

DEAN FOODS CO
Form 10-Q
May 10, 2007

Table of Contents

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

Form 10-Q

(Mark One)

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the Quarterly Period Ended March 31, 2007**

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the Transition Period from to

Commission File Number 001-12755

Dean Foods Company

(Exact name of the registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

75-2559681
(I.R.S. employer
identification no.)

**2515 McKinney Avenue, Suite 1200
Dallas, Texas 75201
(214) 303-3400**
(Address, including zip code, and telephone number, including
area code, of the registrant's principal executive offices)

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 requirements for the past 90 days. Yes No

Edgar Filing: DEAN FOODS CO - Form 10-Q

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act.) Yes No

As of May 4, 2007, the number of shares outstanding of each class of common stock was:

Common Stock, par value \$0.01 129,997,167

Table of Contents

	Page
<u>Part I Financial Information</u>	
<u>Item 1 Financial Statements (Unaudited)</u>	3
<u>Item 2 Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	27
<u>Item 3 Quantitative and Qualitative Disclosures About Market Risk</u>	36
<u>Item 4 Controls and Procedures</u>	37
<u>Part II Other Information</u>	
<u>Item 1 Legal Proceedings</u>	39
<u>Item 1A Risk Factors</u>	39
<u>Item 2 Unregistered Sales of Equity Securities and Use of Proceeds</u>	41
<u>Item 6 Exhibits</u>	41
<u>Signatures</u>	42
<u>Certification of CEO Pursuant to Section 302</u>	
<u>Certification of CFO Pursuant to Section 302</u>	
<u>Certification of CEO Pursuant to Section 906</u>	
<u>Certification of CFO Pursuant to Section 906</u>	
<u>Supplemental Financial Information</u>	

Table of Contents**Part I Financial Information****Item 1. Financial Statements****DEAN FOODS COMPANY
CONDENSED CONSOLIDATED BALANCE SHEETS**

(Unaudited)

(In thousands, except share data)

	March 31, 2007	December 31, 2006
Assets		
Current assets:		
Cash and cash equivalents	\$ 37,954	\$ 31,140
Receivables, net	803,952	799,038
Inventories	380,137	360,754
Deferred income taxes	133,770	117,991
Prepaid expenses and other current assets	58,492	70,367
Total current assets	1,414,305	1,379,290
Property, plant and equipment, net	1,785,656	1,786,907
Goodwill	3,060,052	2,943,139
Identifiable intangible and other assets	636,402	640,857
Assets of discontinued operations		19,980
Total	\$ 6,896,415	\$ 6,770,173
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable and accrued expenses	\$ 841,904	\$ 822,122
Income taxes payable	9,638	30,776
Current portion of long-term debt	478,275	483,658
Total current liabilities	1,329,817	1,336,556
Long-term debt	2,885,166	2,872,193
Deferred income taxes	502,875	504,552
Other long-term liabilities	284,049	238,682
Liabilities of discontinued operations		8,791
Commitments and contingencies (Note 11)		
Stockholders equity:		
Preferred stock, none issued		
Common stock, 129,521,702 and 128,371,104 shares issued and outstanding, with a par value of \$0.01 per share	1,295	1,284
Additional paid-in capital	656,307	624,475

Edgar Filing: DEAN FOODS CO - Form 10-Q

Retained earnings	1,287,520	1,229,427
Accumulated other comprehensive loss	(50,614)	(45,787)
Total stockholders' equity	1,894,508	1,809,399
Total	\$ 6,896,415	\$ 6,770,173

See Notes to Condensed Consolidated Financial Statements.

-3-

Table of Contents

DEAN FOODS COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF INCOME

(Unaudited)

(In thousands, except share data)

	Three Months Ended March 31	
	2007	2006
Net sales	\$ 2,629,749	\$ 2,509,041
Cost of sales	1,942,474	1,857,695
Gross profit	687,275	651,346
Operating costs and expenses:		
Selling and distribution	415,635	405,145
General and administrative	109,390	102,281
Amortization of intangibles	2,322	1,421
Facility closing and reorganization costs	5,775	4,402
Total operating costs and expenses	533,122	513,249
Operating income	154,153	138,097
Other (income) expense:		
Interest expense	52,241	47,536
Other (income) expense, net	300	100
Total other expense	52,541	47,636
Income from continuing operations before income taxes	101,612	90,461
Income taxes	38,409	35,767
Income from continuing operations	63,203	54,694
Income (loss) from discontinued operations, net of tax	617	(1,902)
Net income	\$ 63,820	\$ 52,792
Average common shares:		
Basic	128,889,506	135,170,111
Diluted	134,521,467	142,409,989
Basic earnings per common share:		
Income from continuing operations	\$ 0.49	\$ 0.40
Income (loss) from discontinued operations	0.01	(0.01)
Net income	\$ 0.50	\$ 0.39
Diluted earnings per common share:		
Income from continuing operations	\$ 0.47	\$ 0.38
Loss from discontinued operations		(0.01)

Net income	\$	0.47	\$	0.37
------------	----	------	----	------

See Notes to Condensed Consolidated Financial Statements.

-4-

Table of Contents

DEAN FOODS COMPANY
CONDENSED STATEMENT OF STOCKHOLDERS EQUITY

(Unaudited)

(In thousands, except share data)

	Common Stock		Additional	Retained	Accumulated	Total	
	Shares	Amount	Paid-In	Earnings	Other	Stockholders	Comprehensive
			Capital		Comprehensive	Equity	Income
					Income		
					(Loss)		
Balance, December 31, 2006	128,371,104	\$ 1,284	\$ 624,475	\$ 1,229,427	\$ (45,787)	\$ 1,809,399	
Issuance of common stock	1,150,598	11	23,834			23,845	
Share-based compensation expense			8,303			8,303	
Net income				63,820		63,820	\$ 63,820
Other comprehensive income (Note 8):							
Change in fair value of derivative instruments, net of tax					(3,192)	(3,192)	(3,192)
Amounts reclassified to income statement related to hedging activities, net of tax					(1,240)	(1,240)	(1,240)
Cumulative translation adjustment					(395)	(395)	(395)
Adoption of FIN 48			(305)	(5,727)		(6,032)	
Comprehensive income							\$ 58,993
Balance, March 31, 2007	129,521,702	\$ 1,295	\$ 656,307	\$ 1,287,520	\$ (50,614)	\$ 1,894,508	

See Notes to Condensed Consolidated Financial Statements.

Table of Contents

DEAN FOODS COMPANY
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(In thousands)

	Three Months Ended March 31	
	2007	2006
Cash flows from operating activities:		
Net income	\$ 63,820	\$ 52,792
(Income) loss from discontinued operations	(617)	1,902
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	57,343	55,518
Share-based compensation expense	8,303	9,389
Loss on disposition of assets	802	618
Write-down of impaired assets	4,760	1,424
Deferred income taxes		38,106
Other	(133)	(193)
Changes in operating assets and liabilities, net of acquisitions:		
Receivables	469	42,258
Inventories	(17,126)	4,976
Prepaid expenses and other assets	8,681	(4,939)
Accounts payable and accrued expenses	9,740	(128,199)
Income taxes payable	1,966	(48,403)
Net cash provided by continuing operations	138,008	25,249
Net cash used in discontinued operations		(3,155)
Net cash provided by operating activities	138,008	22,094
Cash flows from investing activities:		
Additions to property, plant and equipment	(51,781)	(54,989)
Payments for acquisitions and investments, net of cash received	(125,839)	(9,760)
Proceeds from divestitures	10,706	
Proceeds from sale of fixed assets	1,550	1,836
Net cash used in continuing operations	(165,364)	(62,913)
Net cash used in discontinued operations		(5,509)
Net cash used in investing activities	(165,364)	(68,422)
Cash flows from financing activities:		
Proceeds from issuance of debt	83,500	65,198
Repayment of debt	(73,175)	(37,792)
Issuance of common stock related to share-based compensation	18,026	5,440
Tax savings on share-based compensation	5,819	22,680
Repurchase of common stock		(15,357)
Net cash provided by continuing operations	34,170	40,169

Edgar Filing: DEAN FOODS CO - Form 10-Q

Net cash provided by discontinued operations		8,588
Net cash provided by financing activities	34,170	48,757
Increase in cash and cash equivalents	6,814	2,429
Cash and cash equivalents, beginning of period	31,140	24,456
Cash and cash equivalents, end of period	\$ 37,954	\$ 26,885

See Notes to Condensed Consolidated Financial Statements.

-6-

Table of Contents

**DEAN FOODS COMPANY
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

Periods ended March 31, 2007 and 2006
(Unaudited)

1. General

Basis of Presentation The unaudited Condensed Consolidated Financial Statements contained in this Quarterly Report have been prepared on the same basis as the Consolidated Financial Statements in our Annual Report on Form 10-K for the year ended December 31, 2006. In our opinion, we have made all necessary adjustments (which include only normal recurring adjustments) in order to present fairly, in all material respects, our consolidated financial position, results of operations and cash flows as of the dates and for the periods presented. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted. Our results of operations for the period ended March 31, 2007 may not be indicative of our operating results for the full year. The Condensed Consolidated Financial Statements contained in this Quarterly Report should be read in conjunction with our 2006 Consolidated Financial Statements contained in our Annual Report on Form 10-K (filed with the Securities and Exchange Commission on March 1, 2007).

Certain reclassifications have been made to conform the prior year's Condensed Consolidated Financial Statements to the current year's classifications. During 2006, we reclassified the presentation of expense recognition for reusable packaging utilized in the distribution of our products from cost of sales to distribution expense. The reclassification reduced cost of sales and increased distribution expense by \$5.5 million for the three months ended March 31, 2006. The reclassification had no impact on net income.

On September 14, 2006, we completed the sale of our operations based in Spain. The sale of our remaining Iberian operations was completed in January 2007 following the conclusion of Portuguese regulatory proceedings. In our Condensed Consolidated Financial Statements for the three-month period ended March 31, 2007, the gain on the sale of the Iberian operations is presented as discontinued operations.

Unless otherwise indicated, references in this report to we, us or our refer to Dean Foods Company and its subsidiaries, taken as a whole.

Shipping and Handling Fees Our shipping and handling costs are included in both cost of sales and selling and distribution expense, depending on the nature of such costs. Shipping and handling costs included in cost of sales reflect inventory warehouse costs, product loading and handling costs. Our Dairy Group includes costs associated with transporting finished products from our manufacturing facilities to our own distribution warehouses within cost of sales while WhiteWave Foods Company includes these costs in selling and distribution expense. Shipping and handling costs included in selling and distribution expense consist primarily of route delivery costs for both company-owned delivery routes and independent distributor routes, to the extent that such independent distributors are paid a delivery fee, and the cost of shipping products to customers through third-party carriers. Shipping and handling costs recorded as a component of selling and distribution expense were approximately \$326.0 million and \$309.3 million for the first three months of 2007 and 2006, respectively.

Recently Adopted Accounting Pronouncements Effective January 1, 2007, we adopted Financial Interpretation No. (FIN) 48, Accounting for Uncertainty in Income Taxes. As a result of adopting the provisions of FIN 48, we recognized a \$25.9 million increase in our liability for uncertain tax positions to \$41.6 million, a \$20.1 million increase in deferred income tax assets, a \$305,000 decrease to additional paid-in capital, a \$265,000 decrease to

goodwill, and a \$5.7 million decrease to beginning retained earnings.

The amount of unrecognized tax benefits at March 31, 2007 recorded in other long-term liabilities is \$42.5 million, of which \$19.0 million would impact our effective tax rate and \$3.4 million would reduce goodwill if recognized. We do not expect any material changes to our liability for uncertain tax positions during the next 12 months.

Table of Contents

Consistent with periods prior to the adoption of FIN 48, we recognize accrued interest related to uncertain tax positions as a component of income tax expense. Penalties, if incurred, are recognized as a component of operating income. As of March 31, 2007, we have accrued approximately \$5.4 million for the payment of tax-related interest and penalties.

Our U.S. federal income tax returns for the years 2004 and 2005 are currently under examination by the Internal Revenue Service. We expect the examination of those years to be completed no earlier than the fourth quarter of 2008. State income tax returns are generally subject to examination for a period of 3 to 5 years after filing. We have various state income tax returns in the process of examination or appeals.

Recently Issued Accounting Pronouncements The Financial Accounting Standards Board (FASB) issued SFAS No. 157, Fair Value Measurements in September 2006. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles (GAAP), and expands disclosures about fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements but does not require any new fair value measurements. We do not believe the adoption of this standard will have a material impact on our Consolidated Financial Statements. This standard will become effective for us in the first quarter of 2008.

2. Acquisitions and Discontinued Operations

Acquisitions

Friendship Dairies On March 13, 2007, our Dairy Group completed the acquisition of Friendship Dairies, Inc., a manufacturer, marketer and distributor of cultured dairy products primarily in the northeastern United States. This transaction expanded our cultured dairy product capabilities and added a strong regional brand. We paid approximately \$130 million, including transaction costs, for the purchase of Friendship Dairies and funded the purchase price with borrowings under our senior credit facility. We have not completed a final allocation of the purchase price to the fair values of Friendship's assets and liabilities. The pro forma impact of this acquisition on consolidated net earnings would not have materially changed reported net earnings.

Discontinued Operations

Iberian Operations Our former Iberian operations included the manufacture and distribution of private label and branded milk across Spain and Portugal. On September 14, 2006, we completed the sale of our operations in Spain. In connection with the sale of our operations in Spain, we entered into an agreement to sell our Portuguese operations (that comprised the remainder of our Iberian operations) for approximately \$11.4 million subject to regulatory approvals and working capital settlements. We completed the sale of our Portuguese operations in January 2007, resulting in a gain of \$617,000.

Our financial statements have been reclassified to give effect to our Iberian operations as discontinued operations.

Major classes of assets and liabilities of our Iberian operations included in Assets and Liabilities of Discontinued Operations were as follows:

December 31,
2006
(In thousands)

Current assets	\$	14,255
Non-current assets		5,725
Current liabilities		8,791

Table of Contents**3. Inventories**

	March 31, 2007	December 31, 2006
	(In thousands)	
Raw materials and supplies	\$ 170,380	\$ 173,208
Finished goods	209,757	187,546
Total	\$ 380,137	\$ 360,754

4. Intangible Assets

Changes in the carrying amount of goodwill for the three months ended March 31, 2007 are as follows:

	Dairy Group	WhiteWave Foods Company (In thousands)	Total
Balance at December 31, 2006	\$ 2,408,413	\$ 534,726	\$ 2,943,139
Acquisitions(1)	117,521		117,521
Purchase accounting adjustments	(608)		(608)
Balance at March 31, 2007	\$ 2,525,326	\$ 534,726	\$ 3,060,052

(1) We have not completed a final allocation of the purchase price to the fair value of Friendship's assets and liabilities.

The gross carrying amount and accumulated amortization of our intangible assets other than goodwill as of March 31, 2007 and December 31, 2006 are as follows:

	March 31, 2007			December 31, 2006		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
	(In thousands)					
Intangible assets with indefinite lives:						
Trademarks	\$ 511,735	\$ (5,877)	\$ 505,858	\$ 511,294	\$ (5,877)	\$ 505,417
Intangible assets with finite lives:						

Edgar Filing: DEAN FOODS CO - Form 10-Q

Customer-related	70,177	(21,962)	48,215	72,789	(21,490)	51,299
Total	\$ 581,912	\$ (27,839)	\$ 554,073	\$ 584,083	\$ (27,367)	\$ 556,716

Amortization expense on intangible assets for the three months ended March 31, 2007 and 2006 was \$1.6 million in both periods.

Estimated aggregate intangible asset amortization expense for the next five years is as follows:

2007	\$ 6.1 million
2008	5.9 million
2009	5.8 million
2010	5.7 million
2011	3.9 million

Table of Contents**5. Long-Term Debt**

	March 31, 2007		December 31, 2006	
	Amount	Interest	Amount	Interest
	Outstanding	Rate	Outstanding	Rate
	(In thousands)			
Dean Foods debt obligations:				
Senior credit facility	\$ 1,784,500	7.74%	\$ 1,757,250	5.99%
Senior notes	498,148	7.00	498,112	7.00
	2,282,648		2,255,362	
Subsidiary debt obligations:				
Senior notes	572,980	6.625-8.15	572,037	6.625-8.15
Receivables-backed facility	500,400	5.67	512,500	5.68
Capital lease obligations and other	7,413		15,952	
	1,080,793		1,100,489	
	3,363,441		3,355,851	
Less current portion	(478,275)		(483,658)	
Total	\$ 2,885,166		\$ 2,872,193	

Senior Credit Facility During the three months ended March 31, 2007, our senior credit facility provided for a \$1.5 billion revolving credit facility and a \$1.39 billion term loan. At March 31, 2007, there was \$397 million outstanding under the revolving credit facility. Letters of credit in the aggregate amount of \$145.3 million were issued but undrawn. At March 31, 2007 approximately \$957.7 million was available for future borrowings under the revolving credit facility, subject to satisfaction of certain ordinary course conditions contained in the credit agreement.

During the three months ended March 31, 2007, both the revolving credit facility and term loan bore interest, at our election, at the base rate plus a margin that varied from zero to 25 basis points depending on our credit ratings (as issued by Standard & Poor's and Moody's), or LIBOR plus a margin that varied from 50 to 150 basis points, depending on our credit ratings (as issued by Standard & Poor's and Moody's). The weighted average blended interest rate in effect on borrowings under the senior credit facility, including the applicable interest rate margin, was 6.03% for the three months ended March 31, 2007. However, we had interest rate swap agreements in place that hedged \$450 million of our borrowings under the senior credit facility at an average rate of 4.21%, plus the applicable interest rate margin. Interest is payable quarterly or at the end of the applicable interest period.

Principal payments on the term loan were scheduled as follows:

\$56.3 million quarterly beginning December 31, 2006 through September 30, 2008;

\$262.5 million quarterly beginning on December 31, 2008 through June 30, 2009; and

A final payment of \$262.5 million on the maturity date of August 13, 2009.

No principal payments were due on the \$1.5 billion revolving credit facility until maturity on August 13, 2009.

The credit agreement also required mandatory principal prepayments upon the occurrence of certain asset dispositions or recovery events.

In consideration for the revolving commitment, we paid a quarterly commitment fee on unused amounts of the revolving credit facility that ranged from 12.5 to 30 basis points, depending on our credit ratings (as issued by Standard & Poor's and Moody's).

Table of Contents

The senior credit facility contained various financial and other restrictive covenants and required that we maintain certain financial ratios, including a maximum leverage and minimum interest coverage ratio. As of March 31, 2007, we were in compliance with all covenants contained in this credit agreement.

On April 2, 2007, we entered into an amended and restated credit agreement that replaced our senior credit facility in existence at March 31, 2007. See Note 13 for more information.

Dean Foods Senior Notes On May 17, 2006, we issued \$500 million aggregate principal amount of 7.0% senior unsecured notes. The senior unsecured notes mature on June 1, 2016 and interest is payable on June 1 and December 1 of each year, beginning December 1, 2006. The outstanding balance at March 31, 2007 was \$498.1 million.

The indenture under which we issued the senior unsecured notes does not contain financial covenants but does contain covenants that, among other things, limit our ability to incur secured indebtedness, enter into sale-leaseback transactions and engage in mergers, consolidations and sales of all or substantially all of our assets.

The notes are senior unsecured obligations and are effectively subordinated to the indebtedness outstanding under our senior credit facility and any other secured debt we may incur. The notes are fully and unconditionally guaranteed by the subsidiaries that are guarantors under our senior credit facility, which are substantially all of our wholly owned U.S. subsidiaries other than our receivables securitization subsidiaries.

We may, at our option, redeem some or all of the notes at any time at a redemption price equal to the greater of:

100% of the principal amount of the notes being redeemed; and

The sum of the present values of the remaining scheduled payments of principal and interest on the notes being redeemed (excluding interest accrued to the redemption date) from the redemption date to the maturity date discounted to the date of redemption on a semi-annual basis (assuming a 360-day year consisting of twelve 30-day months) at a discount rate equal to the Treasury rate plus 50 basis points, plus, in each case, accrued and unpaid interest on the principal amount being redeemed to the redemption date.

If we experience a change in control, we may be required to offer to purchase the notes at a purchase price equal to 101% of the principal amount, plus accrued and unpaid interest.

We used all of the net proceeds from the sale of the notes to reduce a corresponding amount of borrowings under our senior credit facility.

Subsidiary Senior Notes The former Dean Foods Company (Legacy Dean) had certain senior notes outstanding at the time of the acquisition, which remain outstanding. The notes carry the following interest rates and maturities:

\$250 million (\$250 million face value), at 8.15% interest, maturing in August 2007;

\$193.5 million (\$200 million face value), at 6.625% interest, maturing in May 2009; and

\$129.5 million (\$150 million face value), at 6.9% interest, maturing in October 2017.

The related indentures do not contain financial covenants but they do contain certain restrictions, including a prohibition against Legacy Dean and its subsidiaries granting liens on certain of their real property interests and a prohibition against Legacy Dean granting liens on the stock of its subsidiaries.

Receivables-Backed Facility We entered into a \$600 million receivables securitization facility pursuant to which certain of our subsidiaries sell their accounts receivable to three wholly-owned special purpose entities intended to be bankruptcy-remote. The special purpose entities then transfer the receivables to third party asset-backed commercial paper conduits sponsored by major financial institutions. The assets and liabilities of these three special purpose entities are fully reflected on our Condensed Consolidated Balance Sheet, and the securitization is treated as a borrowing for accounting purposes. During the first quarter of

Table of Contents

2007, we made net payments of \$12.1 million on this facility leaving an available and drawn balance of \$500.4 million at March 31, 2007. The receivables-backed facility bears interest at a variable rate based on the commercial paper yield as defined in the agreement. The average interest rate on this facility was 5.67% at March 31, 2007. Our ability to re-borrow under this facility is subject to a borrowing base formula.

On April 2, 2007 we entered into an amendment and restatement of our receivables facility. See Note 13 for more information.

Capital Lease Obligations and Other Capital lease obligations and other subsidiary debt includes various promissory notes for the purchase of property, plant and equipment and capital lease obligations. The various promissory notes payable provide for interest at varying rates and are payable in monthly installments of principal and interest until maturity, when the remaining principal balances are due. Capital lease obligations represent machinery and equipment financing obligations, which are payable in monthly installments of principal and interest and are collateralized by the related assets financed.

Interest Rate Agreements We have interest rate swap agreements in place that have been designated as cash flow hedges against variable interest rate exposure on a portion of our debt, with the objective of minimizing the impact of interest rate fluctuations and stabilizing cash flows. These swap agreements provide hedges for loans under our senior credit facility by fixing the LIBOR interest rates specified in the senior credit facility at the interest rates noted below until the indicated expiration dates of these interest rate swap agreements. In anticipation of the recapitalization of our balance sheet, in March 2007 we entered into a \$2.95 billion forward starting interest rate swap. The notional amount of the swap will decline from \$2.95 billion to \$1.25 billion over its term. This swap became effective on April 2, 2007. For additional information see Note 13.

The following table summarizes our various interest rate agreements at March 31, 2007:

Fixed Interest Rates	Expiration Date	Notional Amounts (In millions)
4.07% to 4.27%	December 2010	\$ 450
4.907%	March 2008-March 2012	2,950

The following table summarizes our various interest rate agreements at December 31, 2006:

Fixed Interest Rates	Expiration Date	Notional Amounts (In millions)
4.81% to 4.84%	December 2007	\$ 500
4.07% to 4.27%	December 2010	450

During the three months ended March 31, 2007, we settled the interest rate swaps expiring in 2007. Amounts included in Other Comprehensive Income related to these swaps will be recognized over the originally forecasted period.

These swaps are required to be recorded as an asset or liability on our Condensed Consolidated Balance Sheet at fair value, with an offset to other comprehensive income to the extent the hedge is effective. Derivative gains and losses included in other comprehensive income are reclassified into earnings as the underlying transaction occurs. Any ineffectiveness in our hedges is recorded as an adjustment to interest expense.

Table of Contents

As of March 31, 2007 and December 31, 2006, our derivative asset and liability balances were:

	March 31, 2007	December 31, 2006
	(In thousands)	
Current derivative asset	\$ 3,405	\$ 6,525
Long-term derivative asset	6,656	8,322
Total derivative asset	\$ 10,061	\$ 14,847
Long-term derivative liability	(2,600)	
Total derivative liability	\$ (2,600)	\$

There was no hedge ineffectiveness for the quarter ended March 31, 2007. Approximately \$1.2 million of interest income (net of taxes) was reclassified to interest expense from other comprehensive income during the quarter ended March 31, 2007. We estimate that approximately \$3.0 million of net derivative income (net of taxes) included in other comprehensive income will be reclassified into earnings within the next 12 months. These gains will partially offset the higher interest payments recorded on our variable rate debt.

We are exposed to market risk under these arrangements due to the possibility of interest rates on the credit facilities falling below the rates on our interest rate swap agreements. Credit risk under these arrangements is remote because the counterparties to our interest rate swap agreements are major financial institutions.

Guarantor Information On May 17, 2006, we issued \$500 million aggregate principal amount of 7.0% senior notes. The senior notes are unsecured obligations and are fully and unconditionally guaranteed by substantially all of our wholly-owned U.S. subsidiaries other than our receivables securitization subsidiaries.

Table of Contents

The following condensed consolidating financial statements present the financial position, results of operations and cash flows of Dean Foods (Parent), the subsidiary guarantors of the senior notes and separately the combined results of the subsidiaries that are not a party to the guarantees. The non-guarantor subsidiaries reflect our foreign subsidiary operations in addition to our three receivables securitization subsidiaries. We do not allocate interest expense from the receivables-backed facility to the three receivables securitization subsidiaries. Therefore, the interest costs related to this facility are reflected within the guarantor financial information presented.

Condensed Consolidating Balance Sheet as of March 31, 2007

	Parent	Guarantor Entities	Non- Guarantor Subsidiaries (In thousands)	Eliminations	Consolidated Totals
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 4,943	\$ 28,838	\$ 4,173	\$	\$ 37,954
Receivables, net		23,110	780,842		803,952
Intercompany receivables	353,573	3,003,857	278,216	(3,635,646)	
Other current assets	116,964	455,425	10		572,399
Total current assets	475,480	3,511,230	1,063,241	(3,635,646)	1,414,305
Property, plant and equipment, net	214	1,767,164	18,278		1,785,656
Goodwill		3,059,961	91		3,060,052
Identifiable intangible and other assets	50,291	586,107	4		636,402
Investment in subsidiaries	6,752,808			(6,752,808)	
Total	\$ 7,278,793	\$ 8,924,462	\$ 1,081,614	\$ (10,388,454)	\$ 6,896,415
LIABILITIES AND STOCKHOLDERS EQUITY					
Current liabilities:					
Accounts payable and accrued expenses	\$ 58,886	\$ 782,696	\$ 322	\$	\$ 841,904
Income taxes payable	41,396	(31,890)	132		9,638
Intercompany notes	2,499,573	633,178	502,895	(3,635,646)	
Current portion of long-term debt	225,000	253,275			478,275
Total current liabilities	2,824,855	1,637,259	503,349	(3,635,646)	1,329,817
Long-term debt	2,057,648	327,118	500,400		2,885,166
Other long-term liabilities	501,782	285,142			786,924
Total stockholders' equity	1,894,508	6,674,943	77,865	(6,752,808)	1,894,508
Total	\$ 7,278,793	\$ 8,924,462	\$ 1,081,614	\$ (10,388,454)	\$ 6,896,415

Table of Contents

Condensed Consolidating Balance Sheet as of December 31, 2006

	Parent	Guarantor Entities	Non- Guarantor Subsidiaries (In thousands)	Eliminations	Consolidated Totals
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 579	\$ 26,254	\$4,307	\$	\$ 31,140
Receivables, net	301	32,720	766,017		799,038
Intercompany receivables	126,707	2,702,858	309,747	(3,139,312)	
Other current assets	105,882	443,210	20		549,112
Total current assets	233,469	3,205,042	1,080,091	(3,139,312)	1,379,290
Property, plant and equipment, net	608	1,767,734	18,565		1,786,907
Goodwill		2,943,048	91		2,943,139
Identifiable intangible and other assets	54,410	586,443	4		640,857
Investment in subsidiaries	6,507,028			(6,507,028)	
Assets of discontinued operations			19,980		19,980
Total	\$ 6,795,515	\$ 8,502,267	\$1,118,731	\$ (9,646,340)	\$ 6,770,173
LIABILITIES AND STOCKHOLDERS EQUITY					
Current liabilities:					
Accounts payable and accrued expenses	\$ 39,077	\$ 782,507	\$538	\$	\$ 822,122
Income taxes payable	28,347	2,295	134		30,776
Intercompany notes	2,194,952	437,725	506,635	(3,139,312)	
Current portion of long-term debt	225,000	258,658			483,658
Total current liabilities	2,487,376	1,481,185	507,307	(3,139,312)	1,336,556
Long-term debt	2,030,362	329,331	512,500		2,872,193
Other long-term liabilities	468,378	274,856			743,234
Liabilities of discontinued operations			8,791		8,791
Total stockholders equity	1,809,399	6,416,895	90,133	(6,507,028)	1,809,399
Total	\$ 6,795,515	\$ 8,502,267	\$1,118,731	\$ (9,646,340)	\$ 6,770,173

Table of Contents

Condensed Consolidating Statement of Income for the Three Months Ended March 31, 2007					
	Parent	Guarantor Entities	Non- Guarantor Subsidiaries (In thousands)	Eliminations	Consolidated Totals
Net sales	\$	\$ 2,628,457	\$ 1,292	\$	\$ 2,629,749
Cost of sales		1,941,495	979		1,942,474
Gross profit		686,962	313		687,275
Selling and distribution		415,495	140		415,635
General and administrative	1,402	109,402	908		111,712
Facility closing and reorganization costs		5,775			5,775
Interest expense	33,691	18,503	47		52,241
Other (income) expense, net	378	(90)	12		300
Income from subsidiaries	(137,083)			137,083	
Income (loss) from continuing operations before income taxes	101,612	137,877	(794)	(137,083)	101,612
Income taxes	38,409	52,019	(306)	(51,713)	38,409
Income (loss) from continuing operations	63,203	85,858	(488)	(85,370)	63,203
Income from discontinued operations, net of tax			617		617
Net income (loss)	\$ 63,203	\$ 85,858	\$ 129	\$ (85,370)	\$ 63,820

Table of Contents

Condensed Consolidating Statement of Income for the Three Months Ended March 31, 2006					
	Parent	Guarantor Entities	Non- Guarantor Subsidiaries (In thousands)	Eliminations	Consolidated Totals
Net sales	\$	\$ 2,507,606	\$ 1,435	\$	\$ 2,509,041
Cost of sales		1,856,590	1,105		1,857,695
Gross profit		651,016	330		651,346
Selling and distribution		404,983	162		405,145
General and administrative	1,577	101,892	233		103,702
Facility closing and reorganization costs		4,402			4,402
Interest expense	28,927	18,682	(73)		47,536
Other (income) expense, net	(10)	(235)	345		100
Income from subsidiaries	(120,955)			120,955	
Income (loss) from continuing operations before income taxes	90,461	121,292	(337)	(120,955)	90,461
Income taxes	35,767	46,988	(133)	(46,855)	35,767
Income (loss) from continuing operations	54,694	74,304	(204)	(74,100)	54,694
Loss from discontinued operations, net of tax			(1,902)		(1,902)
Net income (loss)	\$ 54,694	\$ 74,304	\$ (2,106)	\$ (74,100)	\$ 52,792

Condensed Consolidating Statement of Cash Flows
for the Three Months Ended March 31, 2007

	Parent	Guarantor Entities	Non- Guarantor Subsidiaries (In thousands)	Consolidated Totals
Net cash provided by (used in) operating activities	\$ 41,955	\$ 111,309	\$ (15,256)	\$ 138,008
Additions to property, plant and equipment	(262)	(51,431)	(88)	(51,781)
Payments for acquisitions and investments, net of cash received	(125,839)			(125,839)
Net proceeds from divestitures	10,706			10,706
Proceeds from sale of fixed assets		1,550		1,550
Net cash used in investing activities		(115,395)	(49,881)	(165,364)
Proceeds from issuance of debt		83,500		83,500

Edgar Filing: DEAN FOODS CO - Form 10-Q

Repayment of debt	(56,250)	(4,825)	(12,100)	(73,175)
Issuance of common stock, net of expenses	18,026			18,026
Tax savings on share-based compensation	5,819			5,819
Net cash provided by (used in) financing activities	51,095	(4,825)	(12,100)	34,170
Net change in intercompany balances	26,709	(54,019)	27,310	
Increase (decrease) in cash and cash equivalents	4,364	2,584	(134)	6,814
Cash and cash equivalents, beginning of period	579	26,254	4,307	31,140
Cash and cash equivalents, end of period	\$ 4,943	\$ 28,838	\$ 4,173	\$ 37,954

-17-

Table of Contents

Condensed Consolidating Statement of Cash Flows
for the Three Months Ended March 31, 2006

	Parent	Guarantor Entities	Non- Guarantor Subsidiaries	Consolidated Totals
	(In thousands)			
Net cash provided by (used in) operating activities	\$ (25,826)	\$ (14,735)	\$ 62,655	\$ 22,094
Additions to property, plant and equipment	(439)	(53,337)	(1,213)	(54,989)
Payments for acquisitions and investments, net of cash received	(9,760)			(9,760)
Proceeds from sale of fixed assets		1,836		1,836
Other			(5,509)	(5,509)
Net cash used in investing activities	(10,199)	(51,501)	(6,722)	(68,422)
Proceeds from issuance of debt	65,198			65,198
Repayment of debt		(2,280)	(35,512)	(37,792)
Issuance of common stock, net of expenses	5,440			5,440
Tax savings on share-based compensation	22,680			22,680
Repurchase of common stock	(15,357)			(15,357)
Other			8,588	8,588
Net cash provided by (used in) financing activities	77,961	(2,280)	(26,924)	48,757
Net change in intercompany balances	(42,134)	71,898	(29,764)	
Increase (decrease) in cash and cash equivalents	(198)	3,382	(755)	2,429
Cash and cash equivalents, beginning of period	250	18,677	5,529	24,456
Cash and cash equivalents, end of period	\$ 52	\$ 22,059	\$ 4,774	\$ 26,885

6. Share-Based Compensation

Stock Options The following table summarizes stock option activity during the first three months of 2007:

	Options	Weighted Average Exercise Price	Weighted Average Contractual Life	Aggregate Intrinsic Value
Options outstanding at December 31, 2006	15,322,398	\$ 23.09		
Options granted during the first three months	2,020,175	44.28		
Options canceled or forfeited during the first three months(1)	(51,696)	31.66		
	(1,021,643)	18.90		

Options exercised during the first three months

Options outstanding at March 31, 2007	16,269,234	25.96	6.40	\$ 338,121,111
Options exercisable at March 31, 2007	11,697,456	20.76	5.35	303,921,185

(1) Pursuant to the terms of our stock option plans, options that are canceled or forfeited become available for future grants.

During the three months ended March 31, 2007 and 2006, we recognized stock option expense of \$5.1 million and \$5.0 million, respectively.

Table of Contents

Stock Units The following table summarizes stock unit activity during the first three months of 2007:

	Employees	Directors	Total
Stock units outstanding at December 31, 2006	774,261	69,676	843,937
Stock units issued during the first three months	413,500		413,500
Shares issued during first three months upon vesting of stock units	(122,089)		(122,089)
Stock units cancelled or forfeited during the first three months(1)	(60,716)		(60,716)
Stock units outstanding at March 31, 2007	1,004,956	69,676	1,074,632
Weighted average grant date fair value	\$ 38.21	\$ 35.47	\$ 38.07

(1) Pursuant to the terms of our stock unit plans, stock units that are canceled or forfeited become available for future grants.

During the three months ended March 31, 2007 and 2006, we recognized stock unit expense of \$3.2 million and \$4.4 million, respectively.

The stock option and stock unit information listed above has not been adjusted for the special cash dividend that occurred on April 2, 2007. See Note 13 for more information.

7. Earnings Per Share

Basic earnings per share is based on the weighted average number of common shares outstanding during each period. Diluted earnings per share is based on the weighted average number of common shares outstanding and the effect of all dilutive common stock equivalents outstanding during each period.

The following table reconciles the numerators and denominators used in the computations of both basic and diluted earnings per share (EPS):

	Three Months Ended March 31	
	2007	2006
	(In thousands, except share data)	
Basic EPS computation:		
Numerator:		
Income from continuing operations	\$ 63,203	\$ 54,694
Denominator:		
Average common shares	128,889,506	135,170,111
Basic EPS from continuing operations	\$ 0.49	\$ 0.40
Diluted EPS computation:		
Numerator:		
Income from continuing operations	\$ 63,203	\$ 54,694
Denominator:		

Edgar Filing: DEAN FOODS CO - Form 10-Q

Average common shares basic	128,889,506	135,170,111
Stock option conversion(1)	5,406,785	6,165,261
Stock units	225,176	1,074,617
Average common shares diluted	134,521,467	142,409,989
Diluted EPS from continuing operations	\$ 0.47	\$ 0.38

(1) Stock option conversion excludes anti-dilutive shares of 1,121,578 and 2,359,901 at March 31, 2007 and 2006, respectively.

Table of Contents**8. Comprehensive Income (Loss)**

The components of comprehensive income (loss) are summarized below.

	Pre-Tax Income (Loss)	Tax Benefit (Expense) (In thousands)	Net Amount
Accumulated other comprehensive income (loss), December 31, 2006	\$ (75,156)	\$ 29,369	\$ (45,787)
Cumulative translation adjustment arising during period	(395)		(395)
Net change in fair value of derivative instruments	(5,506)	2,314	(3,192)
Amounts reclassified to income statement related to derivatives	(1,993)	753	(1,240)
Accumulated other comprehensive income (loss), March 31, 2007	\$ (83,050)	\$ 32,436	\$ (50,614)

9. Employee Retirement and Postretirement Benefits

Defined Benefit Plans The benefits under our defined benefit plans are based on years of service and employee compensation.

	Three Months Ended March 31	
	2007	2006
	(In thousands)	
Components of net period cost:		
Service cost	\$ 675	\$ 689
Interest cost	4,246	3,833
Expected return on plan assets	(4,681)	(3,843)
Amortizations:		
Unrecognized transition obligation	28	28
Prior service cost	211	156
Unrecognized net loss	719	931
Effect of settlement		584
Net periodic benefit cost	\$ 1,198	\$ 2,378

We expect to contribute \$23.2 million to our defined benefit plans during 2007.

Postretirement Benefits Certain of our subsidiaries provide healthcare benefits to certain retirees who are covered under specific group contracts.

Table of Contents

	Three Months Ended March 31	
	2007	2006
	(In thousands)	
Components of net period cost:		
Service cost	\$ 358	\$ 301
Interest cost	411	333
Amortizations:		
Prior service cost	(17)	(18)
Unrecognized net loss	266	99
Net periodic benefit cost	\$ 1,018	\$ 715

We expect to contribute \$2.4 million to our postretirement health plans during 2007.

10. Facility Closing And Reorganization Costs

We recorded net facility closing and reorganization costs of \$5.8 million and \$4.4 million during the three months ended March 31, 2007 and 2006, respectively.

The charges recorded during the first three months of 2007 are primarily related to the realignment of our Dairy Group's finance organization and the closing of Dairy Group facilities in Akron, Ohio; Detroit, Michigan; and Union, New Jersey.

Activity for the first three months of 2007 is summarized below:

	Accrued Charges at December 31, 2006	Charges	Payments	Accrued Charges at March 31, 2007
	(In thousands)			
Cash charges:				
Workforce reduction costs	\$ 4,322	\$ 3,502	\$ (3,319)	\$ 4,505
Shutdown costs	16	759	(760)	15
Lease obligations after shutdown	1,313	267	(418)	1,162
Other	216	442	(530)	128
Subtotal	\$ 5,867	4,970	\$ (5,027)	\$ 5,810
Noncash charges:				
Write-down of assets		805		
Total charges		\$ 5,775		

The write-down of assets relate primarily to owned buildings, land and equipment of those facilities identified for closure. The assets are written down to their estimated fair value and held for sale. The effect of suspending depreciation on the buildings and equipment related to the closed facilities was not significant. The carrying value of closed facilities at March 31, 2007 was approximately \$11.9 million. We are marketing these properties for sale.

We expect to incur additional charges related to these restructuring plans of approximately \$12.9 million, including approximately \$7.4 million in work force reduction costs and approximately \$5.5 million in shutdown and other costs. Approximately \$12.0 million and \$800,000 of these additional charges are expected to be completed by December 31, 2007 and 2008, respectively.

Table of Contents

The principal components of our continuing reorganization and cost reduction efforts include the following:

Workforce reductions as a result of facility closings, facility reorganizations and consolidation of administrative functions;

Shutdown costs, including those costs necessary to prepare abandoned facilities for closure; and

Costs incurred after shutdown, such as lease obligations or termination costs, utilities and property taxes.

We consider several factors when evaluating a potential facility closure, including, among other things, the impact of such a closure on our customers, the impact on production, distribution and overhead costs, the investment required to complete any such closure, and the impact on future investment decisions. Some facility closures are pursued to improve our operating cost structure, while others enable us to avoid unnecessary capital expenditures, allowing us to more prudently invest our capital expenditure dollars in our production facilities and better serve our customers.

11. Commitments and Contingencies

Contingent Obligations Related to Divested Operations We have divested several businesses in recent years. In each case, we have retained certain known contingent obligations related to those businesses and/or assumed an obligation to indemnify the purchasers of the businesses for certain unknown contingent liabilities, including environmental liabilities. We believe we have established adequate reserves for potential liabilities and indemnifications related to our divested businesses. Moreover, we do not expect any liability that we may have for these retained liabilities, or any indemnification liability, to materially exceed amounts accrued.

Contingent Obligations Related to Milk Supply Arrangements On December 21, 2001, in connection with our acquisition of the former Dean Foods Company, we purchased Dairy Farmers of America's (DFA) 33.8% interest in our Dairy Group. In connection with that transaction, we entered into two agreements with DFA designed to ensure that DFA has the opportunity to continue to supply raw milk to certain of our facilities, or be paid for the loss of that business. One such agreement is a promissory note with a 20-year term that bears interest based on the consumer price index. Interest will not be paid in cash but will be added to the principal amount of the note annually, up to a maximum principal amount of \$96 million. We may prepay the note in whole or in part at any time, without penalty. The note will only become payable if we materially breach or terminate one of our milk supply agreements with DFA without renewal or replacement. Otherwise, the note will expire in 2021, without any obligation to pay any portion of the principal or interest. Payments made under the note, if any, would be expensed as incurred. The other agreement would require us to pay damages to DFA if we fail to offer DFA the right to supply milk to certain facilities that we acquired as part of the former Dean Foods after the pre-existing agreements with certain other suppliers or producers expire. We have not breached or terminated any of our milk supply agreements with DFA.

Insurance We retain selected levels of property and casualty risks, primarily related to employee health care, workers compensation claims and other casualty losses. Many of these potential losses are covered under conventional insurance programs with third party carriers with high deductible limits. In other areas, we are self-insured with stop-loss coverages. These deductibles range from \$350,000 for medical claims to \$2.0 million for casualty claims. We believe we have established adequate reserves to cover these claims.

During 2005, we experienced operational disruptions in our Dairy Group segment caused by Hurricanes Katrina and Rita. Our insurance policies cover a portion of our business interruption losses for 12 months following the restoration of our property. During the first quarter of 2006, we settled certain business interruption claims for \$3.1 million. During the first quarter of 2007, we settled the remaining claims for \$4.8 million. These amounts are recorded within

cost of sales.

Leases and Purchase Obligations We lease certain property, plant and equipment used in our operations under both capital and operating lease agreements. Such leases, which are primarily for machinery, equipment and vehicles, have lease terms ranging from one to 20 years. Certain of the operating lease

Table of Contents

agreements require the payment of additional rentals for maintenance, along with additional rentals based on miles driven or units produced. Certain leases require us to guarantee a minimum value of the leased asset at the end of the lease. Our maximum exposure under those guarantees is not a material amount.

We have entered into various contracts obligating us to purchase minimum quantities of raw materials used in our production processes, including organic soybeans and organic raw milk. We enter into these contracts from time to time to ensure a sufficient supply of raw ingredients. We expect to utilize all quantities under the purchase commitments in the normal course of business. In addition, we have contractual obligations to purchase various services that are part of our production process.

Litigation, Investigations and Audits We are not party to, nor are our properties the subject of, any material pending legal proceedings. However, we are parties from time to time to certain claims, litigation, audits and investigations. We believe that we have established adequate reserves to satisfy any potential liability we may have under all such claims, litigations, audits and investigations that are currently pending. In our opinion, the settlement of any such currently pending or threatened matter is not expected to have a material adverse impact on our financial position, results of operations or cash flows.

Two shareholder derivative complaints were filed in July and October 2006 in the district court of Dallas County, Texas, which alleged stock option backdating. The complaints named certain current and former members of the Board of Directors and certain current and former members of management. In response to the litigation, a special litigation committee of our Board of Directors was established in August 2006. The Committee, consisting of independent board members not named in the litigation, conducted its own independent review of our stock option grants and the allegations made in the complaints and determined that there were no fraudulent acts by management. The derivative actions were settled in the first quarter of 2007. The settlement resolves all claims and includes no finding of wrongdoing on the part of any of the defendants and no cash payment other than attorneys' fees. The Company has agreed to adoption and implementation of stock option grant procedures that reflect developing best practices. The district court approved the settlement and the actions were dismissed.

As previously announced, the staff of the SEC began an informal inquiry into our historical stock option practices. On May 7, 2007, the staff of the SEC notified us that the informal inquiry was closed without any recommended enforcement action.

12. Segment Information

We have two reportable segments: the Dairy Group and WhiteWave Foods Company.

Our Dairy Group segment is our largest segment. It manufactures, markets and distributes a wide variety of branded and private label dairy case products, such as milk, cream, ice cream, cultured dairy products and juices, to retailers, distributors, foodservice outlets, schools and governmental entities across the United States.

Our WhiteWave Foods Company segment manufactures, develops, markets and sells a variety of nationally branded soy, dairy and dairy-related products, such as *Silk*[®] soymilk and cultured soy products, *Horizon Organic*[®] dairy products, *International Delight*[®] coffee creamers, *LAND O LAKES*[®] creamer and fluid dairy products and *Rachel's Organic*[®] dairy products. WhiteWave Foods Company sells its products to a variety of customers, including grocery stores, club stores, natural foods stores, mass merchandisers, convenience stores and foodservice outlets. A portion of our WhiteWave Foods Company's products are sold through the Dairy Group's distribution network. Those sales, together with their related costs, are included in WhiteWave Foods Company for segment reporting purposes.

We evaluate the performance of our segments based on operating profit or loss before gains and losses on the sale of assets, facility closing and reorganization costs and foreign exchange gains and losses. In addition, the expense related to share-based compensation has not been allocated to our segments and is reflected entirely within the caption

Corporate . Therefore, the measure of segment profit or loss presented below is before such items. The accounting policies of our segments are the same as those described in the summary of

Table of Contents

significant accounting policies set forth in Note 1 to our 2006 Consolidated Financial Statements contained in our 2006 Annual Report on Form 10-K.

Due to changes in the Company's business strategy, primary responsibility for the Hershey relationship has been moved into the Dairy Group beginning in the first quarter of 2007. In addition, we aligned the results related to the sales of certain foodservice products between segments. In order to present results on a comparable basis, segment results for 2006 have been adjusted to reflect the way management evaluates performance related to the Hershey relationship, as well as certain foodservice relationships. These changes had no impact on consolidated operating income.

The amounts in the following tables are obtained from reports used by our executive management team and do not include any allocated income taxes or management fees. There are no significant non-cash items reported in segment profit or loss other than depreciation and amortization.

	Three Months Ended March 31	
	2007	2006
	(In thousands)	
Net sales to external customers:		
Dairy Group	\$ 2,307,062	\$ 2,207,660
WhiteWave Foods Company	322,687	301,381
Total	\$ 2,629,749	\$ 2,509,041
Intersegment sales:		
Dairy Group	\$ 4,211	\$ 3,423
WhiteWave Foods Company	24,081	23,122
Total	\$ 28,292	\$ 26,545
Operating income:		
Dairy Group	\$ 171,053	\$ 156,632
WhiteWave Foods Company	27,775	22,213
Corporate/Other	(38,900)	(36,346)
Segment operating income	159,928	142,499
Facility closing and reorganization costs	(5,775)	(4,402)
Total	\$ 154,153	\$ 138,097
	March 31, 2007	December 31, 2006
	(In thousands)	

Assets:

Edgar Filing: DEAN FOODS CO - Form 10-Q

Dairy Group	\$ 5,287,890	\$ 5,141,662
WhiteWave Foods Company	1,363,200	1,372,946
Corporate	245,325	235,585
Discontinued operations		19,980
Total	\$ 6,896,415	\$ 6,770,173

Geographic Information Less than 1% of our net sales and long-lived assets relate to operations outside of the United States.

Significant Customers Our WhiteWave Foods Company and Dairy Group segments each had a single customer that represented greater than 10% of their net sales in the first three months of 2007 and 2006.

Table of Contents

Approximately 18.8% and 17.8% of our consolidated net sales in the first quarter of 2007 and 2006, respectively, were to this same customer.

13. Subsequent Events

Credit Facilities and Special Cash Dividend

On April 2, 2007, we recapitalized our balance sheet through the completion of \$4.8 billion of new senior credit facilities and the return of \$1.94 billion to shareholders of record on March 27, 2007, through a \$15.00 per share special cash dividend. The number and exercise price of stock options and stock units outstanding at the time of the special cash dividend were proportionately adjusted to maintain their aggregate fair value before and after the special cash dividend.

We entered into an amended and restated credit agreement that consists of a combination of a \$1.5 billion 5-year senior secured revolving credit facility, a \$1.5 billion 5-year senior secured term loan A, and a \$1.8 billion 7-year senior secured term loan B. The proceeds of the new senior credit facilities may be used:

To finance a special cash dividend to our shareholders;

To refinance the existing senior credit facilities;

To finance our working capital needs; and

For general corporate purposes of the Company and its subsidiaries in the ordinary course of business, including acquisitions.

The term loan A is payable in 12 consecutive quarterly installments of:

\$56.25 million in each of the first eight installments, beginning on June 30, 2009 and ending on March 31, 2011 and;

\$262.5 million in each of the next four installments, beginning on June 30, 2011 and ending on April 2, 2012.

The term loan B will amortize 1% per year on a quarterly basis, with any remaining principal balance due at final maturity, April 2, 2014. The revolving credit facility will be available for the issuance of up to \$350 million of letters of credit and up to \$150 million for swing line loans. No principal payments are due on the new \$1.5 billion revolving credit facility until maturity on April 2, 2012. The new credit agreement also requires mandatory principal prepayments upon the occurrence of certain asset dispositions or recovery events.

The new credit facility contains various financial and other restrictive covenants and requires that we comply with certain financial ratios, including a maximum leverage ratio and a minimum interest coverage ratio.

Our new credit agreement permits us to complete acquisitions that meet the following conditions without obtaining prior approval: (1) the acquired company is involved in the manufacture, processing and distribution of food or packaging products or any other line of business in which we are currently engaged, (2) the net cash purchase price for any single acquisition is not greater than \$500 million, (3) we acquire at least 51% of the acquired entity, (4) the transaction is approved by the board of directors or shareholders, as appropriate, of the target and (5) after giving effect to such acquisition on a pro forma basis, we would have been in compliance with all financial covenants. All other acquisitions must be approved in advance by the required lenders.

The new senior credit facility contains limitations on liens, investments and the incurrence of additional indebtedness, and prohibits certain dispositions of property and conditionally restricts certain payments, including dividends. The new senior credit facility is secured by liens on substantially all of our domestic assets including the assets of our subsidiaries, but excluding the capital stock of Legacy Dean's subsidiaries, and the real property owned by Legacy Dean and its subsidiaries.

Table of Contents

The new credit agreement contains standard default triggers, including without limitation: failure to maintain compliance with the financial and other covenants contained in the credit agreement, default on certain of our other debt, a change in control and certain other material adverse changes in our business. The new credit agreement does not contain any default triggers based on our credit rating.

Interest on the outstanding balances under the new senior credit facilities is payable, at our election, at the Alternative Base Rate plus a margin depending on our Leverage Ratio (as defined in our new credit agreement) or LIBOR plus a margin depending on our Leverage Ratio (as defined in our new credit agreement). The Applicable Base Rate margin under our revolving credit and term loan A facilities varies from zero to 75 basis points while the Applicable LIBOR Rate margin varies from 62.5 to 175 basis points. The Applicable Base Rate margin under our term loan facility B varies from 37.5 to 75 basis points while the Applicable LIBOR Rate margin varies from 137.5 to 175 basis points.

As discussed in Note 5, consistent with our overall risk management strategy, we entered into a \$2.95 billion interest rate swap at a fixed interest rate of 4.907%.

In consideration for the new revolving commitment, we are required to pay a quarterly commitment fee on unused amounts of the revolving credit facility that range from 12.5 to 37.5 basis points, depending on our Leverage Ratio (as defined under our new credit agreement).

In addition, on April 2, 2007 we entered into an amendment and restatement of our receivables facility which extended the facility termination date from November 15, 2009 to April 2, 2010. We believe that other modifications related to this amendment will slightly increase our borrowing capacity under the facility.

The pro forma effect of the recapitalization completed on April 2, 2007 is included in the table below:

	March 31, 2007	
	As Reported	Pro forma
	(In thousands)	
Total debt	\$ 3,363,441	\$ 5,324,541
Stockholders equity (deficit)	1,894,508	(49,193)
Total capitalization	\$ 5,257,949	\$ 5,275,348

Table of Contents

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

Business Overview

We are a leading food and beverage company. Our Dairy Group is the largest processor and distributor of milk and various other dairy products in the United States. The Dairy Group manufactures and sells its products under a variety of local and regional brand names and under private labels. Our WhiteWave Foods Company segment manufactures, markets and sells a variety of well known soy, dairy and dairy-related nationally branded products.

Dairy Group Our Dairy Group segment is our largest segment, with approximately 88% of our consolidated net sales in the three months ended March 31, 2007. Our Dairy Group manufactures, markets and distributes a wide variety of branded and private label dairy case products, such as milk, cream, ice cream, cultured dairy products and juices to retailers, distributors, foodservice outlets, schools and governmental entities across the United States. Due to the perishable nature of the Dairy Group's products, our Dairy Group delivers the majority of its products directly to its customers' stores in refrigerated trucks or trailers that we own or lease. This form of delivery is called a "direct store delivery" or "DSD" system and we believe we have one of the most extensive refrigerated DSD systems in the United States. The Dairy Group sells its products primarily on a local or regional basis through its local and regional sales forces, although some national customer relationships are coordinated by the Dairy Group's corporate sales department. Most of the Dairy Group's customers, including its largest customer, purchase products from the Dairy Group either by purchase order or pursuant to contracts that are generally terminable at will by the customer.

WhiteWave Foods Company WhiteWave Foods Company manufactures, develops, markets and sells a variety of nationally-branded soy, dairy and dairy-related products, such as *Silk* soymilk and cultured soy products; *Horizon Organic* dairy and other products; *International Delight* coffee creamers; *LAND O LAKES* creamers and fluid dairy products and *Rachel's Organic* dairy products. WhiteWave Foods Company also sells *The Organic Cow*[®] organic dairy products; *White Wave*[®] and *Tofu Town*[®] branded tofu. We license the *LAND O LAKES* name from third parties.

Developments Since January 1, 2007

Credit Facilities and Special Cash Dividend On April 2, 2007, we recapitalized our balance sheet through the completion of \$4.8 billion of new senior credit facilities and the return of \$1.94 billion to shareholders of record on March 27, 2007, through a \$15.00 per share special cash dividend. We entered into an amended and restated credit agreement that consists of a combination of a \$1.5 billion 5-year secured revolving credit facility, a \$1.5 billion 5-year senior secured term loan A, and a \$1.8 billion 7-year senior secured term loan B. This will result in increased interest expense in the future.

In addition, we entered into an amendment and restatement of our receivables facility which extended the facility termination date from November 15, 2009 to April 2, 2010. We believe that other modifications related to this amendment will slightly increase our borrowing capacity under the facility.

See Note 13 to our Condensed Consolidated Financial Statements for more information.

Dairy Group Settlement In the first quarter of 2007, we entered into a settlement agreement with a customer to exit a supply agreement. In connection with the settlement, we evaluated the realization of certain customer-related intangible assets for potential impairment. The gain from settlement of \$7.2 million, net of an impairment charge, was recognized in the first quarter. As the exiting of the supply agreement impacts anticipated product volumes, the gain will likely be offset by reduced operating income in future periods.

Friendship Dairies On March 13, 2007, our Dairy Group completed the acquisition of Friendship Dairies, Inc., a manufacturer, marketer and distributor of cultured dairy products primarily in the northeastern United States. This transaction expanded our cultured dairy product capabilities and added a strong regional brand. We paid approximately \$130 million, including transaction costs, for the purchase of Friendship Dairies and funded the purchase price with borrowings under our senior credit facility. We have not completed a final allocation of the purchase price to the fair values of Friendship's assets and liabilities.

Table of Contents***Discontinued Operations***

Iberian Operations Our former Iberian operations included the manufacture and distribution of private label and branded milk across Spain and Portugal. On September 14, 2006, we completed the sale of our operations in Spain. In connection with the sale of our operations in Spain, we entered into an agreement to sell our Portuguese operations (that comprised the remainder of our Iberian operations) for approximately \$11.4 million subject to regulatory approvals and working capital settlements. We completed the sale of our Portuguese operations in January 2007, resulting in a gain of \$617,000.

Our financial statements have been reclassified to give effect to our Iberian operations as discontinued operations.

Facility Closing and Reorganization Activities

We recorded a total of approximately \$5.8 million in facility closing and reorganization costs during the first three months of 2007, related to the realignment of our Dairy Group's finance organization and the closing of Dairy Group facilities in Detroit, Michigan as well as other previously announced plans. We expect to incur additional charges related to these restructuring plans of approximately \$12.9 million. Approximately \$12.0 million and \$800,000 of these additional charges are expected to be completed by December 31, 2007 and 2008, respectively. These charges include the following costs:

Workforce reductions as a result of facility closings, facility reorganizations and consolidation of administrative functions;

Shutdown costs, including those costs necessary to prepare abandoned facilities for closure; and

Costs incurred after shutdown, such as lease obligations or termination costs, utilities and property taxes.

See Note 10 to our Condensed Consolidated Financial Statements for more information regarding our facility closing and reorganization activities.

Results of Operations

The following table presents certain information concerning our financial results, including information presented as a percentage of net sales.

	Quarter Ended March 31,			
	2007		2006	
	Dollars	Percent	Dollars	Percent
	(Dollars in millions)			
Net sales	\$ 2,629.8	100.0%	\$ 2,509.0	100.0%
Cost of sales	1,942.5	73.9	1,857.7	74.0
Gross profit	687.3	26.1	651.3	26.0
Operating costs and expenses:				
Selling and distribution	415.6	15.8	405.1	16.1
General and administrative	109.4	4.1	102.3	4.1

Edgar Filing: DEAN FOODS CO - Form 10-Q

Amortization of intangibles	2.3	0.1	1.4	0.1
Facility closing and reorganization costs	5.8	0.2	4.4	0.2
Total operating costs and expenses	533.1	20.2	513.2	20.5
Total operating income	\$ 154.2	5.9%	\$ 138.1	5.5%

-28-

Table of Contents**Quarter Ended March 31, 2007 Compared to Quarter Ended March 31, 2006 Consolidated Results**

Net Sales Consolidated net sales increased approximately \$120.8 million to \$2.63 billion during the first quarter of 2007 from \$2.51 billion in the first quarter of 2006. Net sales by segment are shown in the table below.

	Quarter Ended March 31,			
	2007	2006	\$ Increase/ (Decrease) (Dollars in millions)	% Increase/ (Decrease)
Dairy Group	\$ 2,307.1	\$ 2,207.7	\$ 99.4	4.5%
WhiteWave Foods Company	322.7	301.3	21.4	7.1
Total	\$ 2,629.8	\$ 2,509.0	\$ 120.8	4.8

The change in net sales was due to the following:

	Quarter ended March 31, 2007 vs Quarter ended March 31, 2006			
	Acquisitions	Pricing, Volume And Product Mix Changes (Dollars in millions)	Total Increase/ (Decrease)	
Dairy Group	\$ 9.7	\$ 89.7	\$ 99.4	
WhiteWave Foods Company		21.4	21.4	
Total	\$ 9.7	\$ 111.1	\$ 120.8	

The change in net sales resulted from higher fluid milk volumes combined with the pass-through of higher overall dairy commodity costs in the Dairy Group, as well as continued sales growth at WhiteWave Foods.

Cost of Sales All expenses incurred to bring a product to completion are included in cost of sales, such as raw material, ingredient and packaging costs; labor costs; and plant and equipment costs, including costs to operate and maintain our coolers and freezers. In addition, our Dairy Group includes costs associated with transporting finished products from our manufacturing facilities to our own distribution facilities. Our cost of sales as a percentage of net sales decreased slightly to 73.9% in the first quarter of 2007 compared to 74.0% in the first quarter of 2006. Higher raw milk costs were partially offset by lower resin costs in the first quarter of 2007. In addition, we recorded a favorable contract settlement with a customer related to the loss of a portion of that customer's business.

Operating Costs and Expenses The dollar amount of operating expenses increased approximately \$19.9 million during the first quarter of 2007 as compared to the same period in the prior year. Our operating expense as a percentage of net sales was 20.2% in the first quarter of 2007 compared to 20.5% during the first quarter of 2006. Operating expenses increased primarily due to an increase in distribution costs of \$16.7 million resulting from higher

freight costs and increased volumes. In addition, general and administrative expenses increased approximately \$7.1 million due primarily to higher salaries and benefits and professional services. Facility closing and reorganization costs increased \$1.4 million due to charges related to the closing of certain Dairy Group facilities and the reorganization of our finance organization. These increases were offset by a decline in marketing expenses of \$6.2 million. See Results by Segment for more information.

Operating Income Operating income during the first quarter of 2007 was \$154.2 million, an increase of \$16.1 million from the first quarter of 2006 operating income of \$138.1 million. Our operating margin in the first quarter of 2007 was 5.9% compared to 5.5% in the first quarter of 2006.

Other (Income) Expense Total other expense increased to \$52.5 million in the first quarter of 2007 compared to \$47.6 million in the first quarter of 2006. Interest expense increased to \$52.2 million in the first

Table of Contents

quarter of 2007 from \$47.5 million in the first quarter of 2006 primarily due to higher average debt balances and higher interest rates.

Income Taxes Income tax expense was recorded at an effective rate of 37.8% in the first quarter of 2007 compared to 39.5% in the first quarter of 2006. Our tax rate during the first quarter of 2007 was favorably impacted by relatively higher stock option exercises in the first quarter of 2007 compared to the prior year. In addition, our tax rate varies as the mix of earnings contributed by our various business units changes.

Quarter Ended March 31, 2007 Compared to Quarter Ended March 31, 2006 Results by Segment*Dairy Group*

The key performance indicators of our Dairy Group are sales volumes, gross profit and operating income.

	Quarter Ended March 31			
	2007		2006	
	Dollars	Percent	Dollars	Percent
	(Dollars in millions)			
Net sales	\$ 2,307.1	100.0%	\$ 2,207.7	100.0%
Cost of sales	1,727.7	74.9	1,660.5	75.2
Gross profit	579.4	25.1	547.2	24.8
Operating costs and expenses	408.3	17.7	390.6	17.7
Total segment operating income	\$ 171.1	7.4%	\$ 156.6	7.1%

The Dairy Group's net sales increased approximately \$99.4 million, or 4.5%, in the first quarter of 2007 versus the first quarter of 2006. The change in net sales from the first quarter of 2006 to the first quarter of 2007 was due to the following:

	Dollars	Percent
	(Dollars in millions)	
2006 Net sales	\$ 2,207.7	
Acquisitions	9.7	0.4%
Volume	21.5	1.0
Pricing and product mix	68.2	3.1
2007 Net sales	\$ 2,307.1	4.5%

The Dairy Group's net sales increased primarily due to the effects of higher selling prices resulting from the pass-through of higher raw material prices. In general, we change the prices that we charge our customers for fluid dairy products on a monthly basis, as the costs of our raw materials fluctuate. The Dairy Group generally has been effective at passing through the changes in the prices of the underlying commodities. However, industry estimates of

the rising prices of raw skim milk for the remainder of 2007 may make this more challenging.

A common industry measure for evaluating changes in fluid dairy raw material costs is the blended Class I price, assuming 3.5% butterfat, often referred to as the Class I mover. The following table sets forth the

-30-

Table of Contents

average monthly component prices of the Class I mover and average monthly Class II minimum prices for raw skim milk and butterfat for the first quarter of 2007 compared to the first quarter of 2006:

	Quarter Ended March 31*		
	2007	2006	% Change
Class I mover(1)(3)	\$ 13.74	\$ 13.08	5%
Class I raw skim milk mover(1)(3)	9.45	8.29	14
Class I butterfat mover(2)(3)	1.32	1.45	(9)
Class II raw skim milk minimum(1)(4)	8.80	8.02	10
Class II butterfat minimum(2)(4)	1.34	1.37	(2)

* The prices noted in this table are not the prices that we actually pay. The federal order minimum prices at any given location for Class I raw skim milk or Class I butterfat are based on the Class I mover prices plus a location differential. Class II prices noted in the table are federal minimum prices, applicable at all locations. Our actual cost also includes producer premiums, procurement costs and other related charges that vary by location and vendor. Please see Part I Item 1. Business Government Regulation Milk Industry Regulation in our Annual Report on Form 10-K for 2006, and Known Trends and Uncertainties Prices of Raw Milk and Other Inputs in this Quarterly Report for a more complete description of raw milk pricing.

- (1) Prices are per hundredweight.
- (2) Prices are per pound.
- (3) We process Class I raw skim milk and butterfat into fluid milk products.
- (4) We process Class II raw skim milk and butterfat into products such as cottage cheese, creams and creamers, ice cream and sour cream.

Net sales were further increased by fluid milk volume increases during the first quarter of 2007. Fluid milk volumes (which represented approximately 71% of the Dairy Group's sales volume during the quarter) increased approximately 2.0%. We believe the increase in volumes is a result of the general rise of healthier food and drink choices and the superior value and service that we are able to offer our customers as the largest dairy processor in the nation.

The Dairy Group's cost of sales as a percentage of net sales decreased to 74.9% in the first quarter of 2007 compared to 75.2% in the first quarter of 2006, as the increase in raw milk costs compared to the prior year was partially offset by lower resin costs of approximately \$13.4 million. Resin is the primary component used in our plastic bottles. Included in cost of sales for the first quarter of 2007 and 2006 is \$4.8 million and \$3.1 million, respectively, related to the settlement of certain business interruption claims.

In addition, in the first quarter of 2007 we entered into a settlement agreement with a customer to exit a supply agreement. In connection with the settlement, we evaluated the realization of certain customer-related intangible assets for potential impairment. The gain from settlement of \$7.2 million, net of an impairment charge, was recognized in the first quarter. As the exiting of the supply agreement impacts anticipated product volumes, the gain will likely be offset by reduced operating income in future periods.

The Dairy Group's operating expenses increased approximately \$17.7 million to \$408.3 million during the first quarter of 2007 compared to \$390.6 million in the first quarter of 2006, primarily due to a \$15.2 million increase in distribution costs. Distribution costs increased as a result of increased freight, labor costs and volume. General and administrative expenses increased approximately \$1.3 million primarily due to higher salaries and benefits.

WhiteWave Foods Company

The key performance indicators of WhiteWave Foods Company are sales dollars, gross profit and operating income.

Table of Contents

	Quarter Ended March 31			
	2007		2006	
	Dollars	Percent	Dollars	Percent
	(Dollars in millions)			
Net sales	\$ 322.7	100.0%	\$ 301.3	100.0%
Cost of sales	214.5	66.5	196.8	65.3
Gross profit	108.2	33.5	104.5	34.7
Operating costs and expenses	80.4	24.9	82.3	27.3
Total segment operating income	\$ 27.8	8.6%	\$ 22.2	7.4%

WhiteWave Foods Company's net sales increased by \$21.4 million, or 7.1%, in the first quarter of 2007 versus the first quarter of 2006. The change in net sales from the first quarter of 2006 to the first quarter of 2007 was due to the following:

	Dollars	Percent
	(Dollars in millions)	
2006 Net sales	\$ 301.3	
Volume	9.5	3.1%
Pricing and product mix	11.9	4.0
2007 Net sales	\$ 322.7	7.1%

The increase in net sales was driven by a combination of higher volumes, higher pricing, and a mix shift to higher revenue products. Volumes increased 3.1% driven by growth in our core brands, while price increased principally in response to higher raw material costs.

We are experiencing increasing competitive pressure from branded and private label participants as the industry moves from a supply shortage of organic milk to an oversupply situation. This supply-demand imbalance in the organic milk market could exert downward pricing pressure on the sale of our products.

Cost of sales as a percentage of net sales for WhiteWave Foods Company increased to 66.5% in the first quarter of 2007 from 65.3% in the first quarter of 2006. Cost of sales dollars increased \$17.7 million primarily due to higher sales volumes and higher commodity costs, principally organic milk.

Operating expenses decreased approximately \$1.9 million in the first quarter of 2007 compared to the same period in the prior year primarily driven by a decrease in marketing expenses. This decrease was partially offset by higher general and administrative expenses due to higher amortization related to our SAP operating software installed in 2006.

Liquidity and Capital Resources

Historical Cash Flow

During the first quarter of 2007, we met our working capital needs with cash flow from operations.

Net cash provided by operating activities from continuing operations was \$138.0 million for the first quarter of 2007 as contrasted to \$25.2 million for the same period in 2006, an increase of \$112.8 million. Net cash provided by operating activities was primarily impacted by changes in operating assets and liabilities, which improved approximately \$138.0 million in the first quarter of 2007 compared to the first quarter of the prior year. The improvement primarily relates to higher working capital needs in the first quarter of 2006 as well as a payment made in the first quarter of 2006 in settlement of contractual obligations under a co-pack agreement entered into prior to our acquisition of an entity.

Net cash used in investing activities from continuing operations was \$165.4 million in the first quarter of 2007 compared to \$62.9 million in the first quarter of 2006, an increase of \$102.5 million largely due to the Friendship Dairy acquisition. Our capital expenditures totaled \$51.8 million in the first quarter of 2007

-32-

Other Long-Term Liabilities

We offer pension benefits through various defined benefit pension plans and also offer certain health care and life insurance benefits to eligible employees and their eligible dependents upon the retirement of such employees. Reported costs of providing non-contributory defined pension benefits and other postretirement benefits are dependent upon numerous factors, assumptions and estimates. For example, these costs are impacted by actual employee demographics (including age, compensation levels and employment periods), the level of contributions made to the plan and earnings on plan assets. Our pension plan assets are primarily made up of equity and fixed income investments. Changes made to the provisions of the plan may impact current and future pension costs. Fluctuations in actual equity market returns, as well as changes in general interest rates may result in increased or decreased pension costs in future periods. Pension costs may be

Table of Contents

significantly affected by changes in key actuarial assumptions, including anticipated rates of return on plan assets and the discount rates used in determining the projected benefit obligation and pension costs.

We expect to contribute approximately \$23.2 million to our defined benefit plans and approximately \$2.4 million to our postretirement health plans in 2007.

Other Commitments and Contingencies

On December 21, 2001, in connection with our acquisition of Legacy Dean, we issued a contingent, subordinated promissory note to Dairy Farmers of America (DFA) in the original principal amount of \$40 million. DFA is our primary supplier of raw milk, and the promissory note is designed to ensure that DFA has the opportunity to continue to supply raw milk to certain of our facilities until 2021, or be paid for the loss of that business. The promissory note has a 20-year term and bears interest based on the consumer price index. Interest will not be paid in cash, but will be added to the principal amount of the note annually, up to a maximum principal amount of \$96 million. We may prepay the note in whole or in part at any time, without penalty. The note will only become payable if we materially breach or terminate one of our milk supply agreements with DFA without renewal or replacement. Otherwise, the note will expire at the end of 20 years, without any obligation to pay any portion of the principal or interest. Payments we make under this note, if any, will be expensed as incurred. We have not breached or terminated any of our milk supply agreements with DFA.

We also have the following commitments and contingent liabilities, in addition to contingent liabilities related to ordinary course litigation, investigations and audits:

Certain indemnification obligations related to businesses that we have divested;

Certain lease obligations, which require us to guarantee the minimum value of the leased asset at the end of the lease; and

Selected levels of property and casualty risks, primarily related to employee health care, workers' compensation claims and other casualty losses.

See Note 11 to our Condensed Consolidated Financial Statements for more information about our commitments and contingent obligations.

Future Capital Requirements

During 2007, we intend to invest a total of approximately \$250 million in capital expenditures primarily for our existing manufacturing facilities and distribution capabilities. We expect cash interest to be approximately \$305 million to \$315 million based on current debt levels under our new senior credit facility. Cash interest excludes amortization of deferred financing fees and bond discounts. We expect cash taxes to be approximately \$115 million.

As a result of our recapitalization the portion of our long-term debt due within the next 12 months totals \$271.2 million. We expect that cash flow from operations together with availability under our new senior credit facility will be sufficient to meet our anticipated future capital requirements. As of May 4, 2007, approximately \$1.00 billion was available for future borrowings under new senior credit facility.

Known Trends and Uncertainties

Prices of Raw Milk and Other Inputs

Dairy Group The primary raw material used in our Dairy Group is raw milk (which contains both raw skim milk and butterfat). The federal government and certain state governments set minimum prices for raw milk, and those prices are set on a monthly basis. The regulated minimum prices differ based on how the raw milk is utilized. Raw milk processed into fluid milk is priced at the Class I price, and raw milk processed into products such as cottage cheese, creams and creamers, ice cream and sour cream is priced at the Class II price. Generally, we pay the federal minimum prices for raw milk, plus certain producer premiums (or over-order premiums) and location differentials. We also incur other raw milk procurement costs in some locations

-34-

Table of Contents

(such as hauling, field personnel, etc.). A change in the federal minimum price does not necessarily mean an identical change in our total raw milk costs, as over-order premiums may increase or decrease. This relationship is different in every region of the country, and sometimes within a region based on supplier arrangements. However, in general, the overall change in our raw milk costs can be linked to the change in federal minimum prices.

Because our Class II products typically have a higher fat content than that contained in raw milk, we also purchase bulk cream for use in some of our Class II products. Bulk cream is typically purchased based on a multiple of the AA butter price on the Chicago Mercantile Exchange (CME).

Another significant raw material used by our Dairy Group is resin, which is used to make plastic bottles. We purchase approximately 27 million pounds of resin and bottles per month. Resin is a petroleum-based product, and the price of resin is subject to fluctuations based on changes in crude oil prices. Our Dairy Group purchases approximately 4 million gallons of diesel fuel per month to operate our extensive direct store delivery system.

In general, our Dairy Group changes the prices that it charges for Class I dairy products on a monthly basis, as the costs of raw milk, packaging, fuel and other materials fluctuate. Prices for some Class II products are also changed monthly while others are changed from time to time as circumstances warrant. However, there can be a lag between the time of a raw material cost increase or decrease and a corresponding price change to our customers, especially in the case of Class II butterfat because Class II butterfat prices for each month are not announced by the government until after the end of that month. Also, in some cases we are competitively or contractually constrained with the means and timing of implementing price changes. These factors can cause volatility in our earnings. Our sales and operating profit margin fluctuate with the price of our raw materials and other inputs.

During the first quarter of 2007, prices for raw skim milk increased. We expect raw skim milk, butterfat and cream prices to increase throughout the remainder of 2007. However, raw skim milk, butterfat and cream prices are difficult to predict, and we change our forecasts frequently based on current market activity. The Dairy Group generally has been effective at passing through the changes in the prices of the underlying commodities. However, industry estimates of the rising prices of raw skim milk for the remainder of 2007 may make this more challenging.

During the first quarter of 2007, the prices of resin decreased while diesel prices were largely unchanged. As resin supplies have from time to time been insufficient to meet demand, we are undertaking all reasonable measures in an attempt to secure an adequate resin supply; however, there can be no assurance that we will always be successful in our attempts. We expect prices of both resin and diesel fuel to fluctuate throughout 2007.

WhiteWave Foods Company A significant raw material used to manufacture products sold by WhiteWave Foods Company is organic soybeans. We have entered into supply agreements for organic soybeans, which we believe will meet our needs for 2007. These agreements provide for pricing at fixed levels. However, should our need for organic soybeans exceed the quantity that we have under contract, or if the suppliers do not perform under the contracts, we may have difficulty obtaining sufficient supply, and the price we could be required to pay could be significantly higher.

Significant raw materials used in our products include organic raw milk and sugar. We obtain our supply of organic raw milk by entering into one to two year agreements with farmers pursuant to which the farmers agree to sell us specified quantities of organic raw milk for fixed prices for the duration of the agreement. We also source approximately 20% of our organic raw milk supply from our own farms. In the past, the industry-wide demand for organic raw milk has generally exceeded supply, resulting in our inability to fully meet customer demand. However, due to the recent industry efforts to grow the supply of organic raw milk, there currently is a significant over supply of organic raw milk which may increase competitive pressure both from branded and private label participants, resulting in downward pricing pressure on the sale of our products, which may negatively impact our profitability. We have

entered into supply agreements for organic sugar, which we believe will meet our needs in 2007.

Table of Contents***Competitive Environment***

There has been significant consolidation in the retail grocery industry in recent years, and this trend is continuing. As our customer base consolidates, we expect competition to intensify as we compete for the business of fewer customers. There can be no assurance that we will be able to keep our existing customers, or gain new customers. There are several large regional grocery chains that have captive dairy operations. As the consolidation of the grocery industry continues, we could lose sales if any one or more of our existing customers were to be sold to a chain with captive dairy operations.

Many of our retail customers have become increasingly price sensitive in the current intensely competitive environment. Over the past few years, we have been subject to a number of competitive bidding situations in our Dairy Group, which reduced our profitability on sales to several customers. We expect this trend to continue. In bidding situations, we are subject to the risk of losing certain customers altogether. The loss of any of our largest customers could have a material adverse impact on our financial results. We do not have contracts with many of our largest customers, and most of the contracts that we do have are generally terminable at will by the customer.

The supply-demand imbalance in the organic milk market has increased competition in the marketplace as competitors attempt to stimulate demand through lower retail prices and aggressive distribution expansion. As a result, we could experience downward pricing pressure on the sale of our organic products.

Both the difficult economic environment and the increased competitive environment at the retail level have caused competition to become increasingly intense at the processor level.

Tax Rate

Income tax expense was recorded at an effective rate of 37.8% in the first quarter of 2007. Our tax rate during the first quarter of 2007 was favorably impacted by relatively higher stock option exercises in the first quarter of 2007 compared to the prior year. We estimate the effective tax rate will be approximately 39% for the remainder of 2007. Changes in the relative profitability of our operating segments, as well as changes to federal and state tax laws may cause the rate to change from historical rates.

See Part II Item 1A Risk Factors for a description of various other risks and uncertainties concerning our business.

Item 3. Quantitative and Qualitative Disclosures About Market Risk**Interest Rate Fluctuations**

In order to reduce the volatility of earnings that arises from changes in interest rates, we manage interest rate risk through the use of interest rate swap agreements. These swap agreements provide hedges for loans under our senior credit facility by limiting or fixing the LIBOR interest rates specified in the senior credit facility at the interest rates noted below until the indicated expiration dates.

The following table summarizes our various interest rate agreements at March 31, 2007:

Fixed Interest Rates	Expiration Date	Notional Amounts (In millions)
----------------------	-----------------	-----------------------------------

Edgar Filing: DEAN FOODS CO - Form 10-Q

4.07% to 4.27%	December 2010	\$	450
4.907%	March 2008-March 2012		2,950

The following table summarizes our various interest rate agreements at December 31, 2006:

Fixed Interest Rates	Expiration Date		Notional Amounts (In millions)
4.81% to 4.84%	December 2007	\$	500
4.07% to 4.27%	December 2010		450

During the three months ended March 31, 2007, we settled the interest rate swaps expiring in 2007. Amounts included in Other Comprehensive Income related to these swaps will be recognized over the originally forecasted period.

Table of Contents

We are exposed to market risk under these arrangements due to the possibility of interest rates on our senior credit facility falling below the rates on our interest rate derivative agreements. We recorded \$1.2 million of interest income, net of taxes, during the first quarter of 2007 primarily as a result of interest rates on our variable rate debt rising above the agreed-upon interest rate on our existing swap agreements. Credit risk under these arrangements is remote since the counterparties to our interest rate derivative agreements are major financial institutions.

A majority of our debt obligations are currently at variable rates. We have performed a sensitivity analysis assuming a hypothetical 10% adverse movement in interest rates. As of March 31, 2007, the analysis indicated that such interest rate movement would not have a material effect on our financial position, results of operations or cash flows. However, actual gains and losses in the future may differ materially from that analysis based on changes in the timing and amount of interest rate movement and our actual exposure and hedges.

Other

Market risk with respect to butterfat has not materially changed from prior periods.

We currently do not have material exposure to foreign currency risk as we do not have significant amounts of operating cash flows denominated in foreign currencies.

Item 4. Controls and Procedures

Controls Evaluation and Related Certifications

We conducted an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures (Disclosure Controls) as of the end of the period covered by this quarterly report. The controls evaluation was done under the supervision and with the participation of management, including our Chief Executive Officer (CEO) and Chief Financial Officer (CFO).

Attached as exhibits to this quarterly report are certifications of the CEO and the CFO, which are required in accordance with Rule 13a-14 of the Exchange Act. This Controls and Procedures section includes the information concerning the controls evaluation referred to in the certifications and it should be read in conjunction with the certifications for a more complete understanding of the topics presented.

Definition of Disclosure Controls

Disclosure Controls are controls and procedures designed to reasonably assure that information required to be disclosed in our reports filed with the Securities and Exchange Commission (the SEC) is recorded, processed, summarized and reported within the time periods specified in the SEC 's rules and forms. Disclosure Controls are also designed to reasonably assure that such information is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Our Disclosure Controls include components of our internal control over financial reporting, which consists of control processes designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of financial statements in accordance with US generally accepted accounting principles.

Limitations on the Effectiveness of Controls

We do not expect that our Disclosure Controls or our internal control over financial reporting will prevent all errors and all fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system 's objectives will be met. Further, the design of a control system must reflect the fact

that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Controls can also be

Table of Contents

circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions. Over time, controls may become inadequate because of changes in conditions or deterioration in the degree of compliance with policies or procedures. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Scope of the Controls Evaluation

Our evaluations of our Disclosure Controls include reviews of the controls objectives and design, our implementation of the controls and the effect of the controls on the information generated for use in our SEC filings. In the course of our controls evaluations, we seek to identify data errors, controls problems or acts of fraud and confirm that appropriate corrective actions, including process improvements, are undertaken. Many of the components of our Disclosure Controls are evaluated on an ongoing basis by our Audit Services department. The overall goals of these various evaluation activities are to monitor our Disclosure Controls, and to modify them as necessary. Our intent is to maintain the Disclosure Controls as dynamic systems that change as conditions warrant.

Changes in Internal Control over Financial Reporting

During the third quarter of 2006, WhiteWave Foods Company implemented SAP as its primary financial reporting and resource planning system. SAP was implemented at all locations of WhiteWave Foods Company in the United States except for the manufacturing facilities located in City of Industry, CA, Jacksonville, FL and Mt. Crawford, VA. WhiteWave Foods Company will implement SAP at these facilities during 2007.

Conclusions

Based upon our most recent controls evaluation, our CEO and CFO have concluded that as of the end of the period covered by this quarterly report, our Disclosure Controls were effective at the reasonable assurance level. Other than ongoing control enhancements related to the implementation of SAP as discussed above, there was no change in our internal control over financial reporting in the quarter ended March 31, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

Part II Other Information

Item 1. Legal Proceedings

We are not party to, nor are our properties the subject of, any material pending legal proceedings. However, we are party from time to time to certain claims, litigation, audits and investigations. We believe that we have established adequate reserves to satisfy any potential liability we may have under all such claims, litigations, audits and investigations that are currently pending. In our opinion, the settlement of any such currently pending or threatened matter is not expected to have a material adverse impact on our financial position, results of operations or cash flows.

Two shareholder derivative complaints were filed in July and October 2006 in the district court of Dallas County, Texas, which alleged stock option backdating. The complaints named certain current and former members of the Board of Directors and certain current and former members of management. In response to the litigation, a special litigation committee of our Board of Directors was established in August 2006. The committee, consisting of independent board members not named in the litigation, conducted its own independent review of our stock option grants and the allegations made in the complaints and determined that there were no fraudulent acts by management. The derivative actions were settled in the first quarter of 2007. The settlement resolves all claims and includes no finding of wrongdoing on the part of any of the defendants and no cash payment other than attorneys' fees. The Company has agreed to adoption and implementation of stock option grant procedures that reflect developing best practices. The district court approved the settlement and the actions were dismissed.

As previously announced, the staff of the SEC began an informal inquiry into our historical stock option practices. On May 7, 2007, the staff of the SEC notified us that the informal inquiry was closed without any recommended enforcement action.

Item 1A. Risk Factors

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act. Statements that are not historical in nature are forward-looking statements about our future that are not statements of historical fact. Most of these statements are found in this report under the following subheadings: Management's Discussion and Analysis of Financial Condition and Results of Operations and Quantitative and Qualitative Disclosures About Market Risk. In some cases, you can identify these statements by terminology such as may, should, could, expects, seek to, anticipates, plans, believes, estimates, intends, predicts, projects, potential, or negative of such terms and other comparable terminology. These statements are only predictions, and in evaluating those statements, you should carefully consider the information above, including in Known Trends and Uncertainties, as well as the risks outlined below. Actual performance or results may differ materially and adversely. Except as discussed below, there have been no material changes from the risk factors disclosed in our Annual Report on Form 10-K for the year ended December 31, 2006.

Availability and Changes in Raw Material and Other Input Costs Can Adversely Affect Us

Raw skim milk is the most significant raw material that we use in our Dairy Group. Organic raw milk, organic soybeans and sugar are significant inputs utilized by WhiteWave Foods Company. The prices of these materials increase and decrease based on supply and demand, and in some cases, governmental regulation. Weather also affects the availability and pricing of these inputs. In many cases we are able to adjust our pricing to reflect changes in raw material costs. Volatility in the cost of our raw materials can adversely affect our performance as price changes often lag changes in costs. These lags tend to erode our profit margins. Furthermore, cost increases may exceed the price

increases we are able to pass along to our customers. Extremely high raw material costs also can put downward pressure on our margins and our volumes. We expect certain raw material prices, including raw skim milk prices, to increase in 2007.

In the recent past, the industry-wide demand for organic raw milk has generally exceeded supply, resulting in our inability to fully meet customer demand. However, due to the recent industry efforts to grow

Table of Contents

the supply of organic raw milk, there currently is a significant over supply of organic raw milk which may increase competitive pressure both from branded and private label participants, resulting in downward pricing pressure on the sale of our products, which may negatively impact our profitability.

Because our Dairy Group delivers the majority of its products directly to customers through its direct store delivery system, we are a large consumer of fuel. Similarly, our WhiteWave Foods business is impacted by the costs of petroleum-based products through the use of common carriers in delivering their products. The Dairy Group utilizes a significant amount of resin, which is the primary component used in our plastic bottles. Resin supplies have from time to time been insufficient to meet demand. Increases in fuel and resin prices can adversely affect our results of operations. In addition, a disruption in our ability to secure an adequate resin supply could adversely affect our operations.

We Have Substantial Debt and Other Financial Obligations and We May Incur Even More Debt

We have substantial debt and other financial obligations and significant unused borrowing capacity. See Liquidity and Capital Resources.

We have pledged substantially all of our assets (including the assets of our subsidiaries) to secure our indebtedness. Our debt level and related debt service obligations:

Require us to dedicate significant cash flow to the payment of principal and interest on our debt which reduces the funds we have available for other purposes,

May limit our flexibility in planning for or reacting to changes in our business and market conditions,

Impose on us additional financial and operational restrictions,

Expose us to interest rate risk since a portion of our debt obligations are at variable rates, and

Restrict our ability to fund acquisitions.

Our ability to make scheduled payments on our debt and other financial obligations depends on our financial and operating performance. Our financial and operating performance is subject to prevailing economic conditions and to financial, business and other factors, some of which are beyond our control. A significant increase in interest rates could adversely impact our net income. If we do not comply with the financial and other restrictive covenants under our credit facilities, we may default under them. Upon default, our lenders could accelerate the indebtedness under the facilities, foreclose against their collateral or seek other remedies, which would jeopardize our ability to continue our current operations. As a result of the recapitalization of our balance sheet, which is more fully described in Note 13 to our Condensed Consolidated Financial Statements, we entered into \$4.8 billion of new senior credit facilities. This represents a significant increase in leverage compared to recent years, which will intensify the risks described above.

Table of Contents

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

As of March 31, 2007, approximately \$218.7 million remained available pursuant to the stock repurchase program approved by our Board of Directors. The amount can be increased by actions of our Board of Directors.

No stock has been repurchased during the period January 1, 2007 through May 4, 2007.

Item 6. Exhibits

(a) Exhibits

31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
99	Supplemental Financial Information for Dean Holding Company (filed herewith)

Table of Contents

SIGNATURES

Pursuant to the requirement of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

DEAN FOODS COMPANY

/s/ Ronald L. McCrummen

Ronald L. McCrummen
Senior Vice President and Chief Accounting Officer

May 10, 2007

-42-