



140 BROADWAY NEW YORK, NY 10005

ROBERT J. CUMMINS, CFA
(212) 651-0815

TRADING DESK
(212) 320-3001

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COMPANY SUMMARY

Tuesday, February 1, 2005

Speaker: Bob Cummins

Food Industry Comment:

Dean Foods (DF-\$35.30) last week announced plans to spin off the smallest of its three business segments, the Specialty Foods Group, to Dean shareholders in a tax-free transaction. This move should enhance Dean's valuation, since it will eliminate a non-core business that is oriented toward private label and foodservice products rather than branded lines, and that has had a somewhat unpredictable record. On the other hand, the spinoff company may also prove attractive to investors, in view of its significant recovery potential (operating income declined 35% in the first nine months of 2004), as well as the appointment of a new management team that we consider one of the best in the food industry, having achieved a dramatic turnaround at Keebler in the late 1990s. In the press release announcing the spinoff, Dean's management reiterated its expectation of 2005 EPS (including Specialty Foods) in the \$2.20-\$2.30 range, indicating growth of 9%-14%, after a flat year in 2004 caused by high milk costs and other problems. We reiterate our Strong Buy ("1") on this dynamic company, and are raising our 12-month target price from \$38-\$39 to \$40-\$41.

The Specialty Foods Group, which was part of the "old" Dean Foods, acquired in December, 2001, has annual sales of about \$700 million, or 7% of DF's total. Its businesses are relatively mature, but it has typically had healthy operating margins in the low to mid-teens, well above those of Dean's other two segments. It is believed to be the second largest producer of pickles (after Vlasic) and of non-dairy powdered coffee creamers (after Nestle), but although it has some regional brands, it is primarily a supplier of private label products to retailers and foodservice customers. Its other lines include aseptic cheese sauces, puddings, peppers, dressings, liquid coffee creamers, and egg substitutes. Its poor earnings performance in 2004 reflected high ingredient, packaging and transportation costs, reduced earnings in pickles due to weak demand and a late cucumber harvest, and the discontinuance and writeoff of a contract packing business. Management is forecasting a recovery in 2005, with margins back to 12%-14% of sales (equating to EPS of \$0.37-\$0.39 per DF share), compared with only 9.8% for the January-September 2004 period.

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See pages 3 to 5 of report for important disclosures and Analyst's Certification.

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The spinoff will create a new publicly traded company with a debt-free balance sheet. It is anticipated that the shares will be distributed in the third quarter of 2005. As mentioned, we are particularly intrigued by the new management team for Specialty Foods, who have already joined the company, and have invested \$10 million of their own funds in the Specialty unit. The two top officers are Sam Reed, Chairman and CEO, and David Vermylen, President and COO, who took charge at Keebler in 1996, when it was operating in the red, and transformed it into one of the fastest-growing companies in the food industry, culminating in its acquisition by Kellogg in 2001. Based on our confidence in Messrs. Reed and Vermylen, we will consider initiating coverage of the new company once it begins trading.

Meanwhile, the Dean Foods management continues to follow its strategy of leveraging the infrastructure, expertise and cash flow of its fresh dairy products business, which is by far the largest in that field, to build its Branded Products Group, which is its primary growth vehicle. Having gained critical mass, with 2004 sales estimated at \$1.1 billion, that segment is now reporting significant profit improvement while continuing to spend aggressively on advertising and promotion.

In the nine months ended September, Branded Products sales increased 70%, including internal growth estimated at 32%, and the balance from the acquisition of Horizon Organic last January. Operating income for the segment rose to \$66.4 million, or 12% of the company total, up from only \$10.5 million (2%) a year earlier. For 3Q-04 alone, the Horizon brand registered unit volume growth of 28%, while Silk rose 29%, International Delight 29%, and Land O'Lakes 14%. The 3Q profit margin for the group reached a healthy 10.8% of sales, versus a small loss a year earlier. We expect that 4Q results, to be reported on February 10th, will show continued strong sales and earnings progress in Branded Products, and are bullish on the prospects for 2005 and beyond.

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Strong Buy ("1"). The stock's total return is expected to exceed significantly the average total return of the analyst's industry coverage universe over the next 12 months.

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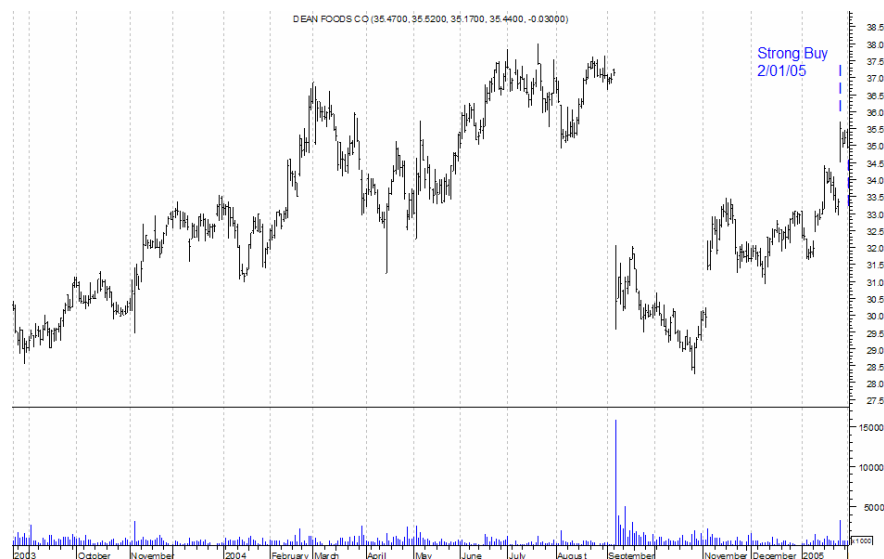
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