

Taglich Brothers, Inc.

The Standard of Excellence in the Microcap Market

Member: NASD, SIPC

Research Report – Update

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

Lifeway Foods, Inc.

Rating: Speculative Buy

Howard Halpern

LWAY \$7.30- (NasdaqNM)

June 11, 2003

	FYE (12/00)	FYE (12/01)	FYE (12/02)	FYE (12/03) E*	FYE (12/04) E
Revenues (in millions)	\$9.2	\$10.7	\$12.2	\$13.8	\$15.7
Earnings per share (diluted)	\$0.21	\$0.28	\$0.36	\$0.43	\$0.56

52week range	\$8.50 – \$4.95	Fiscal year ends:	December
Shares outstanding	4.28 million	Revenue/shares (TTM)	\$2.97
Trading float	1.20 million	Price/Sales (TTM)	2.46X
Insider and institutional ownership	72.0%	Price/Sales (2004)	1.98X
Tangible Book value/shr <small>a/o 03-31-03</small>	\$3.05	Price/Earnings (TTM)*	20.9X
Price/Book	2.39X	Price/Earnings (2004)	13.0X

* Excludes a \$0.14 per share gain from the sale of assets and a one-time loss from sale of marketable securities

Lifeway Foods, Inc., based in Morton Grove, Illinois 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. They currently have approximately 45 employees. Web site address is: www.kefir.com

Key investment considerations:

We are maintaining our Speculative Buy rating and setting a twelve-month price target of \$11.00 per share based on our earnings estimate for the next four quarters and a discounted cash flow analysis. Our previous twelve-month price target was \$10.34 per share.

The Company reported 2003 first quarter revenues of \$3.309 million, which was an increase of 14.6% versus \$2.888 million in the same period last year. Net income was \$0.993 million or \$0.24 per diluted share versus \$0.448 million or \$0.10 per diluted share in the first quarter of 2002. However, 2003 first quarter results included non-recurring items that amounted to a gain of approximately \$0.14 per fully diluted share.

We are maintaining our prior 2003 and 2004 revenue estimates of \$13.8 million and \$15.7 million, respectively.

We continue to believe that our revenue forecasts, which calls for annual growth in excess of 13%, can be achieved through – 1) The Company's marketing efforts; 2) Increasing acceptance of its organic products; 3) Growth of the La Fruta™ product line for the Hispanic market; and 4) New eye-catching packaging for non-fat Kefir products.

** Please view our disclaimer located on page 8.*

1370 Avenue of the Americas, 31st Floor, New York, N.Y. 10019
(800) 456-1220 • Fax (212) 265-4744
www.taglichbrothers.com

The Company

Lifeway Foods, Inc. (LWAY) manufactures a cultured dairy beverage called Kefir and also develops Kefir related products at its two manufacturing facilities in Illinois.

1. A 50,000-square foot facility, which is the largest Kefir manufacturing facility in the United States; and
2. A smaller 12,000-square foot Kefir manufacturing facility.

LWAY distributes its products in Illinois directly to approximately 1,200 local stores including major retail chains (i.e., Jewel Food Stores, Dominick's Finer Foods, and Whole Foods Market), via ten company owned trucks. In the United States, the Company distributes its products to over 10,000 stores. Also, the Company's products are distributed internationally to Canada.

Danone Foods, Inc. the U.S. subsidiary of Groupe Danone of Paris, France, has a 20% ownership interest in the Company.

Kefir

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 Financials

For the three-month period ended March 31, 2003 versus the same period last year:

- Revenues increased to \$3.309 million versus \$2.888 million;
- Operating expenses increased to \$0.845 million versus \$0.649 million;
- EBITDA increased to \$0.638 million versus \$0.716 million;
- Net income was \$0.993 million or \$0.24 per diluted share versus net income of \$0.448 million or \$0.10 per diluted share.

The year-over-year quarterly revenue increase of 14.6% was primarily attributable to the Company's advertising program for its various Kefir-based products and the increasing awareness of the probiotic health-related benefits of its products.

Gross margins decreased to 44.8% versus 47.3% in the same period last year. The decline in gross margins resulted from higher raw material costs. Operating expenses, as a percentage of revenues, increased to 25.5% versus 22.5% in the first quarter of 2002. The increase in operating expenses, on a percentage basis, was due to increased advertising expenses and energy costs during the winter.

Net income for the first quarter of 2003 includes two non-recurring items:

- A gain of \$1.2 million on the sale of real property;
- A loss of \$0.346 million, which is attributable to other than temporary reductions of marketable securities.

Excluding the non-recurring items, we estimate that net income for the quarter was \$0.422 million or \$0.10 per diluted share.

In comparison to the results reported by the Company, Taglich Brothers' estimates called for first quarter revenues of \$3.3 million and net income of \$0.48 million or \$0.11 per diluted share. Our estimates did not include the non-recurring gain and loss reported during the first quarter of 2003.

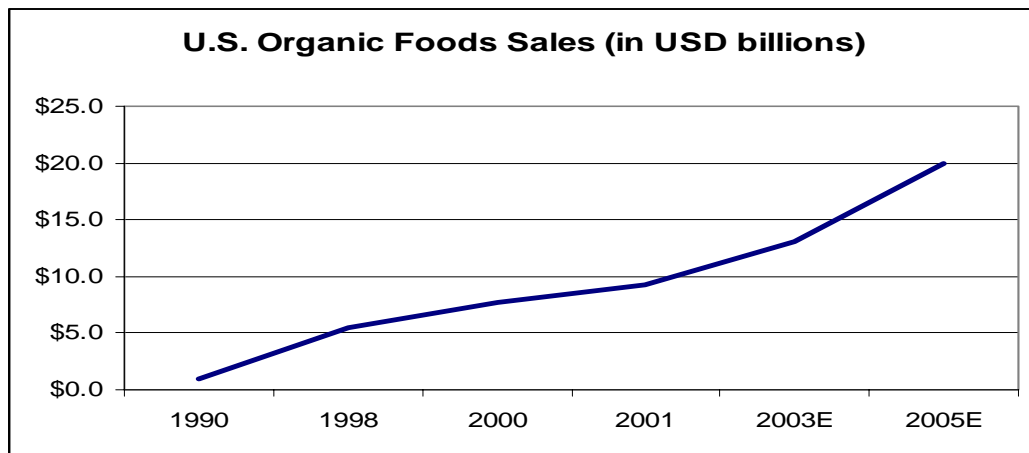
Balance Sheet as of March 31, 2003

The Company had cash and cash equivalents of \$2.79 million and short-term marketable securities of \$5.64 million. This compares to cash and cash equivalents of \$2.73 million and short-term marketable securities of \$4.17 million as of December 31, 2002. Working capital was \$10.30 million versus \$8.56 million in 2001. The Company's long-term liabilities stand at \$0.50 million. We believe that LWAY will be able to fund its sales growth from internally generated funds.

Industry and Competition

It is estimated that Lifeway Foods' target market in the functional and probiotic foods segment of the Food Industry has grown in terms of annual sales from \$16 billion in 1999 to approximately \$23 billion in 2002. The Nutrition Business Journal (NBJ) predicts that by 2010, the U.S. Functional Food Market will double in size to \$34 billion, representing 5.5% of the total Food Market. Currently, NBJ estimates that the Functional Food Market represents 3.3% of the total U.S. Food Market.

In addition, the Company's organic products are targeting a market that generated approximately \$9.3 billion of sales in 2001, according to Rabobank International's Food & Agribusiness Research Industry Note of May 2002. The chart below indicates the growth potential for this segment:



Source: Organic Trade Association; Natural Marketing Institute; Rabobank International, Food & Agribusiness Research

It is estimated that organic beverages comprise approximately 5% of the total U.S. Organic Food Market.

We continue to view the primary factors driving growth in sales of functional, probiotic, and organic foods as:

- The perception that nutrition is an effective tool for disease prevention;
- An aging population; and
- The expanding participation of conventional manufacturers and retailers in niche food segments.

The Company faces almost no direct competition in the United States for its drinkable Kefir product, although the Company's Kefir-based products are subject to competition from other yogurt and dairy products.

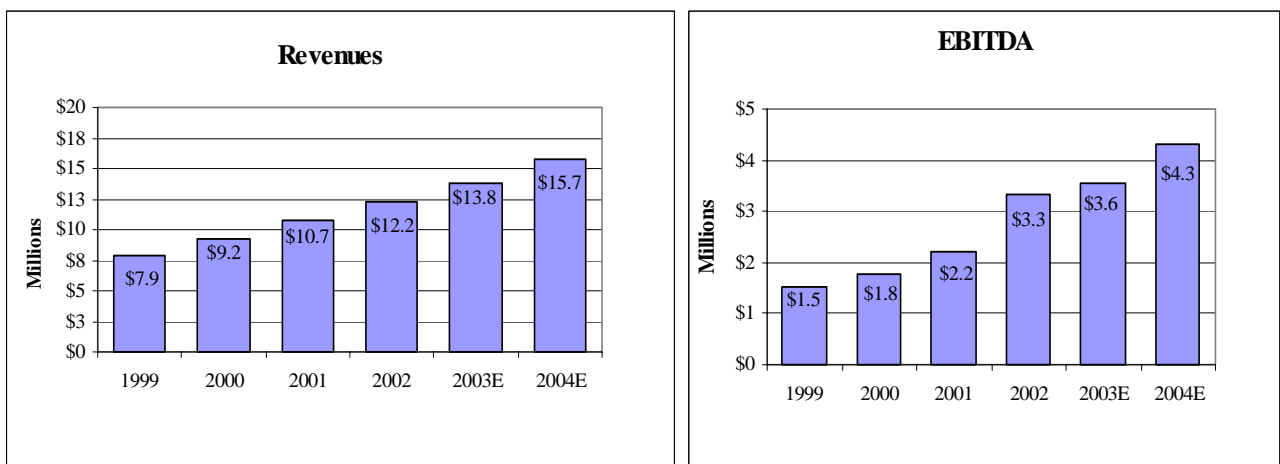
Outlook

We believe annual revenue growth will exceed 13%; therefore, revenues should reach \$13.83 million in 2003 and \$15.7 million in 2004, from \$12.212 million in 2002. Our revenue forecasts are based on:

- Consumers increased acceptance of the Company's organic product line;
- Marketing initiatives that includes:
 - Educating consumers about the potential beneficial uses of Kefir in the replenishment of 'good' bacteria in a person's intestinal system, especially after taking antibiotics or consuming alcohol;
 - Advertising in local newspapers (i.e., primarily in the Chicago area), and in national magazines (ex: Self, Shape, and Men's Fitness); and
 - Sponsoring and participating in various local sporting events around the country and exhibiting at trade shows (i.e., Natural Products Expo West in March 2003);
- The Company building on its current distribution channel, which includes regional supermarket chains and/or regional super-center type stores, and assisting local distributors with product sales; and
- Introduction of new eye-catching packaging for the Company's non-fat Kefir products.

We believe that as a result of the revenue growth, the Company will be able to leverage operating efficiencies at its two owned manufacturing facilities. We estimate that gross margins will improve to 45.3% and 45.4% in 2003 and 2004, respectively, from 44.8% in 2002. Also, SG&A expenses, as a percentage of revenues, should approximate 24.4% and 22.1% in 2003 and 2004, respectively.

The following chart shows our revenue and EBITDA projections:



Source: Company Filings and Taglich Brothers Estimates

Based on our expectations for revenues and expenses and excluding the non-recurring items, we anticipate net income of \$1.828 million or \$0.43 per diluted share in 2003 and \$2.38 million or \$0.56 per diluted share in 2004.

Risks

Legal Issue

During the fourth quarter of 2001, Fresh Made, Inc. amended a previously filed lawsuit against Lifeway Foods in regard to abuse of process, restraint of trade, unfair competition, and interference with business relationships. The Company believes this lawsuit is without merit and is in retaliation to Lifeway's efforts to enforce its rights under a settlement agreement, which the two parties entered into in connection with a prior trademark infringement lawsuit filed against Fresh Made. On August 8, 2002, an order was entered dismissing 19 of 20 counts made against the Company by Fresh Made, Inc. Lifeway intends to vigorously defend the remaining count.

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 anyone. 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 in price it could negatively impact margins for a short period of time.

Corporate Governance

Corporate governance may be an issue facing the Company 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.

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 the first four months of 2003 has decreased to 1,265 shares from 1,943 shares in 2002. Investors need to be aware that liquidity risks in the microcap market are characterized by low trading volume, high volatility of the stock price, and a wide bid-ask spread.

Conclusion

We are maintaining our coverage of Lifeway Foods, Inc., with a Speculative Buy recommendation and setting a twelve-month price target of \$11.00 per share. Our previous twelve-month price target was \$10.34 per share. Our price target is based on our earnings per share estimate for the next four quarters and EBITDA forecasts, which is used as a proxy for cash flow.

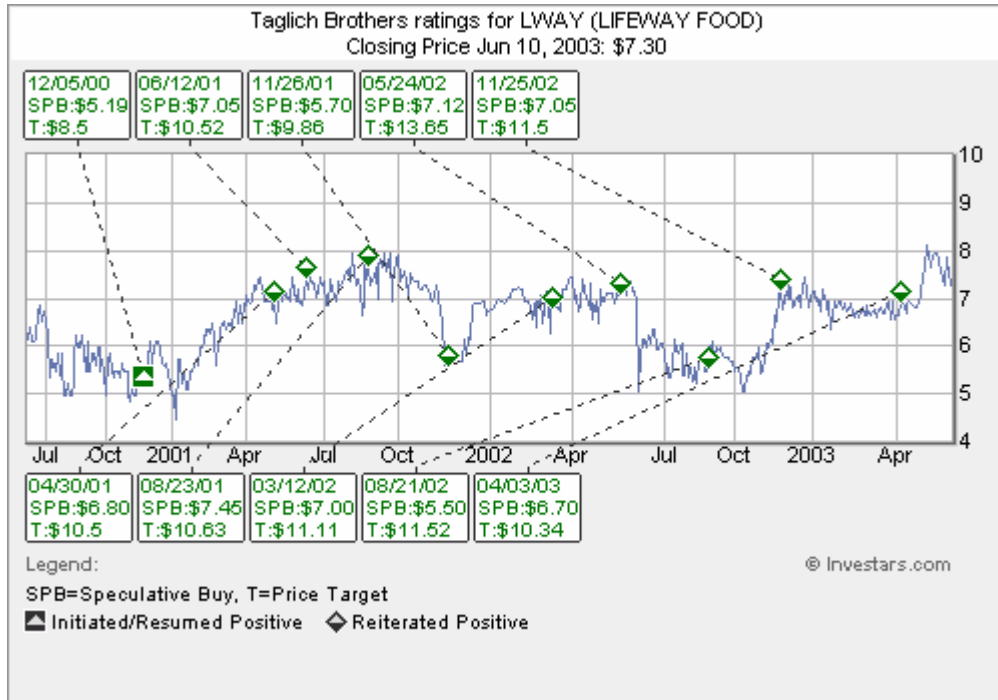
We estimate that the Company will earn \$0.46 per diluted share over the next four quarters. Based on our models, we are forecasting EBITDA of \$3.55 million and \$4.32 million in 2003 and 2004, respectively.

We obtained our price target by averaging the following valuation models discounted by 20% to account for microcap risk, the current stock market environment*, and Company specific risks mentioned earlier:

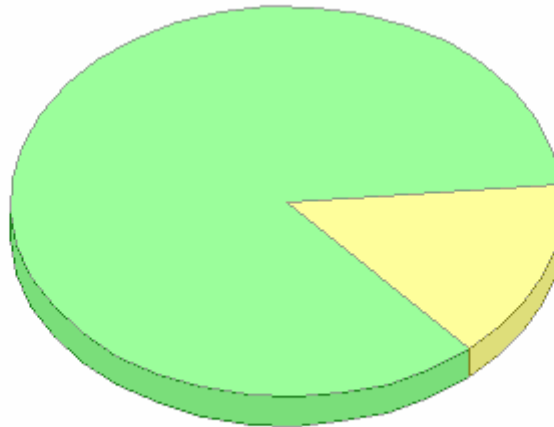
- A 20.4X P/E based on the trailing twelve month average for the Food Processing Industry from multexinvestor.com as of 6/09/03, applied to our earnings per share estimate of \$0.46 for the next four quarters; and
- Our discounted cash flow model, using EBITDA as a proxy for cash flow and a 9.6% discount factor using the estimated five year growth rate for the Food Processing Industry according to multexinvestor.com as of 6/09/03.

* The broad based Russell 3000 index had declined by approximately 3.5% during the first quarter of 2003 and by approximately 26.0% on a year-over-year basis (March 31, 2003 vs. March 31, 2002).

Lifeway Foods, Inc.



Taglich Brothers Current Ratings Distribution



85.11 % Buy 14.89 % Hold

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.

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, BNY Clearing Services, 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. 2000 Full Year	Dec. 2001 Full Year	Dec. 2002 Full Year	Mar. 2003 1st Qtr
ASSETS				
Current assets:				
Cash and cash equivalents	\$ 1,437	\$ 937	\$ 2,732	\$ 2,788
Marketable securities	4,850	5,755	4,172	5,644
Accounts receivable, net	1,182	1,317	1,435	1,731
Other receivables	-	53	60	58
Inventories	920	801	721	774
Prepaid expenses and other assets	-	34	1	4
Deferred income taxes	<u>167</u>	<u>561</u>	<u>692</u>	<u>440</u>
Total current assets	<u>8,556</u>	<u>9,456</u>	<u>9,813</u>	<u>11,438</u>
 Property, plant and equipment, net	 5,020	 5,021	 4,472	 3,903
Total assets	<u>\$ 13,575</u>	<u>\$ 14,477</u>	<u>\$ 14,285</u>	<u>\$ 15,342</u>
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Current maturities of notes payable	706	90	31	31
Margin account	-	432	-	-
Accounts payable	518	543	639	698
Accrued expenses	242	164	184	155
Taxes payable	<u>65</u>	<u>145</u>	<u>398</u>	<u>250</u>
Total current liabilities	<u>1,531</u>	<u>1,374</u>	<u>1,252</u>	<u>1,134</u>
 Long-term liabilities	 529	 1,116	 500	 493
Deferred income taxes	376	436	453	408
Stockholders' equity:				
Common stock, no par value; authorized 10,000,000 shares	6,509	6,509	6,509	6,509
Stock subscription receivable	(15)	(15)	(15)	(15)
Retained earnings	4,851	6,072	7,600	8,594
Accumulated other comprehensive income, net of tax	(205)	(729)	(1,335)	(1,101)
Treasury stock, at cost	<u>-</u>	<u>(287)</u>	<u>(680)</u>	<u>(680)</u>
Total stockholders' equity	<u>11,140</u>	<u>11,550</u>	<u>12,080</u>	<u>13,307</u>
 Total liabilities and stockholders' equity	 <u>\$ 13,575</u>	 <u>\$ 14,477</u>	 <u>\$ 14,285</u>	 <u>\$ 15,342</u>
 SHARES OUT	 4,318	 4,269	 4,218	 4,218

Lifeway Foods, Inc.
Quarterly Income Statement Model
For the Years Ended December 31, 2003
(in thousands)

	<u>FY2000</u>	<u>FY2001</u>	<u>FY2002</u>	<u>FY2003E*</u>	<u>FY2004E</u>
Revenue	\$ 9,177	\$ 10,684	\$ 12,212	\$ 13,834	\$ 15,700
Cost of goods sold	<u>5,308</u>	<u>6,449</u>	<u>6,744</u>	<u>7,566</u>	<u>8,575</u>
Gross Profit	3,869	4,235	5,468	6,268	7,125
<i>Gross Margins</i>	42.16%	39.64%	44.78%	45.31%	45.38%
Sales, general and administrative	<u>2,707</u>	<u>2,785</u>	<u>2,891</u>	<u>3,375</u>	<u>3,470</u>
<i>EBITDA</i>	1,772	2,216	3,385	3,553	4,315
Operating Income	1,162	1,450	2,578	2,893	3,655
<i>Operating Margin</i>	12.66%	13.57%	21.11%	20.91%	23.28%
Other Income (Expense)					
Interest income	369	235	187	126	150
Interest expense	(93)	(93)	(75)	(25)	(11)
Gain on sale of marketable securities	15	220	18	-	-
Other than temporary reduction of marketable securities	-	-	(236)	(347)	-
Gain on sale of assets	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,246</u>	<u>-</u>
Total Other Income (Expense)	<u>291</u>	<u>362</u>	<u>(105)</u>	<u>1,002</u>	<u>139</u>
Pre-Tax Income	1,453	1,812	2,472	3,895	3,794
<i>Pre-Tax Margins</i>	15.84%	16.96%	20.24%	28.15%	24.17%
Income Tax Expense (Benefit)	<u>526</u>	<u>591</u>	<u>943</u>	<u>1,495</u>	<u>1,410</u>
<i>Tax Rate</i>	36.21%	32.59%	38.16%	38.39%	37.16%
Net Income	<u>\$ 927</u>	<u>\$ 1,221</u>	<u>\$ 1,529</u>	<u>\$ 2,399</u>	<u>\$ 2,384</u>
EPS -- Fully Diluted	<u>\$ 0.21</u>	<u>\$ 0.28</u>	<u>\$ 0.36</u>	<u>\$ 0.57*</u>	<u>\$ 0.56</u>
Avg Shares Out-Fully Diluted	<u>4,318</u>	<u>4,318</u>	<u>4,266</u>	<u>4,232</u>	<u>4,270</u>
Percent of Revenue					
Cost of Revenues	57.84%	60.36%	55.22%	54.69%	54.62%
Sales, General and Administrative expenses	29.50%	26.07%	23.67%	24.39%	22.10%
YEAR / YEAR GROWTH					
Total Revenues	16.05%	16.42%	14.30%	13.28%	13.49%
Operating Income	9.12%	24.77%	79.34%	12.24%	26.34%
Pre-Tax Income	35.86%	24.67%	36.47%	57.54%	-2.58%

* Excluding the \$1.246 million gain on sale of assets and \$0.347 million other than temporary reduction of marketable securities our EPS estimate for 2003 is \$0.43 per fully diluted share.

Lifeway Foods, Inc.
Quarterly Income Statement Model
For the Years Ended December 31, 2003
(in thousands)

	<u>Q1(03/02)</u>	<u>Q2 (06/02)</u>	<u>Q3 (09/02)</u>	<u>Q4 (12/02)</u>	<u>FY2002</u>
Revenue	\$ 2,888	\$ 3,003	\$ 3,075	\$ 3,247	\$ 12,212
Cost of goods sold	<u>1,523</u>	<u>1,761</u>	<u>1,586</u>	<u>1,874</u>	<u>6,744</u>
Gross Profit	1,365	1,242	1,488	1,373	5,468
<i>Gross Margins</i>	47.25%	41.37%	48.41%	42.29%	44.78%
Operating Expenses:					
Sales, general and administrative	649	734	750	758	2,891
Total Operating Expenses	<u>649</u>	<u>734</u>	<u>750</u>	<u>758</u>	<u>2,891</u>
EBITDA	920	707	942	816	3,385
Operating Income	716	508	739	615	2,578
<i>Operating Margin</i>	24.79%	16.92%	24.02%	18.94%	21.11%
Other Income (Expense)					
Interest income	37	53	67	29	187
Interest expense	(20)	(19)	(19)	(16)	(75)
Gain on sale of marketable securities	36	3	(3)	(18)	18
Other than temporary reduction of marketable securities	<u>-</u>	<u>-</u>	<u>-</u>	<u>(236)</u>	<u>(236)</u>
Total Other Income (Expense)	<u>53</u>	<u>37</u>	<u>45</u>	<u>(241)</u>	<u>(105)</u>
Pre-Tax Income	769	545	783	374	2,472
<i>Pre-Tax Margins</i>	26.64%	18.16%	25.48%	11.52%	20.24%
Income Tax Expense (Benefit)	<u>322</u>	<u>194</u>	<u>252</u>	<u>176</u>	<u>943</u>
<i>Tax Rate</i>	41.82%	35.52%	32.18%	47.05%	38.16%
Net Income	<u>\$ 448</u>	<u>\$ 352</u>	<u>\$ 531</u>	<u>\$ 198</u>	<u>\$ 1,529</u>
EPS -- Fully Diluted	<u>\$ 0.10</u>	<u>\$ 0.08</u>	<u>\$ 0.12</u>	<u>\$ 0.05</u>	<u>\$ 0.36</u>
Avg Shares Out-Fully Diluted	<u>4,270</u>	<u>4,269</u>	<u>4,269</u>	<u>4,255</u>	<u>4,266</u>
Percent of Revenue					
Cost of Revenues	52.75%	58.63%	51.59%	57.71%	55.22%
Sales, General and Administrative expenses	22.46%	24.45%	24.39%	23.35%	23.67%
YEAR / YEAR GROWTH					
Total Revenues	9.54%	9.20%	15.51%	23.19%	14.30%
Operating Income	65.75%	53.23%	109.89%	91.06%	79.34%
Pre-Tax Income	36.37%	43.02%	75.31%	-10.77%	36.47%

Lifeway Foods, Inc.
Quarterly Income Statement Model
For the Years Ended December 31, 2003
(in thousands)

	<u>Q1(03/03)*</u>	<u>Q2 (06/03)E</u>	<u>Q3 (09/03)E</u>	<u>Q4 (12/03)E</u>	<u>FY2003E*</u>
Revenue	\$ 3,309	\$ 3,375	\$ 3,550	\$ 3,600	\$ 13,834
Cost of goods sold	<u>1,826</u>	<u>1,825</u>	<u>1,890</u>	<u>2,025</u>	<u>7,566</u>
Gross Profit	1,483	1,550	1,660	1,575	6,268
<i>Gross Margins</i>	44.81%	45.93%	46.76%	43.75%	45.31%
Operating Expenses:					
Sales, general and administrative	845	835	840	855	3,375
Total Operating Expenses	<u>845</u>	<u>835</u>	<u>840</u>	<u>855</u>	<u>3,375</u>
EBITDA	803	880	985	885	3,553
Operating Income	638	715	820	720	2,893
<i>Operating Margin</i>	19.28%	21.19%	23.10%	20.00%	20.91%
Other Income (Expense)					
Interest income	33	32	31	30	126
Interest expense	(8)	(7)	(5)	(5)	(25)
	-	-	-	-	-
Other than temporary reduction of marketable securities	(347)	-	-	-	(347)
Gain on sale of assets	<u>1,246</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>1,246</u>
Total Other Income (Expense)	<u>926</u>	<u>25</u>	<u>26</u>	<u>25</u>	<u>1,002</u>
Pre-Tax Income	1,564	740	846	745	3,895
<i>Pre-Tax Margins</i>	47.26%	21.93%	23.83%	20.69%	28.15%
Income Tax Expense (Benefit)	<u>570</u>	<u>290</u>	<u>335</u>	<u>300</u>	<u>1,495</u>
<i>Tax Rate</i>	36.47%	39.19%	39.60%	40.27%	38.39%
Net Income	<u>\$ 993</u>	<u>\$ 450</u>	<u>\$ 511</u>	<u>\$ 445</u>	<u>\$ 2,399</u>
EPS -- Fully Diluted	<u>\$ 0.24</u>	<u>\$ 0.11</u>	<u>\$ 0.12</u>	<u>\$ 0.10</u>	<u>\$ 0.57</u>
Avg Shares Out-Fully Diluted	<u>4,218</u>	<u>4,225</u>	<u>4,235</u>	<u>4,250</u>	<u>4,232</u>
Percent of Revenue					
Cost of Revenues	55.19%	54.07%	53.24%	56.25%	54.69%
Sales, General and Administrative expenses	25.53%	24.74%	23.66%	23.75%	24.39%
YEAR / YEAR GROWTH					
Total Revenues	14.57%	12.40%	15.45%	10.88%	13.28%
Operating Income	-10.90%	40.77%	11.03%	17.06%	12.24%
Pre-Tax Income	103.26%	35.69%	7.99%	99.15%	57.54%
Net Income	121.93%	27.97%	-3.83%	124.64%	56.95%

* Excluding the \$1.246 million gain on sale of assets and \$0.347 million other than temporary reduction of marketable securities our EPS estimate for the first quarter and full year of 2003 is \$0.10 and \$0.43 per fully diluted share, respectively.

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

	<u>Q1(03/04)</u>	<u>Q2 (06/04)E</u>	<u>Q3 (09/04)E</u>	<u>Q4 (12/04)E</u>	<u>FY2004E</u>
Revenue	\$ 3,850	\$ 3,925	\$ 3,950	\$ 3,975	\$ 15,700
Cost of goods sold	<u>2,120</u>	<u>2,125</u>	<u>2,130</u>	<u>2,200</u>	<u>8,575</u>
Gross Profit	1,730	1,800	1,820	1,775	7,125
<i>Gross Margins</i>	44.94%	45.86%	46.08%	44.65%	45.38%
Operating Expenses:					
Sales, general and administrative	875	860	865	870	3,470
Total Operating Expenses	<u>875</u>	<u>860</u>	<u>865</u>	<u>870</u>	<u>3,470</u>
EBITDA	1,020	1,105	1,120	1,070	4,315
Operating Income	855	940	955	905	3,655
<i>Operating Margin</i>	22.21%	23.95%	24.18%	22.77%	23.28%
Other Income (Expense)					
Interest income	35	35	40	40	150
Interest expense	<u>(4)</u>	<u>(3)</u>	<u>(2)</u>	<u>(2)</u>	<u>(11)</u>
Total Other Income (Expense)	<u>31</u>	<u>32</u>	<u>38</u>	<u>38</u>	<u>139</u>
Pre-Tax Income	886	972	993	943	3,794
<i>Pre-Tax Margins</i>	23.01%	24.76%	25.14%	23.72%	24.17%
Income Tax Expense (Benefit)	<u>325</u>	<u>350</u>	<u>370</u>	<u>365</u>	<u>1,410</u>
<i>Tax Rate</i>	36.68%	36.01%	37.26%	38.71%	37.16%
Net Income	<u>\$ 561</u>	<u>\$ 622</u>	<u>\$ 623</u>	<u>\$ 578</u>	<u>\$ 2,384</u>
EPS -- Fully Diluted	<u>\$ 0.13</u>	<u>\$ 0.15</u>	<u>\$ 0.15</u>	<u>\$ 0.13</u>	<u>\$ 0.56</u>
Avg Shares Out-Fully Diluted	<u>4,255</u>	<u>4,265</u>	<u>4,275</u>	<u>4,285</u>	<u>4,270</u>
Percent of Revenue					
Cost of Revenues	55.06%	54.14%	53.92%	55.35%	54.62%
Sales, General and Administrative expenses	22.73%	21.91%	21.90%	21.89%	22.10%
YEAR / YEAR GROWTH					
Total Revenues	16.36%	16.30%	11.27%	10.42%	13.49%
Operating Income	34.02%	31.47%	16.46%	25.69%	26.34%
Pre-Tax Income	-43.33%	31.35%	17.38%	26.58%	-2.58%

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

	<u>FY2000A</u>	<u>FY2001A</u>	<u>FY2002A</u>	<u>Q1 2003A</u>
<i>Cash Flows from Operating Activities</i>				
Net Income	\$ 927	\$ 1,221	\$ 1,529	\$ 993
Depreciation and amortization	610	777	808	165
Gain on sale of marketable securities	(15)	(250)	(18)	347
Other than temporary reductions of marketable securities	-	-	236	(1,246)
Provision for doubtful accounts	-	15	-	-
Deferred income taxes	<u>150</u>	<u>48</u>	<u>(65)</u>	<u>44</u>
	1,672	1,812	2,490	302
<i>Changes In:</i>				
Accounts receivable	(216)	(150)	(119)	(296)
Other receivables	57	(53)	(8)	2
Inventories	(76)	119	80	(53)
Prepaid expenses and other assets	-	(34)	32	(3)
Accounts payable	(38)	26	96	59
Accrued expenses	50	(4)	20	(29)
Taxes payable	65	80	253	(148)
Net Changes in Working Capital	<u>(158)</u>	<u>(15)</u>	<u>355</u>	<u>(468)</u>
Net cash Provided by Operations	<u>1,514</u>	<u>1,797</u>	<u>2,845</u>	<u>(166)</u>
<i>Cash Flows from Investing Activities</i>				
Purchase of marketable securities	(8,808)	(9,247)	(3,316)	(2,029)
Sale of marketable securities	5,202	7,687	4,025	609
Sales of Assets	-	-	-	1,713
Change in margin account	75	357	(432)	-
Purchase of property, plant and equipment	<u>(1,096)</u>	<u>(713)</u>	<u>(259)</u>	<u>(63)</u>
Net cash used in Investing	<u>(4,627)</u>	<u>(1,916)</u>	<u>17</u>	<u>230</u>
<i>Cash Flows from Financing Activities</i>				
Repayment of notes payable	(91)	(94)	(675)	(8)
Purchase of treasury stock	-	(287)	(393)	-
Stock issuance costs	-	-	-	-
Net cash provided by Financing	<u>(91)</u>	<u>(381)</u>	<u>(1,068)</u>	<u>(8)</u>
Net change in Cash	(3,204)	(500)	1,795	56
Cash Beginning of Period	<u>4,641</u>	<u>1,437</u>	<u>936</u>	<u>2,731</u>
Cash End of Period	<u>\$ 1,437</u>	<u>\$ 936</u>	<u>\$ 2,731</u>	<u>\$ 2,787</u>