other organic dairy products, we sell the organic milk as conventional milk, which has a lower selling price. We record the difference between our purchase price for organic milk and the conventional milk price received by us in cost of sales.

Processing fees include payments made to our dairy processors and juice processors to process and package raw ingredients into organic milk, dairy and juice products. Inbound freight costs include all raw material inbound shipping costs to the processors. Milk pooling charges include charges incurred by our processors as calculated by the Federal Milk Market Order System. Because the pooling charge assessments are received from the Market Administrators one month in arrears, we adjust the prior month's estimates to actual amounts charged.

Gross profit includes net sales less cost of sales.

Selling expenses consist of all expenses required to market and sell our products, including our direct selling, marketing and distribution costs.

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General and administrative costs are comprised of all costs of operations and corporate support not specifically included in any of the items above. Most of our depreciation expense is included in this line item.

Intangible assets amortization includes the amortization of intangible assets acquired from the Juniper Valley brand purchase in 1998, The Organic Cow of Vermont brand purchase in 1999 and certain intangibles acquired from the Meadow Farms acquisition in 2000.

Discontinued operations includes the net costs of our milk production from our Idaho Dairy and Colorado herd which are assets held for sale. Such costs primarily include organic feed, cull losses, payroll, general operating expenses, cattle and fixed asset depreciation prior to triggering discontinued operations, interest expense and expected loss on disposal which includes transaction costs. We ceased depreciating our assets held for sale upon their classification as such and recognized on the measurement date of March 31, 2002 the expected loss on disposal. Prior to the measurement date, we depreciated our Idaho Dairy and Colorado herd assets using the straight-line method over the estimated useful lives, which ranged from 3 to 27 years. Cattle were depreciated using a straight-line method over five years commencing with their first milking and had a capitalized cost based on purchase price plus pre-production costs.

Results of Operations

Three Months Ended March 31, 2003, Compared to Three Months Ended March 31, 2002

Net Sales. Net sales increased by 22.7%, or \$9.6 million, to \$51.8 million for the three months ended March 31, 2003 from \$42.2 million for the comparable period in 2002. Net sales from U.S. operations increased 23.6%, or \$8.1 million, to \$42.5 million from \$34.4 million resulting primarily from increased sales volume to existing customers.

Changes in our U.S. product category sales were as follows:

Fluid Milk

Total fluid milk sales increased 26.8%, or \$6.4 million, to \$30.5 million for the three months ended March 31, 2003 from \$24.1 million for the comparable period in 2002. This increase was primarily due to increased sales volume to existing customers.

Sales of ultra-pasteurized (UP) fluid milk increased 51.3%, or \$6.1 million, to \$18.0 million for the three months ended March 31, 2003 from \$11.9 million for the comparable period in 2002. This increase was primarily due to increased sales volume to existing customers.

Sales of traditional pasteurized fluid milk increased 2.8%, or \$0.3 million, to \$12.5 million for the three months ended March 31, 2003 from \$12.2 million for the comparable period in 2002. This increase was primarily due to increased sales volume to existing customers.

As a result of these shifts, our fluid milk product line mix shifted to 41% traditional pasteurized fluid milk for the three months ended March 31, 2003 from 51% for the comparable period in 2002.

Other Dairy

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Sales of our other dairy products increased 21.6%, or \$1.9 million, to \$10.7 million for the three months ended March 31, 2003 from \$8.8 million for the comparable period in 2002, due primarily to increased sales volume of our butter, cheese, dessert and foodservice products.

Sales of butter increased 16.0%, or \$0.4 million, to \$2.8 million for the three months ended March 31, 2003 from \$2.4 million for the comparable period in 2002. This increase was primarily due to increased sales volume to existing customers.

Sales of cheese increased 31.0%, or \$0.4 million, to \$1.7 million for the three months ended March 31, 2003 from \$1.3 million for the comparable period in 2002. This increase was primarily due to increased sales volume to existing customers.

Sales of industrial products, such as powdered milk and cheeses sold for further processing into finished goods, and of foodservice products, such as single serve milk sold to restaurants, other service providers and club stores, increased 23.2%, or \$0.3 million, to \$1.6 million for the three months ended March 31, 2003 from \$1.3 million for the comparable period in 2002. This increase was primarily the result of our introduction of single-serve milk products into club stores.

Juice

Sales of our juice products decreased 6.3%, or \$0.1 million, to \$1.8 million for the three months ended March 31, 2003 from \$1.9 million for the comparable period in 2002. We believe that this decrease was primarily the result of aggressive pricing on conventional juice, which widened the price gap between conventional and organic juice.

Changes in our International sales were as follows:

Net sales from international operations increased 18.8%, or \$1.5 million, to \$9.3 million for the three months ended March 31, 2003 from \$7.8 million in 2002. Expressed in British pounds, sales increased 5.8%; however, shifts in the exchange rate in the two periods produced the balance of the dollar-denominated increase. This increase was primarily due to increased sales volume to existing customers.

Sales of Rachel's Organic branded products which consist primarily of milk, yogurt, double cream, crème fraiche, and butter increased 66.4%, or \$1.9 million, to \$4.6 million for the three months ended March 31, 2003 from \$2.7 million for the comparable period in 2002. Expressed in British pounds, sales increased 48.2%; however, shifts in the exchange rate in the two periods produced the balance of the dollar-denominated increase. This increase was primarily due to increased sales volume to existing customers.

Cost of Sales and Gross Profit. Cost of sales increased 24.5%, or \$6.9 million, to \$35.3 million for the three months ended March 31, 2003 from \$28.4 million for the comparable period in 2002. The increase in cost of sales was primarily the result of our increased sales. Gross profit increased 19.2%, or \$2.7 million, to \$16.5 million for the three months ended March 31, 2003 from \$13.8 million for the comparable period in 2002. As a percentage of net sales, gross profit decreased to 31.9% for the three months ended March 31, 2003 from 32.8% for the comparable period in 2002. Our gross profit in the U.S. decreased to 33.7% for the three months ended March 31, 2003 from 34.9% for the comparable period in 2002 primarily due to increased processor costs, hauling costs and pooling charges versus the comparable three month period a year ago. Our gross profit in the U.K. decreased to 23.4% for the three months ended March 31, 2003 from 23.6% for the comparable period in 2002. This decrease was primarily the result of the sales product mix versus the comparable three month period a year ago.

Selling Expenses. Selling expenses increased 19.9%, or \$1.9 million, to \$11.3 million for the three months ended March 31, 2003 from \$9.4 million for the comparable period in 2002. This increase was primarily a result of the increased delivery and commission costs associated with the increased U.S. sales. Selling expenses as a percentage of net sales decreased to 21.8% for the three months ended March 31, 2003 from 22.3% for the comparable period in 2002.

General and Administrative Expenses. General and administrative expenses increased 26.8%, or \$0.7 million, to \$3.2 million for the three months ended March 31, 2003 from \$2.5 million for the comparable period in 2002. This increase was primarily due to increased overhead including \$0.2 million for costs associated with a contemplated public equity

financing that we elected not to proceed with due to equity market conditions. As a result, our general and administrative expenses as a percentage of net sales increased to 6.2% in 2003 from 6.0% in 2002.

Intangible Asset Amortization. Amortization expense related to intangible assets was \$0.3 million for the three months ended March 31, 2003, virtually unchanged from the comparable period in 2002.

Other Expense, Net. Other expense, net decreased 74.1%, or \$0.2 million, to \$49,000 for the three months ended March 31, 2003 from \$0.2 million for the comparable period in 2002. The decrease was primarily attributable to a \$6.5 million decrease in our outstanding debt balances and partially attributable to a decrease in the average interest rate on our debt facilities. Our average interest rate on our LIBOR-based debt facilities decreased to 3.9% for the three months ended March 31, 2003 from 4.5% for the comparable period in 2002.

Income Tax Expense. Income tax expense increased \$0.1 million to \$0.6 million for the three months ended March 31, 2003 from \$0.5 million for the comparable period in 2002. Our effective income tax rate was 39.0% for the three months ended March 31, 2003, unchanged from the comparable period in 2002.

Income From Continuing Operations. Income from continuing operations increased \$0.2 million to \$1.0 million for the three months ended March 31, 2003 from \$0.8 million for the comparable period in 2002.

Income from continuing operations for U.S. operations increased \$0.1 million to \$0.9 million for the three months ended March 31, 2003 from \$0.8 million for the comparable period in 2002.

Income from continuing operations for international operations was \$0.1 million for the three months ended March 31, 2003, unchanged from the comparable period in 2002.

Loss From Discontinued Operations. Loss from discontinued operations decreased \$1.7 million to a \$0.8 million loss from discontinued operations for the three months ended March 31, 2003 from a \$2.5 million loss from discontinued operations for the comparable period in 2002. The three months ended March 31, 2003 included losses on disposal of \$0.5 million net of tax and no depreciation as compared to charges for anticipated transaction fees and losses on disposal of \$2.0 million net of tax in addition to \$0.5 million net of tax for depreciation for the three months ended March 31, 2002. The resulting \$2.0 million decreased loss on disposal and depreciation for the three months ended March 31, 2003 from the comparable period in 2002 was partially offset during the three months ended March 31, 2003 by increased operating costs at the Idaho Dairy.

If we had determined that the pending sale of our Idaho Dairy assets, including the transferred Colorado herd, had not met the definition of a disposal group under Statement of Financial Accounting Standards No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, the results of the Idaho Dairy and Colorado herd would have been recorded in continuing operations. Accordingly, for the three months ended March 31, 2003, an operating loss before interest and income taxes of \$867,000 from the Idaho Dairy including the transferred Colorado herd would have been included in cost of sales, thereby increasing our cost of sales which in turn would have decreased our gross profit to \$15.6 million for the three months ended March 31, 2003. For the three months ended March 31, 2002, an operating loss before interest and income taxes of \$439,000 from the Idaho Dairy and Colorado herd would have been included in cost of sales, thereby increasing our cost of sales which in turn would have decreased our gross profit to \$13.4 million for the three months ended March 31, 2002. Additionally, if we had included the Idaho Dairy and Colorado herd operations with continuing operations, our reported net income would have been \$203,000, or \$.02 per basic and diluted share, for the three months ended March 31, 2003, and our reported net income would have been \$315,000, or \$.03 per basic and diluted share, for the three months ended March 31, 2002.

Net Income. Net income increased \$1.9 million to \$0.2 million for the three months ended March 31, 2003 from a net loss of \$1.7 million for the comparable period in 2002.

Net income for U.S. operations increased \$1.8 million to \$0.1 million for the three months ended March 31, 2003 from a net loss of \$1.7 million for the comparable period in 2002. The increase in net income was primarily due to decreased losses on discontinued operations for the three months ended March 31, 2003 as compared to the comparable period for 2002.

Net income for international operations was \$0.1 million for the three months ended March 31, 2003, unchanged from the comparable period in 2002.

Comprehensive Income (Loss). Comprehensive income (loss) increased \$1.8 million to a loss of \$0.4 million for the three months ended March 31, 2003 from a loss of \$2.2 million for the comparable period in 2002. This increase was primarily due to a \$1.9 million increase in net income. We translated our investment in our U.K. subsidiaries from pounds sterling to U.S. dollars at the rate in effect at the end of the period. At March 31, 2003, December 31, 2002, March 31, 2002, and December 31, 2001, the British pound was worth approximately U.S. \$1.575, U.S. \$1.604, U.S. \$1.426 and U.S. \$1.452, respectively.

Liquidity and Capital Resources

We have generally used funds generated from operations, trade payables, bank indebtedness and the sale of equity securities to meet our capital requirements.

Net cash provided by operations was \$1.1 million for the three months ended March 31, 2003, a decrease of \$0.8 million from \$1.9 million for the comparable period in 2002. Cash provided by operations in 2003 was primarily attributable to an increase in trade accounts payable of \$1.5 million and a decrease in prepaid and other current assets of \$0.7 million as well as an increase in income as adjusted by the loss on the anticipated disposal of the Idaho Dairy and Colorado herd, net of income taxes; depreciation and amortization charges; and a decrease in inventories partially offset by primarily increased trade accounts receivable of \$3.1 million. Cash provided by operations in 2002 was primarily attributable to an increase in income as adjusted by the \$2.0 million loss on the anticipated disposal of the Idaho Dairy and Colorado herd, amortization, and depreciation charges along with decreases in inventory and increases in other accrued expenses partially offset by increased prepaid and other current assets.

Net cash used in investing activities was \$0.7 million for the three months ended March 31, 2003, virtually unchanged from the comparable period in 2002. Cash used in investing activities in 2003 was primarily attributable to \$0.8 million used in the purchases of property and equipment, including upgraded desktop computers, net of proceeds from equipment sales. Cash used in investing activities in 2002 was primarily attributable to miscellaneous equipment and milk production equipment.

Net cash used in financing activities was \$1.5 million for the three months ended March 31, 2003, a decrease of \$0.1 million from \$1.6 million for the comparable period in 2002. The cash used in financing activities reflects our pay-downs of term debt and our net pay-downs of our outstanding credit line balance during the three month period ended March 31, 2003 and during the comparable period in 2002.

Our cash and cash equivalents were \$0.3 million at March 31, 2003 and \$3.1 million at March 31, 2002. We have a five year \$25.0 million term loan with US Bank which bears an interest rate of LIBOR plus a variable margin spread ranging from 1.65% to 3.75%. At March 31, 2003, the interest rate was 3.8% and we had an outstanding balance of \$16.8 million. In addition, we have a line of credit with US Bank that provides funding of up to \$25.0 million and bears interest primarily at a rate of LIBOR plus a variable margin spread ranging from 1.65% to 3.75%. At March 31, 2003, we had borrowed \$15.9 million against the credit line facility in addition to credit line encumbrances of \$2.5 million. Of this \$15.9 million outstanding credit line balance, \$14.4 million was at an interest rate of 3.8% and \$1.5 million was at an adjustable interest rate of prime plus 0.75%, or 5.0%. We may borrow additional amounts under the revolving line of credit, subject to the terms of the credit agreement, until the facility's maturity date which has been extended to November 30, 2003. Total availability under the line of credit pursuant to the borrowing base as defined was \$5.5 million at March 31, 2003. We expect to use a substantial portion of the proceeds from the sale of assets held for sale to repay outstanding debt.

We currently anticipate that our available cash resources, funds generated by operations and available credit facilities, will be sufficient to meet our presently anticipated capital needs for the next twelve months, but may be insufficient for cash acquisitions under our corporate development program. If additional funds are required, we may seek additional equity or debt financing. Such financing may not be available to us on terms that are acceptable to us, if at all, or on terms that would not be dilutive to our stockholders.

Critical Accounting Policies

The critical accounting policies effective during the three months ended March 31, 2003 were consistent with the critical accounting policies reported in the Company's Form 10-K for the year ended December 31, 2002.

Effect of Recently Issued Accounting Standards

In April 2002, the FASB issued Statement of Financial Accounting Standards No. 145, *Rescission of FASB Statement No. 4, 44 and 64, Amendment of FASB Statement No. 13, and Technical Corrections*, or SFAS 145. This statement provides guidance on the classification of gains and losses from the extinguishment of debt and on the accounting for certain specified lease transactions. We adopted the provisions of SFAS 145 effective January 1, 2003, and its implementation did not have any material impact on our financial position, results of operations or cash flows.

In June 2002, the FASB issued Statement of Financial Accounting Standards No. 146, *Accounting for Costs Associated with Exit or Disposal Activities*, or SFAS 146, which addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies

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Emerging Issues Task Force (EITF) Issue No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring). Generally, SFAS 146 requires that a liability for a cost associated with an exit or disposal activity be recognized as incurred, whereas EITF Issue No. 94-3 required such a liability to be recognized at the time that an entity committed to an exit plan. We adopted the provisions of SFAS 146 effective January 1, 2003, which is effective for exit or disposal activities that are initiated after December 31, 2002, and its implementation did not have any material impact on our financial position, results of operations or cash flows.

In December 2002, the FASB issued Statement of Financial Accounting Standards No. 148, *Accounting for Stock-Based Compensation Transition and Disclosure*, or SFAS 148. This statement amends FASB Statement No. 123, *Accounting for Stock-Based Compensation*, to provide alternative methods of transition for a voluntary change to the fair value based method of accounting for stock-based employee compensation. This statement also amends the disclosure requirements of Statement 123 to require prominent disclosures in both annual and interim financial statements about the method of accounting for stock-based employee compensation and the effect of the method used on reported results. The provisions of this statement relating to alternative transition methods and annual disclosure requirements are effective for fiscal years ending after December 15, 2002. The provisions of this statement relating to interim financial information are effective for the quarter ending March 31, 2003. The transitional provisions will not have an impact on our financial statements unless we elect to change from the intrinsic value method to the fair value method. We adopted SFAS 148 as of December 31, 2002 and the provisions relating to annual and interim disclosures have changed the manner in which we disclose information regarding stock-based compensation.

In November 2002, the Financial Accounting Standards Board issued FASB Interpretation No. 45, *Guarantors Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*, or FIN 45, which addresses the disclosure to be made by a guarantor in its interim and annual financial statements about its obligations under guarantees. FIN 45 also requires the recognition of a liability by a guarantor at the inception of certain guarantees and requires the guarantor to recognize a liability for the non-contingent component of the guarantee. This is the obligation to stand ready to perform in the event that specified triggering events or conditions occur. The initial measurement of this liability is the fair value of the guarantee at inception. The recognition of the liability is required even if it is not probable that payments will be required under the guarantee or if the guarantee was issued with a premium payment or as part of a transaction with multiple elements. We have adopted the disclosure provisions of FIN 45 as of January 1, 2003, and will apply the recognition and measurement provisions for all guarantees entered into or modified after December 31, 2002. The adoption has no significant impact on our consolidated financial statements.

In January 2003, the Financial Accounting Standards Board issued FASB Interpretation No. 46, *Consolidation of Variable Interest Entities*, or FIN 46. FIN 46 clarifies existing accounting principles related to the preparation of consolidated financial statements when the equity investors in an entity do not have the characteristics of a controlling financial interest or when the equity at risk is not sufficient for the entity to finance its activities without additional subordinated financial support from other parties. FIN 46 requires a company to evaluate all existing arrangements to identify situations where a company has a variable interest (commonly evidenced by a guarantee arrangement or other commitment to provide financial support) in a variable interest entity (commonly a thinly capitalized entity) and further determine when such variable interests require a company to consolidate the variable interest entities' financial statements with its own. We are required to perform this assessment by September 30, 2003 and consolidate any variable interest entities for which we will absorb a majority of the entities' expected losses or receive a majority of the expected residual gains. We do not have investments in variable interest entities that we may be required to consolidate.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Qualitative Market Risk

Market risk refers to the risk that a change in the level of one or more market prices, interest rates, indices, volatilities, correlations or other market factors such as liquidity, will result in losses for a certain financial instrument or group of financial instruments. We occasionally enter into forward financial instruments with major financial institutions to manage and reduce the impact of changes in foreign currency rates. We do not use financial instruments to manage changes in commodity prices and we do not hold or issue financial instruments for trading purposes. Based on the controls in place and the relative size of the financial instruments we enter into, we believe the risks associated with not using these instruments will not have a material adverse effect on our consolidated financial position or results of operations.

Quantitative Market Risk: Value At Risk

Foreign Exchange Contracts. We occasionally enter into forward financial instruments to manage and reduce the impact of changes in foreign currency rates with a financial institution. These instruments are marked-to-market at the end of each month and gains and losses are recorded in the statement of operations.

Interest Rates. At March 31, 2003, we had approximately \$2.8 million of fixed rate long-term debt (including current maturities). The fair value of long-term fixed interest rate debt is subject to interest rate risk. Generally, among other factors including credit ratings, the fair value of fixed interest rate debt will increase as interest rates fall and decrease as interest rates rise. The estimated fair value of our total fixed rate long-term debt with fixed interest rates (including current portion) at March 31, 2003 was \$2.9 million, which was \$0.1 million greater than the carrying value. Fair values were determined primarily from quoted market rates. A full percentage point decrease from prevailing interest rates at March 31, 2003, would result in an estimated increase in fair value of total fixed interest rate long-term debt of approximately \$30,000. Additionally at March 31, 2003, we had approximately \$36.5 million of floating rate long-term debt (including current maturities) subject to interest rate risk. A full percentage point fluctuation in interest rates would result in decreasing or increasing interest expense by approximately \$365,000 over a twelve month period.

Item 4. Controls and Procedures

(a) Evaluation of disclosure controls and procedures. The Company, under the supervision and with the participation of the Company's management, including its Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures [as defined in Rules 240.13a-14(c) and 15d-14(c) under the Securities Exchange Act of 1934 (the Exchange Act)] as of a date within ninety days before the filing date of this quarterly report (the Evaluation Date). Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures were effective for the purposes of recording, processing, summarizing and timely reporting information required to be disclosed by the Company in the reports that it files under the Securities Exchange Act of 1934 and that such information is accumulated and communicated to the Company's management in order to allow timely decisions regarding required disclosure.

(b) Changes in internal controls. There have been no significant changes in the Company's internal controls or in other factors that could significantly affect the Company's disclosure controls and procedures subsequent to the Evaluation Date, nor were there any significant deficiencies or material weaknesses in the Company's internal controls.

PART II - OTHER INFORMATION

Items 1, 2, 3, 4 and 5 of this Part II are either inapplicable or are answered in the negative and are omitted pursuant to the instructions to Part II.

Item 6. Exhibits and Reports on Form 8-K

A) Exhibits

3.1+ Amended and Restated Certificate of Incorporation

3.2+ Amended and Restated Bylaws of the Company

99.1 Certificate of Horizon Organic Holding Corporation's Chief Executive Officer and Chief Financial Officer pursuant to section 906 of the Sarbanes-Oxley Act of 2002

Exhibits identified above are incorporated by reference as follows:

+ Incorporated by reference to Registrant's Registration Statement on Form S-1, No. 333-51465

B) Reports on Form 8-K

None.

SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned thereunto duly authorized.

HORIZON ORGANIC HOLDING CORPORATION

Date: May 14, 2003

/s/ Thomas P. Briggs

Thomas P. Briggs

Senior Vice President, Finance and Administration, Chief Financial
Officer, and Secretary

(principal financial and accounting officer of the Company)

CERTIFICATIONS

I, Charles F. Marcy, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Horizon Organic Holding Corporation;

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

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

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

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

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the Evaluation Date); and

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

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors:

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

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

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

Date: May 14, 2003

/s/ Charles F. Marcy
Charles F. Marcy
President and Chief Executive Officer

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I, Thomas P. Briggs, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Horizon Organic Holding Corporation;

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

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

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

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

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the Evaluation Date); and

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

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors:

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

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

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

Date: May 14, 2003

/s/ Thomas P. Briggs

Thomas P. Briggs

Senior Vice President, Finance and Administration, Chief Financial Officer, and Secretary