

TODHUNTER INTERNATIONAL INC
Form 10-Q
August 14, 2003

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2003

Commission File No. 1-13453

TODHUNTER INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

DELAWARE

(State or other jurisdiction of
incorporation or organization)

59-1284057

IRS Employer Identification No.

**222 Lakeview Avenue, Suite 1500, West Palm
Beach, FL**

(Address of principal executive offices)

33401

(Zip Code)

Registrant's telephone number, including area code: **(561) 655-8977**

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, and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes No

The number of shares outstanding of registrant's Common Stock, \$.01 par value per share, as of August 12, 2003 was 5,576,234.

TODHUNTER INTERNATIONAL, INC.

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* Item is omitted because answer is negative or item is inapplicable.

PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

TODHUNTER INTERNATIONAL, INC.
CONSOLIDATED BALANCE SHEETS

| | June 30, 2003 (Unaudited) | September 30, 2002 * |
|---|---------------------------------|----------------------------|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 14,205,007 | \$ 13,946,736 |
| Short-term investments | 3,402,636 | 3,397,033 |
| Trade receivables | 13,801,588 | 13,505,737 |
| Other receivables | 2,617,059 | 2,696,743 |
| Inventories | 32,442,963 | 27,854,925 |
| Notes receivable, current maturities | 246,767 | 118,165 |
| Deferred income taxes | 2,205,750 | 1,992,000 |
| Other current assets | 2,488,589 | 3,078,437 |
| Total current assets | 71,410,359 | 66,589,776 |
| LONG-TERM INVESTMENTS AND NOTES RECEIVABLE | | |
| Investments in and advances to equity investees | 1,886,416 | 1,584,628 |
| Notes receivable from affiliates, less current maturities | 4,121,204 | 3,774,773 |
| Notes receivable, less current maturities | 523,608 | 584,687 |
| | 6,531,228 | 5,944,088 |
| PROPERTY AND EQUIPMENT | | |
| PROPERTY AND EQUIPMENT | 91,632,043 | 89,775,329 |
| Less accumulated depreciation | 50,824,798 | 47,590,112 |
| | 40,807,245 | 42,185,217 |
| GOODWILL | | |
| GOODWILL | 20,524,404 | 20,524,404 |
| AMORTIZED INTANGIBLE ASSETS | | |
| AMORTIZED INTANGIBLE ASSETS | 1,785,030 | 2,040,181 |
| OTHER ASSETS | | |
| OTHER ASSETS | 29,250 | 598,838 |
| | \$ 141,087,516 | \$ 137,882,504 |

*From audited financial statements.

See Notes to Consolidated Financial Statements.

TODHUNTER INTERNATIONAL, INC.

CONSOLIDATED BALANCE SHEETS

| | June 30, 2003 (Unaudited) | September 30, 2002 * |
|---|---------------------------------|----------------------------|
| LIABILITIES AND STOCKHOLDERS EQUITY | | |
| CURRENT LIABILITIES | | |
| Current maturities of long-term debt | \$ 4,000,000 | \$ 4,000,000 |
| Accounts payable | 7,949,135 | 4,051,379 |
| Accrued expenses | 3,041,682 | 3,223,293 |
| Total current liabilities | 14,990,817 | 11,274,672 |
| | | |
| LONG-TERM DEBT, less current maturities | 49,900,206 | 53,017,009 |
| | | |
| DEFERRED INCOME TAXES | 5,033,250 | 4,710,000 |
| | | |
| OTHER LIABILITIES | 2,233,337 | 1,811,459 |
| | 72,157,610 | 70,813,140 |
| | | |
| STOCKHOLDERS EQUITY | | |
| Preferred stock, par value \$.01 per share; authorized 2,500,000 shares; no shares issued | | |
| Common stock, par value \$.01 per share; authorized 10,000,000 shares; issued 5,673,434 shares June 30, 2003, and 5,669,434 shares September 30, 2002 | 56,734 | 56,694 |
| Additional paid-in capital | 18,696,909 | 18,664,449 |
| Retained earnings | 50,914,043 | 49,086,001 |
| | 69,667,686 | 67,807,144 |
| Less cost of 99,200 shares of treasury stock | (737,780) | (737,780) |
| | 68,929,906 | 67,069,364 |
| | \$ 141,087,516 | \$ 137,882,504 |

*From audited financial statements.

See Notes to Consolidated Financial Statements.

TODHUNTER INTERNATIONAL, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

| | Nine Months Ended June 30, | | Three Months Ended June 30, | |
|--|----------------------------|---------------|-----------------------------|---------------|
| | 2003 | 2002 | 2003 | 2002 |
| Sales | \$ 88,646,677 | \$ 97,693,371 | \$ 30,924,864 | \$ 34,377,199 |
| Less excise taxes | 22,769,722 | 24,948,483 | 7,837,133 | 8,443,889 |
| Net sales | 65,876,955 | 72,744,888 | 23,087,731 | 25,933,310 |
| Cost of goods sold | 44,423,842 | 49,402,731 | 15,022,995 | 17,289,143 |
| Gross profit | 21,453,113 | 23,342,157 | 8,064,736 | 8,644,167 |
| Selling, general and administrative expenses | 17,392,479 | 15,592,695 | 6,305,257 | 5,778,418 |
| Operating income | 4,060,634 | 7,749,462 | 1,759,479 | 2,865,749 |
| Other income (expense): | | | | |
| Interest income | 570,479 | 480,619 | 227,759 | 107,986 |
| Interest expense | (2,583,583) | (2,070,276) | (985,150) | (649,550) |
| Equity in income (loss) of equity investee | 325,970 | 136,035 | 76,565 | (21,378) |
| Other, net | (1,363,999) | 327,212 | 94,622 | 81,406 |
| | (3,051,133) | (1,126,410) | (586,204) | (481,536) |
| Income before income taxes | 1,009,501 | 6,623,052 | 1,173,275 | 2,384,213 |
| Income tax expense (benefit): | | | | |
| Current | (928,041) | 1,441,017 | (883,657) | 444,267 |
| Deferred | 109,500 | 211,500 | 164,500 | 185,000 |
| | (818,541) | 1,652,517 | (719,157) | 629,267 |
| Net Income | \$ 1,828,042 | \$ 4,970,535 | \$ 1,892,432 | \$ 1,754,946 |
| Earnings per common share: | | | | |
| Basic | \$ 0.33 | \$ 0.90 | \$ 0.34 | \$ 0.32 |
| Diluted | \$ 0.32 | \$ 0.88 | \$ 0.34 | \$ 0.31 |
| Common shares and equivalents outstanding: | | | | |
| Basic | 5,572,608 | 5,518,675 | 5,574,322 | 5,528,558 |
| Diluted | 5,639,825 | 5,631,189 | 5,647,923 | 5,661,247 |

See Notes to Consolidated Financial Statements.

TODHUNTER INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

| | Nine Months Ended June 30, | |
|---|----------------------------|----------------|
| | 2003 | 2002 |
| CASH FLOWS FROM OPERATING ACTIVITIES | | |
| Net income | \$ 1,828,042 | \$ 4,970,535 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation | 4,015,637 | 3,902,721 |
| Amortization | 30,150 | 67,650 |
| (Gain) loss on sale of property and equipment | 65,583 | (30,373) |
| Equity in income of equity investees | (325,970) | (136,035) |
| Deferred income taxes | 109,500 | 211,500 |
| Changes in assets and liabilities: | | |
| (Increase) decrease in: | | |
| Receivables | (216,167) | (81,183) |
| Inventories | (4,588,038) | (709,611) |
| Other current assets | 589,848 | (787,925) |
| Increase (decrease) in: | | |
| Accounts payable | 3,897,756 | (348,117) |
| Accrued expenses | (181,611) | (314,764) |
| Other liabilities | 421,878 | 25,413 |
| Net cash provided by operating activities | 5,646,608 | 6,769,811 |
| CASH FLOWS FROM INVESTING ACTIVITIES | | |
| Proceeds from sale of property and equipment | 60,152 | 58,598 |
| Principal payments received on notes receivable | 92,046 | 68,045 |
| Purchase of property and equipment | (2,763,400) | (4,815,666) |
| Disbursements for notes receivable | (506,000) | (286,797) |
| Purchase of short-term investments | (103,603) | (2,918,664) |
| Redemption of short-term investments | 98,000 | |
| Investments in subsidiaries | 24,182 | |
| Increase in other assets | 794,589 | 190,600 |
| Net cash used in investing activities | \$ (2,304,034) | \$ (7,703,884) |

| | Nine Months Ended June 30, | |
|--|-----------------------------------|--------------|
| | 2003 | 2002 |
| CASH FLOWS FROM FINANCING ACTIVITIES | | |
| Net borrowings on line of credit | \$ 50,000 | \$ 1,900,000 |
| Issuance of common stock | 32,500 | 213,000 |
| Disbursements for loan costs | | (889,833) |
| Principal payments on long-term borrowings | (3,166,803) | (3,124,247) |
| Net cash used in financing activities | (3,084,303) | (1,901,080) |
| Net increase (decrease) in cash and cash equivalents | 258,271 | (2,835,153) |
| Cash and cash equivalents: | | |
| Beginning | 13,946,736 | 5,624,029 |
| Ending | \$ 14,205,007 | \$ 2,788,876 |
| SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION | | |
| Cash payments (receipts) for: | | |
| Interest | \$ 2,580,428 | \$ 2,059,474 |
| Income taxes | \$ (595,939) | \$ 1,271,488 |

See Notes to Consolidated Financial Statements.

TODHUNTER INTERNATIONAL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

Note 1. Basis of Presentation

The consolidated financial statements included herein have been prepared by the Company, without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. 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 condensed or omitted pursuant to such rules and regulations. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, except for the retirement of the Executive Officers (see Note 7), necessary for a fair presentation of the financial information for the periods indicated have been included. For further information regarding the Company's accounting policies, refer to the consolidated financial statements and related notes included in the Company's Annual Report on Form 10-K for the year ended September 30, 2002.

Aggregate amortization expenses were \$30,150 and \$10,050 for the nine and three months ended June 30, 2003, respectively, and \$67,650 and \$22,550 for the nine and three months ended June 30, 2002, respectively.

The Company applies Accounting Principles Board Opinion Number 25, *Accounting for Stock Issued to Employees* (APB 25) and related interpretations in accounting for options granted, which requires compensation expense for the Company's options to be recognized only if the market price of the underlying stock exceeds the exercise price on the date of grant. Accordingly, the Company has not recognized compensation expense for its options granted after 1994. Statement of Financial Accounting Standards (SFAS) No. 123, *Accounting for Stock-Based Compensation*, issued in October 1995, requires pro forma disclosures for option grants made after December 31, 1994, when accounting for stock-based compensation plans in accordance with APB 25.

If the Company elected to recognize compensation cost based on the fair value of the options granted at grant date as prescribed by SFAS No. 123, net income and earnings per common share would have been reduced to the pro forma amounts show below:

| | Nine Months Ended June 30, | | Three Months Ended June 30, | |
|---|-------------------------------|--------------|--------------------------------|--------------|
| | 2003 | 2002 | 2003 | 2002 |
| Net income, as reported | \$ 1,828,042 | \$ 4,970,535 | \$ 1,892,432 | \$ 1,754,946 |
| Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects | 126,103 | 126,103 | 42,034 | 42,034 |
| Net income, pro forma | \$ 1,701,939 | \$ 4,844,432 | \$ 1,850,398 | \$ 1,712,912 |

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Earnings per common share, as reported

| | | | | |
|---------|------|------|------|------|
| Basic | 0.33 | 0.90 | 0.34 | 0.32 |
| Diluted | 0.32 | 0.88 | 0.34 | 0.31 |

Earnings per common share, pro forma

| | | | | |
|---------|------|------|------|------|
| Basic | 0.30 | 0.87 | 0.33 | 0.30 |
| Diluted | 0.30 | 0.86 | 0.32 | 0.30 |

Note 2. Inventories

The major components of inventories are:

| | June 30, 2003 (Unaudited) | September 30, 2002 |
|----------------------------|------------------------------|--------------------|
| Finished goods | \$ 17,241,342 | \$ 16,470,057 |
| Work in process | 3,138,158 | 1,513,786 |
| Raw materials and supplies | 12,063,463 | 9,871,082 |
| | \$ 32,442,963 | \$ 27,854,925 |

Note 3. Financing Arrangements

Long-term debt consists of the following as of June 30, 2003:

| | |
|--|---------------|
| Term loans under a credit agreement (i) (ii), interest payable monthly based on either the Eurodollar or prime rate at the Company's option, plus an applicable margin as defined in the agreement. The interest rate at June 30, 2003 was 5.32%. Future minimum quarterly principal installments of \$1,000,000 through September 30, 2006 with any remaining balance due September 30, 2006. | \$ 33,000,000 |
| Revolving loans under a credit agreement (i), interest payable quarterly based on either the Eurodollar or prime rate at the Company's option, plus an applicable margin as defined in the agreement. The blended interest rate at June 30, 2003 was 5.1%. The revolving lines of credit terminate in October 2004. | 20,550,000 |
| Other | 350,206 |
| | 53,900,206 |
| Less current maturities | 4,000,000 |
| | \$ 49,900,206 |

(i) In October 2001, the Company entered into a \$70 million credit agreement, which consists of a \$40 million term loan and a \$30 million revolving loan facility. The credit agreement is collateralized principally by all assets located in the United States of America. The Company is restricted from paying dividends to stockholders. Also, the Company is required to maintain unencumbered cash or marketable securities of \$4 million at the end of each fiscal quarter and to maintain certain financial covenants.

(ii) In addition to quarterly principal payments, the Company may be required to make additional principal payments based on results of the Company's domestic operating profits, as defined in the agreement.

As of December 31, 2002 and March 31, 2003, the Company was not in compliance with the Funded Debt to EBITDA (earnings before interest, taxes, depreciation and amortization) financial covenant under its credit agreement. In addition, as of March 31, 2003 the Company was not in compliance with its Interest Coverage and Fixed Charge Coverage financial covenants. On February 18, 2003, the Company received a waiver for the December 31, 2002 covenant violation. On May 14, 2003, the Company received a waiver of the March 31, 2003 covenant violations and amended the credit agreement prospectively to reset the levels of certain financial covenants to reflect the Company's current business plan and forecasts. The Company paid a fee of \$136,250 for the December waiver and \$160,000 for the March waiver and amendment. The Company's interest rate under the term-loan and revolving credit agreement was increased 50 basis points effective January 1, 2003 and an additional 50 basis points effective May 14, 2003.

Note 4. Earnings Per Common Share

Basic earnings per common share are calculated by dividing net income by the average common shares outstanding. On a diluted basis, shares outstanding are adjusted to assume the exercise of stock options.

| | Nine Months Ended June 30, | | Three Months Ended June 30, | |
|---|-------------------------------|--------------|--------------------------------|--------------|
| | 2003 | 2002 | 2003 | 2002 |
| Net income | \$ 1,828,042 | \$ 4,970,535 | \$ 1,892,432 | \$ 1,754,946 |
| Determination of shares: | | | | |
| Weighted average number of common shares outstanding | 5,572,608 | 5,518,675 | 5,574,322 | 5,528,558 |
| Shares issuable on exercise of stock options, net of shares assumed to be purchased out of proceeds | 67,217 | 112,514 | 73,601 | 132,689 |
| Average common shares outstanding for diluted earnings per share computation | 5,639,825 | 5,631,189 | 5,647,923 | 5,661,247 |
| Earnings per common share: | | | | |
| Basic | \$ 0.33 | \$ 0.90 | \$ 0.34 | \$ 0.32 |
| Diluted | \$ 0.32 | \$ 0.88 | \$ 0.34 | \$ 0.31 |

The Company's Virgin Islands subsidiary, through the Economic Development Commission of the Government of the Virgin Islands of the United States, has received a 90% exemption from income taxes on operating income. This exemption is effective through September 2020. The per share effect of this exemption on earnings (on a diluted basis) was to increase earnings per share by \$0.15 and \$0.06 for the nine and three months ended June 30, 2003, respectively, and \$0.12 and \$0.04 for the nine and three months ended June 30, 2002, respectively.

Note 5. Segment and Geographical Information

The Company operates primarily in the beverage alcohol industry in the United States. The Company reports its operating results in four segments:

Bulk Alcohol Products (citrus brandy, citrus spirits, rum, cane spirits, fortified citrus wine, purchased distilled products and byproducts)

Premium Branded Spirits (primarily Cruzan Estate Rums and Cruzan Flavored Rums)

Bottling Operations (contract bottling services and proprietary and private label products)

Vinegar and Cooking Wine (bulk vinegar, bulk cooking wine, vinegar stock and proprietary and private label case goods)

The accounting policies of the reportable segments are the same as those referred to in Note 1 to the consolidated financial statements. The Company evaluates the performance of its operating segments based on income before income taxes, equity in income or loss of equity investees, interest income and interest expense. Material intersegment sales and transfers have been eliminated.

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Summarized financial information concerning the Company's reportable segments is shown in the following table.

Net sales, operating income (loss), depreciation and amortization and capital expenditures for the Company's reportable segments for the nine and three months ended June 30, 2003 and 2002, and identifiable assets as of June 30, 2003 and 2002, were as follows:

| | Nine Months Ended June 30, | | Three Months Ended June 30, | |
|--------------------------------------|-------------------------------|-----------|--------------------------------|-----------|
| | 2003 | 2002 | 2003 | 2002 |
| | (in thousands) | | (in thousands) | |
| Net Sales | | | | |
| Bulk Alcohol Products | \$ 26,276 | \$ 26,911 | \$ 8,749 | \$ 9,219 |
| Premium Branded Spirits | 13,521 | 15,134 | 4,796 | 6,702 |
| Bottling Operations | 10,953 | 14,923 | 4,542 | 4,718 |
| Vinegar and Cooking Wine | 15,127 | 15,777 | 5,001 | 5,294 |
| | \$ 65,877 | \$ 72,745 | \$ 23,088 | \$ 25,933 |
| Operating Income (Loss) | | | | |
| Bulk Alcohol Products | \$ 8,673 | \$ 8,235 | \$ 2,900 | \$ 2,835 |
| Premium Branded Spirits | (1,290) | (230) | (544) | 312 |
| Bottling Operations | (1,450) | 973 | 287 | (35) |
| Vinegar and Cooking Wine | 2,947 | 3,306 | 895 | 1,203 |
| Corporate Operations and Other | (4,819) | (4,535) | (1,778) | (1,450) |
| | \$ 4,061 | \$ 7,749 | \$ 1,760 | \$ 2,865 |
| Depreciation and Amortization | | | | |
| Bulk Alcohol Products | \$ 2,424 | \$ 2,226 | \$ 815 | \$ 765 |
| Premium Branded Spirits | 72 | 104 | 22 | 33 |
| Bottling Operations | 1,099 | 1,193 | 401 | 381 |
| Vinegar and Cooking Wine | 362 | 352 | 120 | 118 |
| Corporate Operations and Other | 89 | 95 | 30 | 31 |
| | \$ 4,046 | \$ 3,970 | \$ 1,388 | \$ 1,328 |
| Capital Expenditures | | | | |
| Bulk Alcohol Products | \$ 1,370 | \$ 3,757 | \$ 298 | \$ 1,066 |
| Premium Branded Spirits | 71 | 63 | 55 | 4 |
| Bottling Operations | 1,178 | 687 | 171 | 344 |
| Vinegar and Cooking Wine | 68 | 193 | 34 | 115 |
| Corporate Operations and Other | 76 | 116 | 65 | |
| | \$ 2,763 | \$ 4,816 | \$ 623 | \$ 1,529 |
| Identifiable Assets | | | | |
| Bulk Alcohol Products | \$ 76,132 | \$ 71,355 | | |
| Premium Branded Spirits | 7,673 | 8,153 | | |
| Bottling Operations | 25,150 | 25,447 | | |

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| | | |
|--------------------------------|------------|------------|
| Vinegar and Cooking Wine | 19,753 | 20,167 |
| Corporate Operations and Other | 12,380 | 12,047 |
| | \$ 141,088 | \$ 137,169 |

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Sales and operating income for the nine and three months ended June 30, 2003 and 2002 and identifiable assets as of June 30, 2003 and 2002, classified by geographic area, were as follows:

| | United States | U. S. Virgin Islands and the Bahamas (in thousands) | Consolidated |
|----------------------------------|---------------|--|--------------|
| <u>Nine Months Ended</u> | | | |
| June 30, 2003: | | | |
| Net sales | \$ 57,561 | \$ 8,316 | \$ 65,877 |
| Operating income | 1,603 | 2,458 | 4,061 |
| Identifiable assets | 96,023 | 45,065 | 141,088 |
| June 30, 2002: | | | |
| Net sales | 64,991 | 7,754 | 72,745 |
| Operating income | 5,752 | 1,997 | 7,749 |
| Identifiable assets | 95,563 | 41,606 | 137,169 |
| <u>Three Months Ended</u> | | | |
| June 30, 2003: | | | |
| Net sales | 20,078 | 3,010 | 23,088 |
| Operating income | 615 | 1,145 | 1,760 |
| June 30, 2002: | | | |
| Net sales | 22,947 | 2,986 | 25,933 |
| Operating income | 2,042 | 823 | 2,865 |

Included in net sales for the United States are export sales, primarily to Europe, Canada and the Caribbean, totaling approximately \$6,203,000 and \$2,506,000 for the nine and three months ended June 30, 2003, respectively, and \$7,948,000 and \$2,837,000 for the nine and three months ended June 30, 2002, respectively.

Note 6. Comprehensive income

Comprehensive income is the total of net income and other changes in equity. Total comprehensive income for the nine and three months ended June 30, 2003 and 2002 was as follows:

| Nine Months Ended June 30, | | Three Months Ended June 30, | |
|-------------------------------|------|--------------------------------|------|
| 2003 | 2002 | 2003 | 2002 |

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| | (in thousands) | | (in thousands) | |
|--|----------------|----------|----------------|----------|
| Net income | \$ 1,828 | \$ 4,970 | \$ 1,892 | \$ 1,755 |
| Other comprehensive income, interest rate cap adjustment | | 63 | | |
| | \$ 1,828 | \$ 5,033 | \$ 1,892 | \$ 1,755 |

Note 7. Retirement of Executive Officers

On November 26, 2002, the Company announced the retirement and resignation of A. Kenneth Pincourt, Jr., its Founder, Chairman and Chief Executive Officer. The Company has entered into a retirement agreement with Mr. Pincourt, setting forth the terms of his retirement and resignation. The retirement agreement replaces Mr. Pincourt's previous employment agreement. Under the retirement agreement, the Company elected to accelerate retirement benefits under its deferred compensation program and to continue to pay compensation and provide related benefits through July 15, 2004, the remaining term of Mr. Pincourt's previous employment contract.

Accelerated benefits under the deferred program amounted to \$1,040,987, of which \$549,220 had been accrued as of September 30, 2002. Mr. Pincourt's deferred compensation was paid to him on December 13, 2002. Also under the retirement agreement, Mr. Pincourt will continue to receive monthly payments of \$41,004 through July 15, 2004, one bonus payment of \$150,491 payable on or before October 31, 2003, and a second bonus payment of \$119,138 payable on or before August 31, 2004. Among other benefits, Mr. Pincourt is also able to participate in any health insurance plan, employee benefit plan or other arrangement made available by the Company or its subsidiaries to its executives and key management employees, through July 15, 2004. The Company recorded a charge for the retirement of Mr. Pincourt during the first quarter of fiscal 2003. The effect of this charge was included in other expense in the Company's consolidated statement of income and amounted to \$1,503,925 before income taxes.

The following table summarizes the charge made during the first quarter for Mr. Pincourt's retirement:

| | | |
|---|----|-----------|
| Deferred compensation | \$ | 1,040,987 |
| Compensation and related benefits | | 1,012,158 |
| Total | | 2,053,145 |
| Less deferred compensation accrued as of September 30, 2002 | | (549,220) |
| Charged to expense | \$ | 1,503,925 |

On May 22, 2003, the Company announced the retirement of Troy Edwards, its Chief Financial Officer, Secretary, Treasurer and Controller. The Company recorded a charge for the retirement of Mr. Edwards of \$207,683 during the third quarter of fiscal 2003. The effect of this charge was included in other expense in the Company's consolidated statement of income.

Note 8. Income Taxes

As of June 30, 2003, the Company had a tax loss from U.S. operations of \$2.5 million, and the Company currently estimates that its tax loss from U.S. operations through September 30, 2003 will be \$3.0 million. The net operating loss will be carried back to prior tax years resulting in a refund of approximately \$0.9 million. As of June 30, 2003, the estimated refund has been recorded as an income tax benefit in the Company's consolidated statement of income and as a receivable included in other current assets on the Company's consolidated balance sheet.

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

Forward-Looking Statements

Management's Discussion and Analysis contains Forward-Looking Statements, as defined in section 27a of the Securities Act of 1933, as amended, and Section 21e of the Securities Exchange Act of 1934, as amended. Forward-Looking Statements are statements other than historical information or statements of current condition and relate to future events or the future financial performance of the Company. Some Forward-Looking Statements may be identified by use of such terms as believes, anticipates, intends or expects. Such Forward-Looking Statements involve known and unknown risks, uncertainties and other factors that may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such Forward-Looking Statements. The following is a list of factors, among others, that could cause actual results to differ materially from those contemplated by the Forward-Looking Statements: business conditions in certain market segments and industries and the general economy; competitive factors, including increased competition and price pressures; availability of third-party component products at reasonable prices; increased excise taxes; foreign currency exposure; changes in product mix between and among product lines; lower than expected customer orders and quarterly seasonal fluctuations of those orders; and product shipment interruptions. The Company undertakes no obligation to update or revise any Forward-Looking Statements, whether as a result of new information, future events or otherwise.

Introduction

The following discussion and analysis summarizes the significant factors affecting (i) consolidated results of operations of the Company for the nine months ended June 30, 2003 compared to the nine months ended June 30, 2002, (ii) consolidated results of operations of the Company for the three months ended June 30, 2003 compared to the three months ended June 30, 2002, and (iii) financial liquidity and capital resources. This discussion and analysis should be read in conjunction with the Company's consolidated financial statements and notes thereto included herein. Certain amounts presented in this Item 2 have been rounded to the nearest thousand or hundred thousand, as applicable, but the percentages calculated are based on actual amounts without rounding.

The Company operates primarily in the beverage alcohol industry in the United States. The Company is a leading producer and supplier of brandy, rum, wine and spirits to other beverage alcohol manufacturers; produces, imports and markets premium branded spirits; bottles beverage alcohol and other beverages on a contract basis and under its own labels; and produces vinegar and cooking wine. The Company reports its operating results in four segments: Bulk Alcohol Products (citrus brandy, citrus spirits, rum, cane spirits, fortified citrus wine, purchased distilled products and byproducts); Premium Branded Spirits (primarily Cruzan Estate Rums and Cruzan Flavored Rums); Bottling Operations (contract bottling services and proprietary and private label products); and Vinegar and Cooking Wine (bulk vinegar, bulk cooking wine, vinegar stock and proprietary and private label case goods).

Information regarding the net sales, operating income and total assets of each of the Company's business segments and information regarding geographic areas is set forth in Note 5 to the consolidated financial statements.

The Company's net sales and gross margins (gross profit as a percentage of net sales) vary depending on the mix of business among the Company's products. Historically, gross margins have been highest in bulk alcohol products and premium branded spirits and lower in bottling operations and vinegar and cooking wine operations.

The Company has a limited number of customers, and these customers often purchase bulk alcohol products in significant quantities or place significant orders for contract bottling services, distilled spirits, vinegar and cooking wine. Accordingly, the size and timing of purchase orders and product shipments can cause operating results to fluctuate significantly from quarter to quarter. Additionally, some Company products generate higher profit margins than others, and changes in the Company's product mix can cause gross margins to fluctuate. Certain aspects of the Company's business are seasonal, with increased demand for the Company's contract bottling services from April to October and increased production of the Company's bulk alcohol products from November to June, corresponding to

the Florida citrus harvest. As a result of these factors, the Company's operating results may vary significantly from quarter to quarter.

Net sales represent the Company's gross sales less excise taxes. Excise taxes are generally payable on products bottled by the Company. In addition, excise taxes are payable on sales of industrial alcohol to certain customers. Accordingly, excise taxes vary from period to period depending upon the Company's product and customer mix.

Results of Operations

The following table sets forth statement of income items as a percentage of net sales.

| | Nine Months Ended June 30, | | Three Months Ended June 30, | |
|--|-------------------------------|--------|--------------------------------|--------|
| | 2003 | 2002 | 2003 | 2002 |
| Net sales | 100.0% | 100.0% | 100.0% | 100.0% |
| Cost of goods sold | 67.4 | 67.9 | 65.1 | 66.7 |
| Gross margin | 32.6 | 32.1 | 34.9 | 33.3 |
| Selling, general and administrative expenses | 26.4 | 21.4 | 27.3 | 22.3 |
| Operating income | 6.2 | 10.7 | 7.6 | 11.0 |
| Interest expense | (3.9) | (2.8) | (4.3) | (2.5) |
| Other income (expense), net | (0.7) | 1.2 | 1.8 | 0.7 |
| Income before income taxes | 1.6 | 9.1 | 5.1 | 9.2 |
| Income tax (expense) benefit | 1.2 | (2.3) | 3.1 | (2.4) |
| Net income | 2.8% | 6.8% | 8.2% | 6.8% |

The following table provides information on net sales of certain Company products.

| | Nine Months Ended June 30, | | | Three Months Ended June 30, | | |
|--------------------------|-------------------------------|-----------|----------|--------------------------------|-----------|----------|
| | 2003 | 2002 | % Change | 2003 | 2002 | % Change |
| | (in thousands) | | | (in thousands) | | |
| Bulk Alcohol Products | \$ 26,276 | \$ 26,911 | (2.4) | \$ 8,749 | \$ 9,219 | (5.1) |
| Premium Branded Spirits | 13,521 | 15,134 | (10.7) | 4,796 | 6,702 | (28.5) |
| Bottling Operations | 10,953 | 14,923 | (26.6) | 4,542 | 4,718 | (3.7) |
| Vinegar and Cooking Wine | 15,127 | 15,777 | (4.1) | 5,001 | 5,294 | (5.5) |
| | \$ 65,877 | \$ 72,745 | (9.4) | \$ 23,088 | \$ 25,933 | (11.0) |

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The following table provides unit sales volume data for certain Company products.

| | Nine Months Ended June 30, | | | Three Months Ended June 30, | | |
|--------------------------------------|-------------------------------|------------------------|----------|--------------------------------|------------------------|----------|
| | 2003 (in thousands) | 2002 (in thousands) | % Change | 2003 (in thousands) | 2002 (in thousands) | % Change |
| Bulk alcohol products: | | | | | | |
| Distilled products, in proof gallons | | | | | | |
| Citrus Brandy | 1,131 | 928 | 21.8 | 260 | 268 | (3.0) |
| Citrus Spirits | 238 | 430 | (44.6) | 55 | 156 | (64.5) |
| Rum | 3,323 | 3,238 | 2.6 | 1,176 | 1,265 | (7.0) |
| Cane Spirits | 389 | 485 | (19.8) | 144 | 146 | (0.9) |
| Fortified citrus wine, in gallons | 7,559 | 7,613 | (0.7) | 2,531 | 2,506 | 1.0 |
| Premium branded spirits, in cases | 360 | 414 | (12.9) | 133 | 233 | (42.6) |
| Bottling operations, in cases | 2,876 | 4,540 | (36.7) | 1,435 | 1,360 | 5.5 |
| Vinegar | | | | | | |
| Bulk, in 100 grain gallons | 4,290 | 4,112 | 4.3 | 1,588 | 1,294 | 22.7 |
| Cases | 396 | 518 | (23.7) | 125 | 160 | (22.0) |
| Drums, in 100 grain gallons | 1,162 | 1,302 | (10.8) | 389 | 527 | (26.3) |
| Cooking Wine | | | | | | |
| Bulk, in gallons | 3,226 | 3,350 | (3.7) | 1,048 | 1,273 | (17.7) |
| Cases | 476 | 519 | (8.3) | 126 | 141 | (11.3) |

Nine months ended June 30, 2003 compared to nine months ended June 30, 2002. Unless otherwise noted, references to 2003 represent the nine-month period ended June 30, 2003 and references to 2002 represent the nine-month period ended June 30, 2002. In 2002, net sales and cost of goods sold of premium branded spirits included excise taxes of approximately \$2.0 million, representing excise taxes included in cases sold from warehouses located outside of the Company's Florida bonded warehouse facilities. Beginning October 1, 2002, the Company no longer includes excise taxes in net sales and cost of goods sold of premium branded spirits case sales from locations outside of the Company's Florida bonded warehouse facilities. Net sales and cost of sales in 2002 have been reclassified to conform to the 2003 presentation.

Net Sales. Net sales were \$65.9 million in 2003, a decrease of 9.4% from net sales of \$72.7 million in 2002.

Net sales of bulk alcohol products were \$26.3 million in 2003, a decrease of 2.4% from net sales of \$26.9 million in 2002. The decrease resulted primarily from decreased shipments of citrus spirits, cane spirits and fortified citrus wine. Due to a decrease in orders from certain customers, management believes that its fortified wine volume in fiscal 2003 may decline by approximately 5% from fiscal 2002. In 2002, the Company had sales of citrus and cane spirits to new customers that had difficulty sourcing bulk alcohol from their regular suppliers. These sales are not expected to reoccur in 2003.

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Net sales of premium branded spirits were \$13.5 million in 2003, a decrease of 10.7% from net sales of \$15.1 million in 2002. In 2002, net sales of premium branded spirits included \$1.9 million of bulk tequila sales, and \$1.2 million of new Cruzan ready-to-drink products. Bulk tequila sales represent the liquidation of inventory that was held to produce Porfidio tequila. During the third quarter of 2002, the Company introduced a new line of Cruzan products in the new ready-to-drink category and sold approximately 101,000 cases of this new product through June 30, 2002. Due to increased competition and management's expectation of limited growth potential within the ready-to-drink product category, the Company made a strategic decision to exit this category and concentrate on the growing segment of its premium branded spirits business, Cruzan Rums and Cruzan Flavored Rums. Excluding bulk tequila and new Cruzan ready-to-drink product sales, net sales of premium branded spirits were \$13.5 million in 2003, an increase of 12.4% from net sales of \$12.0 million in 2002. Sales of the Company's Cruzan Estate Rums

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and Cruzan Flavored Rums, collectively, increased 9.6% and Cruzan Flavored Rums alone increased 11.2% in 2003 compared to 2002.

Net sales of the Company's bottling operations were \$11.0 million in 2003, a decrease of 26.6% from net sales of \$14.9 million in 2002. The unit volume of the Company's bottling operations decreased 36.7% in 2003 as a result of the decision of a large bottling customer to shift production from the Company to its own bottling facilities. During fiscal 2002, this customer represented approximately 48% of the Company's unit volume in bottling operations. Management believes that this loss in volume will be partially offset by increased business with new and existing customers and that total bottling operations volume may decline by approximately 33% in fiscal 2003. During the third quarter of fiscal 2003, management implemented a plan to consolidate the Company's bottling operations to increase efficiencies and reduce overhead in the future. Management expects to realize cost savings from this plan beginning in the first quarter of fiscal 2004, with these cost savings increasing in the second, third and fourth quarters of fiscal 2004.

Net sales of vinegar and cooking wine were \$15.1 million in 2003, a decrease of 4.1% from net sales of \$15.8 million in 2002. Management believes that the decrease in net sales is due to increased competition and the timing of customer orders.

Gross Profit. Gross profit was \$21.5 million in 2003, a decrease of 8.1% from gross profit of \$23.3 million in 2002. Gross margin increased to 32.6% in 2003 from 32.1% in 2002.

Selling, General and Administrative Expenses. Selling, general and administrative expenses were \$17.4 million in 2003, an increase of 11.5% from \$15.6 million in 2002. The increase was primarily attributable to increased administrative, marketing and advertising expenses related to the Company's premium branded spirits business. The Company has increased its administrative, marketing and advertising expenses in its premium branded spirits business as it continues to place emphasis on this growing business segment.

Operating Income. The following table sets forth the operating income (loss) by reportable segment of the Company for 2003 and 2002.

| | Nine Months Ended June 30, | | | % Change |
|--------------------------------|-------------------------------|----------|--|----------|
| | 2003 | 2002 | | |
| | (In thousands) | | | |
| Bulk Alcohol Products | \$ 8,673 | \$ 8,235 | | 5.3 |
| Premium Branded Spirits | (1,290) | (230) | | |
| Bottling Operations | (1,450) | 973 | | |
| Vinegar and Cooking Wine | 2,947 | 3,306 | | (10.8) |
| Corporate Operations and Other | (4,819) | (4,535) | | |
| | \$ 4,061 | \$ 7,749 | | (47.6) |

As a result of the above factors, operating income was \$4.1 million in 2003, a decrease of 47.6% from operating income of \$7.7 million in 2002.

The Company's premium branded spirits segment experienced operating losses of \$1.3 million in 2003 and \$0.2 million in 2002. The operating losses reflected the Company's continuing efforts to increase market share by reinvesting segment gross profits in selling and marketing expenses. Included in the operating loss of premium branded spirits in 2002 was profit of \$0.5 million related to bulk tequila sales. Excluding bulk tequila sales, operating loss of premium branded spirits would have been \$0.7 million in 2002.

The Company's bottling operations segment reported an operating loss of \$1.5 million in 2003 compared to operating income of \$1.0 million in 2002. The operating loss reflected the decision of a large bottling customer to shift production from the Company to its own bottling facilities. This customer represented approximately 48% of the Company's annual bottling operations unit volume for fiscal year 2002. Management believes that this loss in volume will be partially offset by increased business with new and existing customers and that total bottling operations volume may decline by approximately 33% in fiscal 2003. During the third quarter of fiscal 2003, management implemented a plan to consolidate the Company's bottling operations to increase efficiencies and reduce overhead in the future. Management expects to realize cost savings from this plan beginning in the first quarter of fiscal 2004, with these cost savings increasing in the second, third and fourth quarters of fiscal 2004.

Interest Expense. Interest expense was \$2.6 million in 2003 and \$2.1 million in 2002. The increase in interest expense was due to higher interest rates during 2003 as compared to 2002 and the payment of \$296,250 in waiver fees during 2003 as described in Note 3 to the consolidated financial statements. The Company's interest rate under the term-loan and revolving credit agreement was increased 50 basis points effective January 1, 2003 and an additional 50 basis points effective May 14, 2003.

Other Expense. On November 26, 2002, the Company announced the retirement and resignation of A. Kenneth Pincourt, Jr., its Founder, Chairman and Chief Executive Officer. The Company has entered into a retirement agreement with Mr. Pincourt, setting forth the terms of his retirement and resignation. The retirement agreement replaces Mr. Pincourt's previous employment agreement. Under the retirement agreement, the Company elected to accelerate retirement benefits under its deferred compensation program and to continue to pay compensation and provide related benefits through July 15, 2004, the remaining term of Mr. Pincourt's previous employment contract.

Accelerated benefits under the deferred program amounted to \$1,040,987, of which \$549,220 had been accrued as of September 30, 2002. Mr. Pincourt's deferred compensation was paid to him on December 13, 2002. Also under the retirement agreement, Mr. Pincourt will continue to receive monthly payments of \$41,004 through July 15, 2004, one bonus payment of \$150,491 payable on or before October 31, 2003, and a second bonus payment of \$119,138 payable on or before August 31, 2004. Among other benefits, Mr. Pincourt is also able to participate in any health insurance plan, employee benefit plan or other arrangement made available by the Company or its subsidiaries to its executives and key management employees, through July 15, 2004. The Company recorded a charge for the retirement of Mr. Pincourt during the first quarter of fiscal 2003. The effect of this charge was included in other expense in the Company's consolidated statement of income and amounted to \$1,503,925 before income taxes.

The following table summarizes the charge made during the first quarter for Mr. Pincourt's retirement:

| | | |
|---|----|-----------|
| Deferred compensation | \$ | 1,040,987 |
| Compensation and related benefits | | 1,012,158 |
| Total | | 2,053,145 |
| Less deferred compensation accrued as of September 30, 2002 | | (549,220) |
| Charged to expense | \$ | 1,503,925 |

On May 22, 2003, the Company announced the retirement of Troy Edwards, its Chief Financial Officer, Secretary, Treasurer and Contoller. The Company recorded a charge for the retirement of Mr. Edwards of \$207,683 during the third quarter of fiscal 2003. The effect of this charge was included in other expense in the Company's consolidated statement of income.

Income Tax Expense. The Company's effective income tax rate was 24.9% in 2002. The low tax rate was attributable to a 90% exemption of the Company's Virgin Islands subsidiary from U.S. Virgin Islands income taxes. The exemption is effective through September 2020. In addition, the Company benefited from the extraterritorial income exclusion in 2003 and 2002. During 2003, the Company incurred operating losses from its U.S. operations and recorded an

income tax benefit of \$0.9 million.

Three months ended June 30, 2003 compared to three months ended June 30, 2002. Unless otherwise noted, references to 2003 represent the three-month period ended June 30, 2003 and references to 2002 represent the three-month period ended June 30, 2002. In 2002, net sales and cost of goods sold of premium branded spirits included excise taxes of approximately \$0.9 million, representing excise taxes included in cases sold from warehouses located outside of the Company's Florida bonded warehouse facilities. Beginning October 1, 2002, the Company no longer includes excise taxes in net sales and cost of goods sold of premium branded spirits case sales from locations outside of the Company's Florida bonded warehouse facilities. Net sales and cost of sales in 2002 have been reclassified to conform to the 2003 presentation.

Net Sales. Net sales were \$23.1 million in 2003, a decrease of 11.0% from net sales of \$25.9 million in 2002.

Net sales of bulk alcohol products were \$8.7 million in 2003, a decrease of 5.1% from net sales of \$9.2 million in 2002. Management believes that the decrease in bulk alcohol shipments is primarily due to the timing of customer orders. However, in 2002, the Company had sales of citrus and cane spirits to new customers that had difficulty sourcing bulk alcohol from their regular suppliers. These sales are not expected to reoccur in 2003.

Net sales of premium branded spirits were \$4.8 million in 2003, a decrease of 28.5% from net sales of \$6.7 million in 2002. In 2002, net sales of premium branded spirits included \$0.7 million in sales of Antiqueno Aguardiente compared to \$0.2 million in sales of Antiqueno Aguardiente in 2003, and \$1.2 million of new Cruzan ready-to-drink products. During the third quarter of 2002, the Company entered into a settlement agreement with the producer of Antiqueno Aguardiente and was reappointed exclusive U.S. importer of Antiqueno Aguardiente for a four-year period. The Company resumed sales of Antiqueno Aguardiente in June 2002 after not having received a product shipment since June 2001, and therefore, the replenishment of inventories by customers resulted in a one time increase in these sales. During the third quarter of 2002, the Company introduced a new line of Cruzan products in the new ready-to-drink category and sold approximately 101,000 cases of this new product through June 30, 2002. Due to increased competition and management's expectation of limited growth potential within the ready-to-drink product category, the Company made a strategic decision to exit this category and concentrate on the growing segment of its premium branded spirits business, Cruzan Rums and Cruzan Flavored Rums. Excluding pipeline sales of Antiqueno Aguardiente and new Cruzan ready-to-drink product sales, net sales of premium branded spirits were \$4.8 million in 2003, a decrease of 4.4% from net sales of \$5.0 million in 2002. Sales of the Company's Cruzan Estate Rums and Cruzan Flavored Rums, collectively, decreased 10.9% and Cruzan Flavored Rums alone decreased 12.2% in 2003 compared to 2002. During the quarter ended June 30, 2003, Bacardi, Ltd., the world's largest rum supplier, entered the flavored rum category with the introduction of four flavored rum products. There were also product introductions in the flavored rum category by at least three other rum producers. This increase in competition in the flavored rum category, along with price decreases by the Company's major competitors in the rum segment, affected the Company's retail shelf space allocation and product sales. However, distributor's sales of Cruzan Rum products to retailers continue to be strong. Therefore, management believes that the effect of these new product introductions and price promotions will be short-term and that over the long-term the Company's Cruzan Rum brands will return to strong growth in this growing product segment.

Net sales of the Company's bottling operations were \$4.5 million in 2003, a decrease of 3.7% from net sales of \$4.7 million in 2002. The unit volume of the Company's bottling operations increased 5.5% in 2003 as a result of increased business with new and existing customers. However, the average price per case of product sold decreased. During the third quarter of fiscal 2003, management implemented a plan to consolidate the Company's bottling operations to increase efficiencies and reduce overhead in the future. Management expects to realize cost savings from this plan beginning in the first quarter of fiscal 2004, with these cost savings increasing in the second, third and fourth quarters of fiscal 2004.

Net sales of vinegar and cooking wine were \$5.0 million in 2003, a decrease of 5.5% from net sales of \$5.3 million in 2002. Management believes that the decrease in net sales is due to increased competition and the timing of customer orders.

Gross Profit. Gross profit was \$8.1 million in 2003, a decrease of 6.7% from gross profit of \$8.6 million in 2002. Gross margin increased to 34.9% in 2003 from 33.3% in 2002. The increase in gross margin was primarily attributable to a favorable change in product mix.

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Selling, General and Administrative Expenses. Selling, general and administrative expenses were \$6.3 million in 2003, an increase of 9.1% from \$5.8 million in 2002. The increase was primarily attributable to increased administrative, marketing and advertising expenses related to the Company's premium branded spirits business. The Company has increased its administrative, marketing and advertising expenses in its premium branded spirits business as it continues to place emphasis on this growing business segment.

Operating Income. The following table sets forth the operating income (loss) by reportable segment of the Company for 2003 and 2002.

| | Three Months Ended June 30, | | | % Change |
|--------------------------------|--------------------------------|---------|----------|----------|
| | 2003 | | 2002 | |
| | (In thousands) | | | |
| Bulk Alcohol Products | \$ | 2,900 | \$ 2,835 | 2.3 |
| Premium Branded Spirits | | (544) | 312 | |
| Bottling Operations | | 287 | (35) | |
| Vinegar and Cooking Wine | | 895 | 1,203 | (25.6) |
| Corporate Operations and Other | | (1,778) | (1,450) | |
| | \$ | 1,760 | \$ 2,865 | (38.6) |

As a result of the above factors, operating income was \$1.8 million in 2003, a decrease of 38.6% from operating income of \$2.9 million in 2002.

The Company's bottling operations segment reported operating income of \$0.3 million in 2003 compared to breaking even in 2002. The operating loss reflected the decision of a large bottling customer to shift production from the Company to its own bottling facilities. This customer represented approximately 48% of the Company's annual bottling operations unit volume for fiscal year 2002. Management believes that this loss in volume will be partially offset by increased business with new and existing customers and that total bottling operations volume may decline by approximately 33% in fiscal 2003. During the third quarter of fiscal 2003, management implemented a plan to consolidate the Company's bottling operations to increase efficiencies and reduce overhead in the future. Management expects to realize cost savings from this plan beginning in the first quarter of fiscal 2004, with these cost savings increasing in the second, third and fourth quarters of fiscal 2004.

Interest Expense. Interest expense was \$1.0 million in 2003 and \$0.6 million in 2002. The increase in interest expense was due to higher interest rates during 2003 as compared to 2002 and the payment of a \$160,000 waiver fee during 2003 as described in Note 3 to the consolidated financial statements. The Company's interest rate under the term-loan and revolving credit agreement was increased 50 basis points effective January 1, 2003 and an additional 50 basis points effective May 14, 2003.

Income Tax Expense. The Company's effective income tax rate was 26.3% in 2002. The low tax rate was attributable to a 90% exemption of the Company's Virgin Islands subsidiary from U.S. Virgin Islands income taxes. The exemption is effective through September 2020. In addition, the Company benefited from the extraterritorial income exclusion in 2003 and 2002. During 2003, the Company incurred operating losses from its U.S. operations and recorded an income tax benefit of \$0.9 million.

Financial Liquidity and Capital Resources

General

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The Company's principal use of cash in its operating activities is for purchasing raw materials to be used in its manufacturing operations, purchasing imported products for its premium branded spirits business and carrying inventories and receivables. The Company's source of liquidity has historically been cash flow from operations and its line of credit. Some of the Company's manufacturing operations are seasonal and the Company's borrowings on its line of credit vary during the year. For example, the Company uses citrus molasses as its primary raw material in the production of citrus brandy and spirits at its two Florida distilleries. The Company buys citrus molasses, a by-product of citrus juice production, from local manufacturers of citrus juice and concentrate during the citrus harvest, which generally runs from November to June. The Company generally begins purchasing citrus molasses in November and manufactures and builds inventory of citrus brandy and spirits. The Company manufactures and builds inventory while raw materials are available due to the short life of the citrus molasses it purchases. Another seasonal business of the Company is its contract bottling services. Demand for contract bottling services is highest during the months from April through October. Management believes that cash provided by its operating and

financing activities will provide adequate resources to satisfy its working capital, liquidity and anticipated capital expenditure requirements for both its short-term and long-term capital needs.

Operating Activities

Net cash provided by operating activities in 2003 was \$5.6 million, which resulted from \$5.7 million in net income adjusted for noncash items, and \$0.1 million representing the net increase in operating assets and liabilities.

The Company currently has approximately \$2.1 million of ready-to-drink finished goods inventory and related raw materials and supplies, the sales of which have not yet met expectations. The Company continues to sell this inventory in the ordinary course and during July entered into a barter agreement with a large media trading company for the trade of a portion of this inventory in exchange for media advertising and other trade credits. The Company believes that the value of the media advertising and other trade credits received is at least equal to the book value of the inventory exchanged.

Investing and Financing Activities

Net cash used in investing activities in 2003 was \$2.3 million, which resulted primarily from \$2.7 million of capital expenditures.

Net cash used in financing activities in 2003 was \$3.1 million, which resulted primarily from payments of \$3.2 million of long-term debt.

The Company's revolving credit facility provides for maximum borrowings of \$30 million. Borrowings under this facility were \$20.6 million at June 30, 2003 (see Note 3 to the consolidated financial statements).

The Company's bank debt was \$53.6 million as of June 30, 2003, and its ratio of total debt to equity was 1.04 to 1.

As of December 31, 2002 and March 31, 2003, the Company was not in compliance with the Funded Debt to EBITDA (earnings before interest, taxes, depreciation and amortization) financial covenant under its credit agreement. In addition, as of March 31, 2003 the Company was not in compliance with its Interest Coverage and Fixed Charge Coverage financial covenants. On February 18, 2003, the Company received a waiver for the December 31, 2002 covenant violation. On May 14, 2003, the Company received a waiver of the March 31, 2003 covenant violations and amended the credit agreement prospectively to reset the levels of certain financial covenants to reflect the Company's current business plan and forecasts. The Company paid a fee of \$136,250 for the December waiver and \$160,000 for the March waiver and amendment. The Company's interest rate under the term-loan and revolving credit agreement was increased 50 basis points effective January 1, 2003 and an additional 50 basis points effective May 14, 2003.

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The Company's share of the undistributed earnings of the Bahamian and Virgin Islands subsidiaries was approximately \$7.5 million and \$27.9 million, respectively, as of September 30, 2002. See Note 10 to the Company's consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended September 30, 2002 for additional information on income taxes related to these subsidiaries.

Based on current plans and business conditions, management expects that its cash, cash equivalents, and short-term investments, together with any amounts generated from operations and available borrowings, will be sufficient to meet the Company's cash requirements for at least the next 12 months.

Effects of Inflation and Changing Prices

The Company's results of operations and financial condition have not been significantly affected by inflation and changing prices. The Company has been able, subject to normal competitive conditions, to pass along rising costs through increased selling prices.

Critical Accounting Policies

The Company's significant accounting policies are more fully described in Note 1 to the Company's consolidated financial statements located in Item 8 of its Annual Report on Form 10-K. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, and expenses, and the related disclosures of contingent assets and liabilities. Actual results could differ from those estimates under different assumptions or conditions. The Company believes that the following critical accounting policy is subject to estimates and judgments used in the preparation of its consolidated financial statements:

The Company has goodwill and intangible assets associated with business acquisitions. The Company reviews these assets for impairment annually and whenever an event occurs or circumstances change that would more likely than not reduce the fair value of these assets below their carrying value. If the fair value of these assets is less than their carrying value, then an impairment loss would be recognized equal to the excess of the carrying value over the fair value of the asset.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

The information required under this Item 3 is incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended September 30, 2002.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, management, including the Company's Chief Executive Officer and Chief Financial Officer, carried out an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rules 13a-15(e) or 15d-15(e) under the Securities Exchange Act, as amended). Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures are effective in timely alerting them to material information required to be included in the Company's periodic SEC reports. It should be noted that 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, regardless of how remote.

Changes in Internal Controls

In addition, management, including the Company's Chief Executive Officer and Chief Financial Officer, reviewed the Company's internal controls, and there have been no significant changes in the internal controls during the Company's most recently completed fiscal quarter that

could significantly affect those controls subsequent to the date of their last evaluation.

PART II. OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

- 3.1 Amended and Restated Certificate of Incorporation of Todhunter International, Inc. (1)
- 3.2 Amended and Restated By-Laws of Todhunter International, Inc. (5)
- 4.1 Form of Todhunter International, Inc. Common Stock Certificate (1)
- 10.6 Todhunter International, Inc. 1992 Stock Option Plan, as amended (3)
- 10.8 Lease, dated March 24, 1988, as amended, between Todhunter International, Inc. and Esperanté Limited Partnership (1)
- 10.8(a) Amendment to Lease, dated January 1, 1997, between Todhunter International, Inc. and Florida Acquisition Fund Esperanté, Ltd. (4)

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- 10.18 Executive Employment Agreement dated as of July 15, 1999, between Thomas A. Valdes and Todhunter International, Inc. (5)
- 10.19 Executive Employment Agreement dated as of July 15, 1999, between Jay S. Maltby and Todhunter International, Inc. (5)
- 10.21 Executive Employment Agreement dated as of July 15, 1999, between D. Chris Mitchell and Todhunter International, Inc. (5)
- 10.22 Amended and Restated Credit Agreement dated as of October 19, 2001, by and among Todhunter International, Inc., and each of the Financial Institutions Initially a Signatory thereto, and SouthTrust Bank (6)
- 10.22(a) Waiver of Defaults Under Credit Agreement, dated February 18, 2003, by and among Todhunter International, Inc., SouthTrust Bank, acting as lender and Agent, Wachovia Bank, N.A., National City Bank and SunTrust Bank (8)
- 10.22(b) Modification of Credit Agreement, dated May 14, 2003, by and among Todhunter International, Inc., SouthTrust Bank, acting as lender and Agent, Wachovia Bank, N.A., National City Bank and SunTrust Bank (10)
- 10.23 Agreement and General Release of All Claims between Todhunter International, Inc. and A. Kenneth Pincourt, Jr., dated as of November 26, 2002 (7)
- 11.1 Statement of Computation of Per Share Earnings (9)
- 20.1 Earnings press release for the three-month and nine-month periods ended June 30, 2003 (10)
- 21.1 Subsidiaries of Todhunter International, Inc. (2)
- 31.1 Certification of Jay S. Maltby, Chairman, Chief Executive Officer and President, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 (10)
- 31.2 Certification of Ezra Shashoua, Executive Vice President and Chief Financial Officer, pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 (10)
- 32.1 Certification of Jay S. Maltby, Chairman, Chief Executive Officer and President, pursuant to 18 U.S.C. Section 1350 (10)
- 32.2 Certification of Ezra Shashoua, Executive Vice President and Chief Financial Officer, pursuant to 18 U.S.C. Section 1350 (10)

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- (1) Incorporated herein by reference to the Company's Registration Statement on Form S-1 (File No. 33-50848).
 - (2) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended September 30, 1995.
 - (3) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended September 30, 1997.
 - (4) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended September 30, 1998.
 - (5) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended September 30, 1999.
 - (6) Incorporated herein by reference to the Company's Annual Report on Form 10-K for the year ended September 30, 2001.
 - (7) Incorporated herein by reference to the Company's Report on Form 8-K for November 26, 2002.
 - (8) Incorporated herein by reference to the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2003.
 - (9) Filed herewith and incorporated herein by reference to Note 4 of notes to consolidated financial statements, included in Item 1 of the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2003.
 - (10) Filed herewith.

(b) Reports on Form 8-K

During the third quarter of fiscal 2003, the Company filed the following current report on Form 8-K:

- (1) Form 8-K dated May 15, 2003. This Form 8-K reported information under Item 9 (Regulation FD Disclosure).
- (2) Form 8-K dated May 22, 2003. This Form 8-K reported information under Item 5 (Other Events and required FD Disclosure).

Signatures

Pursuant to the requirements 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.

Date: August 14, 2003

/s/ Jay S. Maltby
Jay S. Maltby
Chairman, Chief Executive Officer and President

Date: August 14, 2003

/s/ Ezra Shashoua
Ezra Shashoua
Executive Vice President and Chief Financial Officer