TAGLICHBROTHERS
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Research Report – Update

Investors should consider this report as only a single factor in making their investment decision.

Lifeway Foods, Inc.

Rating: Underperform

Howard Halpern

April 27, 2006

LWAY $12.12 - (NasdaqNM)

	FY (12/03)A	FY (12/04)A	FY (12/05)A	*FY (12/06) E*
Revenue (in millions)	$14.9	$16.32	$20.13	***$25.43***
Earnings per share (diluted)*	$0.26	$0.24	$0.30	***$0.34***

52-Week range	$18.17 – $8.06	Fiscal year ends:	December
Shares outstanding a/o 02/28/06	8.396 million	Revenue/shares (TTM)	$2.39
Trading float	2.210 million	Price/Sales (TTM)	5.07X
Insider and institutional ownership	73.7%	Price/Sales (2006)E	4.01X
Tangible Book value/shr a/o 12-31-05	$2.35	Price/Earnings (TTM)	40.4X
Price/Book	5.16X	Price/Earnings (2006)E	35.6X

* All per share figures reflect the 2-1 stock split effective March 9, 2004.

Lifeway Foods, Inc., is a manufacturer of cultured, probiotic and functional food products in the health food industry, and is America's leading supplier of the cultured dairy product known as Kefir. Their products are sold to health conscious consumers through health food stores and to the mass-market consumers through supermarkets. Web site address is: www.kefir.com

Key investment considerations:

We are maintaining our Underperform rating on Lifeway Foods, Inc. (NasdaqNM: LWAY). We continue to believe its shares remain fairly valued based on our current revenue, EBITDA, and EPS estimates.

Investors need to be aware that the Company's Stockholders' Agreement with Danone terminated on December 30, 2005 (according to LWAY's 10-K filing). Investors should be cognizant that the non-compete covenant between Lifeway and Danone also expired. This means competition between them can occur.

According to SEC filings, as of December 31, 2005, Danone owned approximately 20.4% of LWAY's common shares. Since the agreements have expired, Danone could increase its stake or conversely sell its stake in LWAY. Also, direct competition could occur between the companies. At this point in time, investors will just have to watch carefully to see what transpires.

Lifeway Foods reported 2005 revenue of $20.132 million, which was an increase of 23.4% versus $16.319 million in the same period last year. Net income was $2.535 million or $0.30 per diluted share versus $2.052 million or $0.24 per diluted share in 2004.

Based on results during the second half of 2005, first quarter 2006 public guidance issued by Management, and comments made in the Company's 2005 10-K filing, we are adjusting our 2006 revenue estimate to $25.428 million from $25.165 million.

Given our revenue estimate, public statements made by Management, and the potential for productivity improvements, we are increasing our 2006 forecast for net income to $2.893 million or $0.34 per diluted share from $2.660 million or $0.32 per diluted share.

**** Please view our disclaimer located on page 10.***

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The Company

Lifeway Foods, Inc. (NasdaqNM: LWAY) manufactures a cultured dairy beverage called Kefir and also develops Kefir related products at its two manufacturing facilities in Illinois. The Company's distribution of its fifteen Kefir-based products in Illinois is accomplished through approximately 1,200 local stores including major retail chains (i.e., Jewel Food Stores, Dominick's Finer Foods, Treasure Island Food Marts, Whole Foods, and independent retailers), via twelve company owned trucks. Also, over 40 different assorted cream cheese products are distributed under the Cream Cheese Gourmet brand in the Philadelphia metropolitan area. In addition, the Company distributes its products throughout the United States and to some parts of Canada (Ontario and Quebec), utilizing verbal distribution arrangements with a number of distributors. Management believes that verbal arrangements provide the necessary latitude to expand into new markets and establish new relationships on an ongoing basis.

As of December 31, 2005, Danone Foods, Inc., the U.S. subsidiary of Groupe Danone of Paris, France, has a 20.4% ownership interest in Lifeway Foods, Inc. According to the Company's 10-K filing, Lifeway and Danone Foods, Inc. Stockholders' Agreement and non-compete covenant terminated on December 30, 2005. Since the agreements have expired, Danone could increase its stake or conversely sell its stake in LWAY. Also, direct competition could occur between the companies. At this point in time, investors will just have to watch carefully to see what transpires.

<u>*Kefir*</u>

Lifeway Kefir contains ten active "friendly" microorganisms and is probiotic* in nature because it promotes the growth of those microorganisms naturally. The product is a good source of calcium, protein, minerals, and vitamins (i.e. B-complex vitamins) and is highly digestible due to its acidity and enzymes. Kefir is similar to, but distinct from, yogurt. The fermentation process produces a less sour tasting product. Also, less sugar is required; therefore, the product contains fewer calories.

* Probiotics are defined as live cultures consumed for a health benefit. These cultures are comprised of one or more types of bacteria. Probiotic cultures have recently undergone controlled scientific investigations. The results lend some credence to the old folklore that suggests fermented dairy products that contain probiotic cultures are healthful.

Recent Developments

On March 29, 2006, Lifeway announced the launch of ProBugs™, which is for children aged 2-9 and is made with organic whole milk kefir. ProBugs™ comes in two flavors (Sublime Slime Lime™ and Orange Creamy Crawler™), is a certified organic product, and come in packs of four 5-ounce servings. The product has a patented no-spill spout, making it easy for kids to consume, while eliminating messes. ProBugs™ was sampled at the Natural Products Expo West in Anaheim, California. According to Management, the response from retails was overwhelmingly positive. This product will be shipped nationwide during June 2006.

On March 9, 2006, the Company announced its Board of Directors authorized a stock repurchase program. The number of shares authorized to be repurchases is up to 50,000 shares. Under the program, LWAY may repurchase shares in the open market for a one-year period from the date of the first purchase.

On February 1, 2006, LWAY announced distribution of their kefir product to military commissaries that are run by the Defense Commissary Agency headquartered in Fort Lee, Virginia. The first purchase orders from military distributors were shipped during the third week of February 2006. According the Company's CEO, these commissaries constitute the 16th largest grocery retailer in the country with annual sales of approximately $5 billion.

On January 27, 2006, Lifeway announced the addition of Greek Style Kefir. According to Management, the growing popularity of Greek style yogurt was the inspiration to create this new offering.

On December 27, 2005, the Company began distribution to a limited test market of Costco (NasdaqNM: COST) stores in the Midwest region of the U.S. The LowFat Plain Kefir will be resold as a two pack.

Recent Financials

For the twelve-months ended December 31, 2005, versus the twelve-months ended 31, 2004:

- Revenue increased to $20.132 million versus $16.319 million;
- Gross margin decreased to 42.06% versus 44.64%;
- Operating expenses increased to $5.066 million versus $4.334 million;
- EBITDA increased to $4.052 million versus $3.620 million; and
- Net income was $2.548 million or $0.30 per diluted share versus net income of $2.052 million or $0.24 per diluted share.

The year-over-year revenue increase of 23.4% was primarily attributable to increased awareness of the Company’s existing drinkable dairy products (i.e., La Fruta and Kefir). Also, the Company’s acquisition of Ilya’s Farms, Inc. contributed $0.525 million to total revenue from the sale of gourmet cream cheese products, as well as $0.482 million in sales from the distribution of Lifeway’s Kefir and Farmer Cheese products in the tri-state area of PA, NJ, and NY. In addition, during 2005, Lifeway increased its distribution to some of the country’s largest retailer (including Walmart, Target, and Costco), as well as to a healthcare facility.

Gross margin decreased to 42.06% versus 44.64% in the same period last year. While the average cost of milk (the Company’s largest component of cost of goods sold) was similar to last year, the Company was negatively impacted by an 18% increase in the minimum wage in Illinois. According to Management, LWAY intends to offset wage increases by continuing to invest in the automation of its production process. As a consequence of increased shipments of its products, the overall rise in fuel and transportation costs, as well as the rise in other oil related costs (i.e., sugar and plastic) negatively impacted gross margin in 2005. In the Company’s 10-K filing, Management stated its belief that LWAY can offset a portion of the oil related costs by making prudent investments in energy related securities, which will show up in other income.

Operating expenses in 2005 increased by $0.732 million, primarily due to higher utility and fuel costs, advertising expenses, rising insurance and professional fees associated with the Sarbanes-Oxley Act, as well as other regulatory compliance requirements. On a percentage of revenue, operating expenses decreased to 25.17% versus 26.56% in 2005, primarily due to the Company’s revenue growth.

In comparison, Taglich Brothers' estimates called for revenue of $20.260 million and net income of $2.262 million or $0.27 per diluted share.

Balance Sheet as of December 31, 2005

The Company had cash and cash equivalents of $4.354 million and short-term marketable securities of $7.478 million. This compares to cash and cash equivalents of $5.773 million and short-term marketable securities of $6.742 million as of December 31, 2004. Working capital was $14.474 million versus $14.901 million in 2004. The Company’s long-term liabilities stood at $2.903 million, which was an increase from $0.464 million at the end of 2004. The increase in long-term liabilities was primarily related to the purchase of a storage and distribution facility. In order to purchase the facility the Company entered into a $3.0 million five-year note at an interest rate of 5.6%.

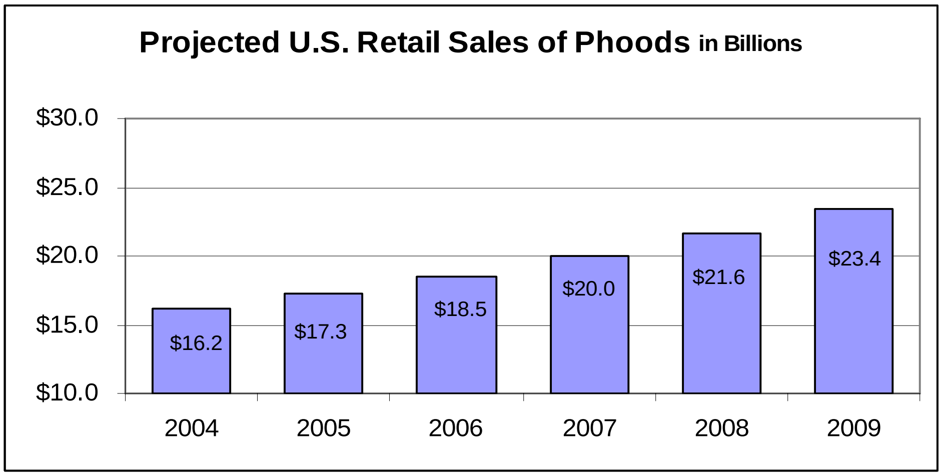
The Company’s portfolio mix of marketable securities (at fair value as of December 31, 2005) consisted of:

- 37.9% fixed income securities; and
- 62.1% in equities and mutual funds.

We believe that LWAY will be able to fund its sales growth from cash on hand and internally generated funds. Management is not aware of any circumstances or trends, which would have a negative impact upon future sales or earnings and that there have been no material fluctuations in the standard seasonal variation of the Company’s business. Investors should be aware that Management continues to explore potential acquisition opportunities in order to boost sales while leveraging the Company’s distribution system in order to consolidate and lower costs.

Market Comment

It is estimated that Lifeway Foods' target market, the functional and probiotic foods segment of the Food Industry, generates annual revenue in excess of $20 billion. In addition, according to an article (January 2005) in the Chemical Market Reporter magazine (a trade publication provides business information for the global chemical market), the U.S. retail sales of phoods and bepherages (terms used for foods and drinks with health benefits) was approximately $16.2 billion in 2004 and is forecast to reach $20 billion by 2007 (stats were from a research report published by Packaged Facts – is a provider of authoritative consumer market research). The following offers some prospective as to the potential future sales trends:



Source: Packaged Facts

In addition, Marketresearch.com (an aggregator of global business intelligence) predicts that by the end of the decade, the U.S. Functional Food Market will approach $30 billion. This would represent approximately 5.5% of the total Food Market. The Nutrition Business Journal (research, publishing and consulting company serving the nutrition, natural products and alternative health care industries) estimates that the Functional Food Market currently represents 3.8% of the total U.S. Food Market.

Outlook/Projections

Management stated in the Company's full year earnings press release on March 29, 2006, that 2005 was a milestone year as public interest for Lifeway's Kefir reached an all time high, as well as the mainstream market beginning to accept all its healthy products. In addition, the Company's CEO continues to see gains in distribution outlets across the country and new product introductions (i.e., ProBugs™ and Greek Style Kefir). The Company's CFO, commented that he was pleased to see improved fourth quarter operating margins to 16.9% versus third quarter operating margins of 14.7%; even though, the Company continues to see an increase in oil related costs such as transportation, utilities, and several raw materials.

On April 5, 2006, Lifeway Foods pre-announced sales for its first quarter ended March 31, 2006, of approximately $6.003 million. This would translate into a weekly sales run rate of approximately $0.460 million, which would be just above the lower end of Taglich Brothers' expected range of $0.450 million to $0.490 million. Taglich Brothers' weekly sale run rate is based primarily on increased orders from existing customers, as well as expanded distribution opportunities. In addition, Management believes the Company's packaging has improved point-of-sale education, as well as heightened visibility among mainstream consumers. While Lifeway continues to market its products through local radio station, newspaper, and magazines advertisements, it also has additional exposure through the Internet, catalog advertising and promotion, in store demonstration throughout the U.S., and participation in various trade shows. Also, a new warehouse facility purchase in 2005, gives the Company added flexibility and the opportunity to expand its product line to include more nonperishable food items.

Based on results during the second half of 2005, first quarter 2006 public guidance by Management, and comments made in the Company's 2005 10-K filing, we are adjusting our 2006 revenue estimate to $25.428 million from $25.165 million. Given our revenue estimate, public statements made by Management, and the potential for productivity improvements made through investments in automation, we are increasing our 2006 forecast for net income to $2.893 million or $0.34 per diluted share from $2.660 million or $0.32 per diluted share. Our forecast incorporates the following:

– A distribution agreement with Target stores;

– A limited test market of LowFat Plain Kefir to Costco stores in the Midwest region of the U.S;

– The average price of milk remaining stabile;

– Investments made to improve productivity through the automation process;

– Higher energy and raw material costs; and

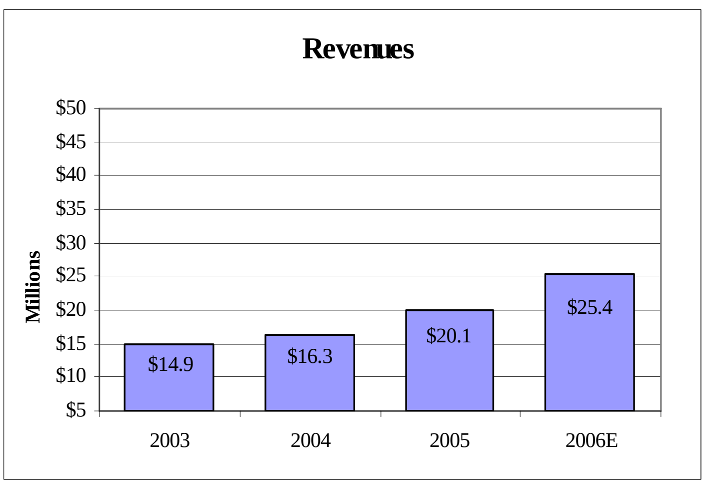
– The continued high cost of being a public company (i.e., insurance, legal, and regulatory compliance).

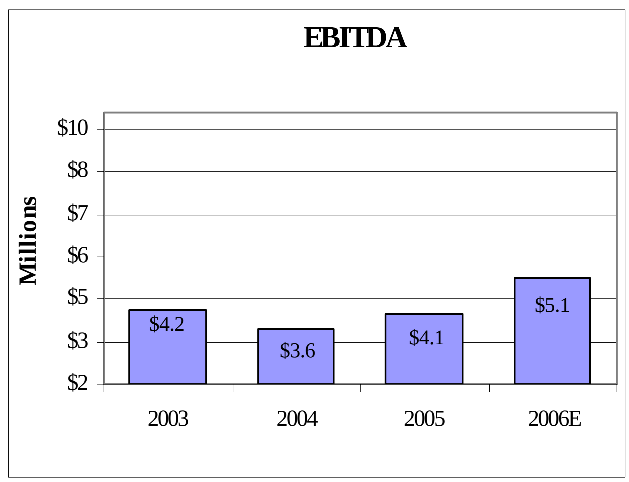
We have adjusted the following from our prior forecast, based on the previously discussed operating trends:

– Gross margins to 42.50% from 42.35%; and

– SG&A expenses, as a percentage of revenues, to 25.03% from 25.43%.

The chart on top of the next page shows our revenue and EBITDA projections:





Source: Company Filings and Taglich Brothers Estimates

Risks

Commodities

The Company's products use raw materials, such as milk, sugar, and fruit from unaffiliated suppliers. Lifeway is not limited or contractually bound to any supplier. The raw and packaging materials purchased by the Company are considered commodity items and are widely available on the open market. If the price of those commodity products were to unexpectedly rise, it could negatively impact margins.

Regulation

Lifeway is subject to regulation by federal, state and local governmental authorities regarding the distribution and sale of food products. Management believes that the Company is currently in compliance with all material government permits, licenses, qualifications, and approvals for its operations; however, there can be no assurance that it will be able to maintain its existing licenses and permits. In addition, the Company believes that it is currently in compliance with all applicable environmental laws.

Also, the products exported to Canada are subject to strict quotas imposed by the Trade Control Policy Division of the Department of Foreign Affairs and International Trade of Canada. Management believes that the Company is in compliance with all applicable Canadian regulations.

Groupe Danone SA Relationship

Investors need to be aware that the Company's Stockholders' Agreement with Danone terminated on December 30, 2005 (according to LWAY's 2005 10-K filing); therefore, investors should be cognizant that the non-compete covenant between Lifeway and Danone also expired.

According to SEC filings, as of December 31, 2005, Danone owned approximately 20.4% of LWAY's common shares. Since the agreements have expired, Danone could increase its stake or conversely sell its stake in LWAY. Also, direct competition could occur between the companies. At this point in time, investors will just have to watch carefully to see what transpires. However, if Danone were to sell its large stake in the Company, it could have a negative effect on LWAY's share price. Additionally, competition between the two companies could increase, which could negatively impact LWAY's operations because of the financial resources of Danone. On the other hand, Danone could increase its stake or even make an offer to purchase the Company at some future point in time.

Legal Issue

On December 4, 2004, a former employee requested a motion for summary judgment on the issue of liability in a lawsuit filed against the Company by a former employee. The motion was granted on February 10, 2005 and on February 18, 2005 the case was referred to a Magistrate Judge for a settlement conference. The cause of action alleges non-payment of overtime wages in violation of federal employment laws. The suit was filed in the U.S. District Court for the Northern District of Illinois on behalf of all employees who were classified as non-exempt during 2001 through 2003. On December 2, 2005, the Company settled the case for approximately $0.095 million.

In addition, Lifeway is from time to time engaged in other litigation matter arising in the ordinary course of business none of which presently is expected to have a material adverse effect on its business results or operations.

Customer Concentration

In 2005, Lifeway's largest customer represented approximately 9% of sales and reflected sales in various regions of the United States outside the Chicago, Illinois metropolitan area.

Corporate Governance

Corporate governance may be an issue facing Lifeway Foods in light of new rules and regulation being issued by government regulatory agencies. This could mean that the Company will eventually be required to hire additional management personnel in order to diversify various operational functions.

Growth Management

LWAY has returned to growing revenues in excess of 20% annually. As a result, the Company will need to meet the challenges associated with growth, such as management of raw materials and increased production staff. If Lifeway Foods is not successful in meeting these challenges, revenue growth may slow in future periods.

Marketable Securities

At December 31, 2005, the fair value of the Company’s marketable securities available for sale was $7.479 million. In the Company’s 10-K filing, Management stated its belief that LWAY can offset a portion of the oil related costs that have been incurred over the last twelve months, by making prudent investments in energy related securities, which will show up in other income. Investors should be aware that investments in energy related securities can be volatile and could have a negative impact on its portfolio if energy prices were to decline.

Federal Reserve

Investors should be aware that if the Federal Reserve continues increasing interest rates (over the last fifteen meetings it has increased rates 25 basis points each time), it is likely to have a negative impact on valuation multiples.

Miscellaneous

The Company’s financial results and equity values are subject to other risks and uncertainties known and unknown, including but not limited to competition, operations, financial markets, regulatory risk, and/or other events. These risks may cause actual results to differ from expected results.

Trading Volume

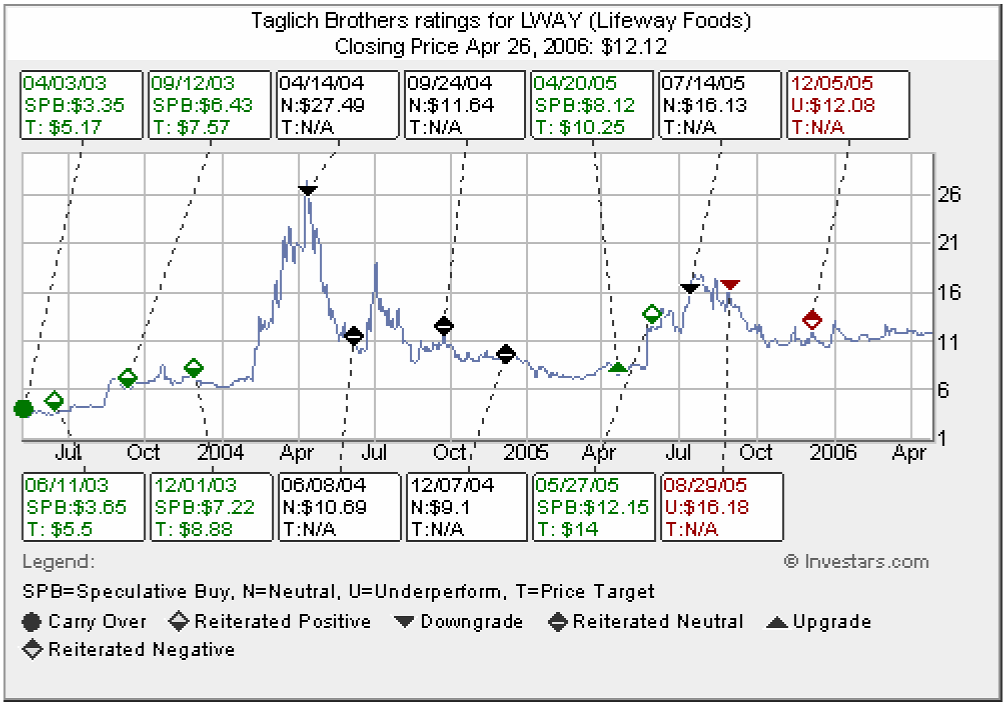
Liquidity has the potential to be a concern. Based on our calculations average daily-volume during 2003 increased to 4,451 shares from 1,943 shares in 2002. During 2004, average volume increased significantly to 154,399 shares traded a day. In 2005, average volume declined to 43,400 shares traded a day. During the first three months of 2006, average daily volume has declined to 14,698 shares traded a day. Average daily volume remains relatively low; therefore, investors need to be aware that by nature a thinly traded equity can have significant price volatility.

Conclusion

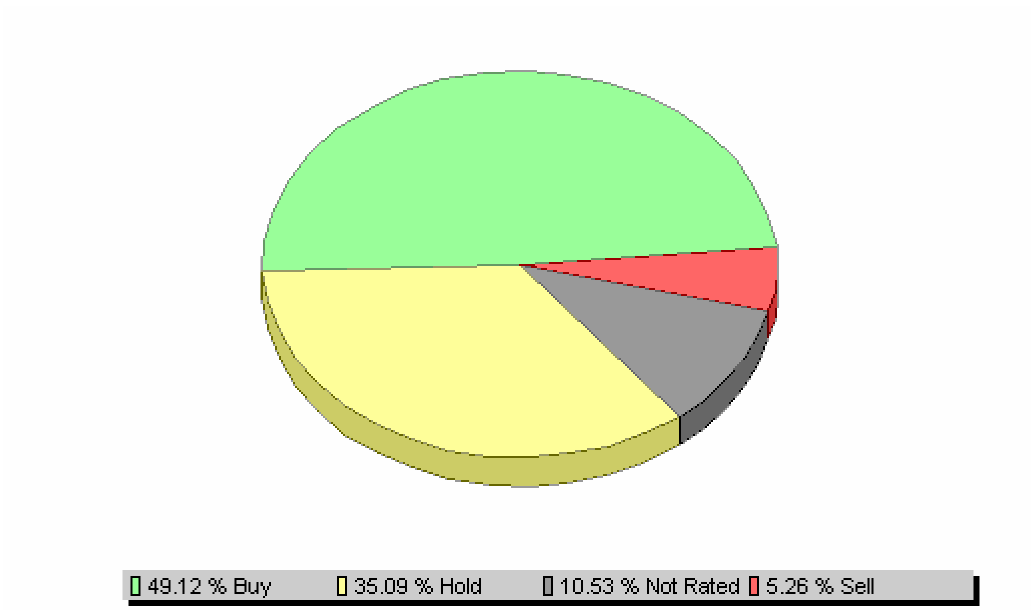
We are maintaining our Underperform rating on Lifeway Foods, Inc. (NasdaqNM: LWAY). We continue to believe its shares remain fairly valued based on our current revenue, EBITDA, and EPS estimates.

Investors need to be aware that the Company’s Stockholders’ Agreement with Danone terminated on December 30, 2005 (according to LWAY’s 2005 10-K filing); therefore, investors should be cognizant that the non-compete covenant between Lifeway and Danone also expired.

According to SEC filings, as of December 31, 2005, Danone owned approximately 20.4% of LWAY’s common shares. Since the agreements have expired, Danone could increase its stake or conversely sell its stake in LWAY. Also, direct competition could occur between the companies. At this point in time, investors will just have to watch carefully to see what transpires.



Taglich Brothers Current Ratings Distribution



Investment Banking Services for Companies Covered in the Past 12 Months

Rating	#	%
Buy	0	0
Hold	0	0
Sell	0	0
Not Rated	1	8.33%

Meaning of Ratings

Buy

We believe the Company is undervalued relative to its market and peers. We believe its risk reward ratio strongly advocates purchase of the stock relative to other stocks in the marketplace. Remember, with all equities there is always downside risk.

Speculative Buy

We believe that the long run prospects of the Company are positive. We believe its risk reward ratio advocates purchase of the stock. We feel the investment risk is higher than our typical “buy” recommendation. In the short run, the stock may be subject to high volatility and continue to trade at a discount to its market.

Neutral

We will remain neutral pending certain developments.

Underperform

We believe that the Company may be fairly valued based on its current status. Upside potential is limited relative to investment risk.

Sell

We believe that the Company is significantly overvalued based on its current status. The future of the Company's operations may be questionable and there is an extreme level of investment risk relative to reward.

Some notable Risks within the Microcap Market

Stocks in the Microcap segment of the market have many risks that are not as prevalent in Large-cap, Blue Chips or even Small-cap stocks. Often it is these risks that cause Microcap stocks to trade at discounts to their peers. The most common of these risks is liquidity risk, which is typically caused by small trading floats and very low trading volume which can lead to large spreads and high volatility in stock price. In addition, Microcaps tend to have significant company specific risks that contribute to lower valuations. Investors need to be aware of the higher probability of financial default and higher degree of financial distress inherent in the microcap segment of the market.

From time to time our analysts may choose to withhold or suspend a rating on a company. We continue to publish informational reports on such companies; however, they have no ratings or price targets. In general, we will not rate any company that has too much business or financial uncertainty for our analysts to form an investment conclusion, or that is currently in the process of being acquired.

Public Companies mentioned in this report:

Groupe Danone (NYSE: DA)

* The information and statistical data contained herein have been obtained from sources, which we believe to be reliable but in no way are warranted by us as to accuracy or completeness. We do not undertake to advise you as to changes in figures or our views. This is not a solicitation of any order to buy or sell. Taglich Brothers, Inc. is fully disclosed with its clearing firm, Pershing, LLC, is not a market maker and does not sell to or buy from customers on a principal basis. The above statement is the opinion of Taglich Brothers, Inc. and is not a guarantee that the target price for the stock will be met or that predicted business results for the company will occur. There may be instances when fundamental, technical and quantitative opinions contained in this report are not in concert. We, our affiliates, any officer, director or stockholder or any member of their families may from time to time purchase or sell any of the above-mentioned or related securities. Analysts and members of the Research Department are prohibited from buying or selling securities issued by the companies that Taglich Brothers, Inc. has a research relationship with, except if ownership of such securities was prior to the start of such relationship, then an Analyst or member of the Research Department may sell such securities after obtaining expressed written permission from the Director of Research. As of the date of this report, we, our affiliates, any officer, director or stockholder, or any member of their families do not have a position in the stock of the company mentioned in this report. All research issued by Taglich Brothers, Inc. is based on public information. Taglich Brothers, Inc. does not currently have an Investment Banking relationship with the company mentioned in this report and was not a manager or co-manager of any offering for the company with in the last three years. Since December 2000, the company pays a monthly monetary fee of $1,500 (USD) to Taglich Brothers, Inc. for the creation and dissemination of research reports.

I, Howard Halpern, the research analyst of this report, hereby certify that the views expressed in this report accurately reflect my personal views about the subject securities and issuers; and that no part of my compensation was, is, or will be directly or indirectly related to the specific recommendations or views contained in this report.

Lifeway Foods, Inc.
Consolidated Balance Sheets
(in thousands)

	Dec. 2002 Year End	Dec. 2003 Year End	Dec. 2004 Year End	Dec. 2005 Year End
ASSETS				
Current assets:				
Cash and cash equivalents	$ 2,732	$ 4,598	$ 5,773	$ 4,354
Marketable securities	4,172	6,303	6,742	7,479
Accounts receivable, net	1,435	1,800	2,024	2,518
Other receivables	60	166	72	56
Inventories	721	812	906	1,717
Prepaid income taxes	-	306	259	12
Prepaid expenses and other assets	1	1	7	9
Deferred income taxes	692	27	-	143
Total current assets	**9,813**	**14,012**	**15,783**	**16,287**
Property, plant and equipment, net	4,472	3,733	3,420	7,751
Total assets	**$ 14,285**	**$ 17,745**	**$ 19,688**	**$ 24,465**
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Current maturities of notes payable	31	28	9	532
Accounts payable	639	795	642	426
Accrued expenses	184	184	196	355
Taxes payable	398	-	36	-
Total current liabilities	**1,252**	**1,007**	**882**	**1,314**
Long-term liabilities	500	473	464	2,903
Deferred income taxes	453	472	424	349
Stockholders' equity:				
Common stock, no par value; authorized 10,000,000 shares	6,509	6,509	6,509	6,509
Paid-in capital	-	-	64	91
Stock subscription receivable	(15)	(15)	-	-
Retained earnings	7,600	9,822	11,874	14,423
Accumulated other comprehansive income, net of tax	(1,335)	156	119	(100)
Treasury stock, at cost	(680)	(680)	(649)	(1,025)
Total stockholders' equity	**12,080**	**15,793**	**17,918**	**19,899**
Total liabilities and stockholders' equity	**$ 14,285**	**$ 17,745**	**$ 19,688**	**$ 24,465**
SHARES OUT	8,437	8,437	8,420	8,396

Lifeway Foods, Inc.
Quarterly Income Statement Model
For the Years Ended December 31,
(in thousands)

	FY2002A	FY2003A	FY2004A	FY2005A	**FY2006E**
Revenue	$ 12,212	$ 14,878	$ 16,319	$ 20,132	**$ 25,428**
Cost of goods sold	6,744	7,841	9,035	11,664	**14,620**
Gross Profit	5,468	7,037	7,284	8,468	**10,808**
Gross Margins	44.78%	47.30%	44.64%	42.06%	**42.50%**
Sales, general and administrative	2,891	3,558	4,334	5,066	**6,365**
EBITDA	3,385	4,167	3,620	4,052	**5,123**
Operating Income	2,578	3,479	2,950	3,401	**4,443**
Operating Margin	21.11%	23.38%	18.08%	16.90%	**17.47%**
Other Income (Expense)					
Interest income	187	97	186	323	**515**
Interest expense	(75)	(41)	(31)	(101)	**(220)**
Gain on sale of marketable securities	18	(1,294)	354	445	-
Other than temporary reduction of marketable securities	(236)	89	(16)	14	-
Gain on sale of assets	-	1,246	-	-	-
Total Other Income (Expense)	(105)	98	492	682	**295**
Pre-Tax Income	2,472	3,576	3,442	4,083	**4,738**
Pre-Tax Margins	20.24%	24.04%	21.09%	20.28%	**18.63%**
Income Tax Expense (Benefit)	943	1,355	1,390	1,535	**1,845**
Tax Rate	38.16%	37.89%	40.39%	37.58%	**38.94%**
Net Income	$ 1,529	$ 2,221	$ 2,052	$ 2,548	**$ 2,893**
EPS -- Fully Diluted	$ 0.18	$ 0.26	$ 0.24	$ 0.30	**$ 0.34**
Avg Shares Out-Fully Diluted *	8,531	8,437	8,439	8,404	**8,413**
Percent of Revenue					
Cost of Revenues	55.22%	52.70%	55.36%	57.94%	57.50%
Sales, General and Administrative expenses	23.67%	23.92%	26.56%	25.17%	25.03%
YEAR / YEAR GROWTH					
Total Revenues	14.30%	21.83%	9.69%	23.36%	26.31%
Operating Income	79.34%	34.96%	-15.18%	15.28%	30.62%
Pre-Tax Income	36.47%	44.67%	-3.75%	18.62%	16.04%
Net Income	25.21%	45.31%	-7.62%	24.19%	13.52%

* Adjusted for the 2-1 stock split effective March 9, 2004

Lifeway Foods, Inc.
Quarterly Income Statement Model
For the Years Ended December 31, 2004
(in thousands)

	Q1(03/04)A	Q2 (06/04)A	Q3 (09/04)A	Q4 (12/04)A	**FY2004A**
Revenue	$ 3,935	$ 4,002	$ 4,139	$ 4,243	**$ 16,319**
Cost of goods sold	2,099	2,266	2,240	2,430	**9,035**
Gross Profit	1,836	1,736	1,899	1,813	**7,284**
Gross Margins	*46.65%*	*43.38%*	*45.89%*	*42.73%*	**44.64%**
Operating Expenses:					
Sales, general and administrative	882	1,049	1,158	1,244	**4,334**
Total Operating Expenses	882	1,049	1,158	1,244	**4,334**
EBITDA	1,110	846	901	764	**3,620**
Operating Income	954	687	741	569	**2,950**
Operating Margin	*24.24%*	*17.16%*	*17.91%*	*13.40%*	**18.08%**
Other Income (Expense)					
Interest income	41	34	50	61	**186**
Interest expense	(8)	(8)	(8)	(8)	**(31)**
Total Other Income (Expense)	302	39	70	80	**492**
Pre-Tax Income	1,256	726	811	649	**3,442**
Pre-Tax Margins	*31.91%*	*18.15%*	*19.60%*	*15.29%*	**21.09%**
Income Tax Expense (Benefit)	491	294	296	309	**1,390**
Tax Rate	*39.06%*	*40.50%*	*36.51%*	*47.66%*	**40.39%**
Net Income	$ 765	$ 432	$ 515	$ 340	**$ 2,052**
EPS -- Fully Diluted	$ 0.09	$ 0.05	$ 0.06	$ 0.04	**$ 0.24**
Avg Shares Out-Fully Diluted	8,437	8,438	8,440	8,440	**8,439**
Percent of Revenue					
Cost of Revenues	53.35%	56.62%	54.11%	57.27%	55.36%
Sales, General and Administrative expenses	22.41%	26.22%	27.98%	29.33%	26.56%
YEAR / YEAR GROWTH					
Total Revenues	18.94%	5.99%	7.86%	7.26%	9.69%

Lifeway Foods, Inc.
Quarterly Income Statement Model
For the Years Ended December 31, 2005
(in thousands)

	Q1(03/05)A	Q2 (06/05)A	Q3 (09/05)A	Q4 (12/05)A	**FY2005A**
Revenue	$ 4,657	$ 5,073	$ 5,195	$ 5,208	**$ 20,132**
Cost of goods sold	2,578	2,956	3,073	3,057	**11,664**
Gross Profit	2,079	2,116	2,121	2,151	**8,468**
Gross Margins	*44.64%*	*41.72%*	*40.84%*	*41.31%*	**42.06%**
Operating Expenses:					
Sales, general and administrative	1,155	1,279	1,359	1,273	**5,066**
Total Operating Expenses	1,155	1,279	1,359	1,273	**5,066**
EBITDA	1,064	1,015	930	1,043	**4,052**
Operating Income	924	837	762	878	**3,401**
Operating Margin	*19.84%*	*16.51%*	*14.67%*	*16.86%*	**16.90%**
Other Income (Expense)					
Interest income	65	75	72	110	**323**
Interest expense	(7)	(7)	(37)	(50)	**(101)**
Total Other Income (Expense)	259	44	197	181	**682**
Pre-Tax Income	1,183	881	959	1,059	**4,083**
Pre-Tax Margins	*25.41%*	*17.37%*	*18.47%*	*20.34%*	**20.28%**
Income Tax Expense (Benefit)	458	324	400	352	**1,535**
Tax Rate	*38.69%*	*36.80%*	*41.74%*	*33.24%*	**37.58%**
Net Income	$ 725	$ 557	$ 559	$ 707	**$ 2,548**
EPS -- Fully Diluted	$ 0.09	$ 0.07	$ 0.07	$ 0.08	**$ 0.30**
Avg Shares Out-Fully Diluted	8,433	8,398	8,401	8,404	**8,404**
Percent of Revenue					
Cost of Revenues	55.36%	58.28%	59.16%	58.69%	57.94%
Sales, General and Administrative expenses	24.81%	25.21%	26.16%	24.44%	25.17%
YEAR / YEAR GROWTH					
Total Revenues	18.34%	26.75%	25.52%	22.72%	23.36%

Lifeway Foods, Inc.
Quarterly Income Statement Model
For the Years Ended December 31, 2006
(in thousands)

	Q1(03/06)E	Q2 (06/06)E	Q3 (09/06)E	Q4 (12/06)E	**FY2006E**
Revenue	$ 6,003	$ 6,250	$ 6,525	$ 6,650	**$ 25,428**
Cost of goods sold	3,335	3,635	3,800	3,850	**14,620**
Gross Profit	2,668	2,615	2,725	2,800	**10,808**
Gross Margins	*44.44%*	*41.84%*	*41.76%*	*42.10%*	**42.50%**
Operating Expenses:					
Sales, general and administrative	1,365	1,575	1,675	1,750	**6,365**
Total Operating Expenses	1,365	1,575	1,675	1,750	**6,365**
EBITDA	1,473	1,210	1,220	1,220	**5,123**
Operating Income	1,303	1,040	1,050	1,050	**4,443**
Operating Margin	*21.71%*	*16.65%*	*16.09%*	*15.78%*	**17.47%**
Other Income (Expense)					
Interest income	115	120	135	145	**515**
Interest expense	(55)	(55)	(55)	(55)	**(220)**
Total Other Income (Expense)	60	65	80	90	**295**
Pre-Tax Income	1,363	1,105	1,130	1,140	**4,738**
Pre-Tax Margins	*22.71%*	*17.69%*	*17.32%*	*17.14%*	**18.63%**
Income Tax Expense (Benefit)	530	435	465	415	**1,845**
Tax Rate	*38.88%*	*39.35%*	*41.15%*	*36.42%*	**38.94%**
Net Income	$ 833	$ 670	$ 665	$ 725	**$ 2,893**
EPS -- Fully Diluted	$ 0.10	$ 0.08	$ 0.08	$ 0.09	**$ 0.34**
Avg Shares Out-Fully Diluted	8,405	8,410	8,415	8,420	**8,413**
Percent of Revenue					
Cost of Revenues	55.56%	58.16%	58.24%	57.90%	57.50%
Sales, General and Administrative expenses	22.74%	25.20%	25.67%	26.32%	25.03%
YEAR / YEAR GROWTH					
Total Revenues	28.91%	23.22%	25.61%	27.69%	26.31%

Lifeway Foods, Inc.
Cash Flow Statement
(in thousands)

	FY2002A	FY2003A	FY2004A	FY2005A
Cash Flows from Operating Activities				
Net Income	$ 1,529	$ 2,222	$ 2,052	$ 2,548
Depreciation and amortization	808	688	670	651
Amortization of discounts on securities	-	-	-	-
Gain on sale of marketable securities	(18)	1,294	(354)	(445)
Loss on marketable securities classified as trading	-	-	16	(14)
Gain on sale of assets	-	(1,246)	-	-
Other than temporary reductions of marketable securities	236	-	-	-
Issuance of common stock in exchange for services rendered	-	-	95	52
Decrease in allowance for doubtful accounts	-	-	-	-
Provision for doubtful accounts	-	-	-	-
Deferred income taxes	(65)	9	46	(100)
	2,490	2,967	2,525	2,692
Changes In:				
Accounts receivable	(119)	(365)	(224)	(494)
Other receivables	(8)	(106)	94	16
Inventories	80	(91)	(94)	(811)
Prepaid income taxes	-	(306)	48	247
Prepaid expenses and other assets	32	0	(6)	(2)
Accounts payable	96	156	(154)	(215)
Accrued expenses	20	0	12	159
Taxes payable	253	(398)	-	-
Net Changes in Working Capital	355	(1,109)	(325)	(1,100)
Net cash Provided by Operations	2,845	1,858	2,200	1,592
Cash Flows from Investing Activities				
Purchase of marketable securities	(3,316)	(4,284)	(6,266)	(6,461)
Sale of marketable securities	4,025	3,025	6,097	5,810
Sales of Assets	-	1,713	-	-
Change in margin account	(432)	-	-	-
Acquisition of Ilya's Farms, Inc., net of assets acquired	-	-	(512)	-
Loan acquisition costs	-	-	-	-
Purchase of property, plant and equipment	(259)	(415)	(330)	(4,917)
Net cash used in Investing	17	39	(1,011)	(5,567)
Cash Flows from Financing Activities				
Repayment of notes payable	(675)	(31)	(28)	(37)
Proceeds from issuance of common stock	-	-	15	-
Proceeds from note payable	-	-	-	3,000
Purchase of treasury stock	(393)	-	-	(402)
Loan costs	-	-	-	(7)
Net cash provided by Financing	(1,068)	(31)	(13)	2,555
Net change in Cash	1,795	1,866	1,175	(1,419)
Cash Beginning of Period	936	2,732	4,598	5,773
Cash End of Period	$ 2,732	$ 4,598	$ 5,773	$ 4,354