

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For Quarter Ended September 30, 1998
Commission file number 0-1375

FARMER BROS. CO.

California
State of Incorporation

95-0725980
Federal ID Number

20333 S. Normandie Avenue, Torrance, California
Registrant's Address

90502
Zip

(310) 787-5200
Registrant's telephone number

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 ☐

Number of shares of Common Stock outstanding: 1,926,414 as of September 30, 1998.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Dollars in thousands, except per share data)

FARMER BROS. CO.
CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	For the three months ended September 30,	
	1998	1997
Net sales	\$54,035	\$59,497
Cost of goods sold	22,920	30,171
	31,115	29,326
Selling expense	19,914	19,755
General and administrative expenses	1,880	1,919
	21,794	21,674
Income from operations	9,321	7,652
Other income:		
Dividend income	605	658
Interest income	2,239	1,842
Other, net	400	313
	3,244	2,813
Income before taxes	12,565	10,465

Income taxes	5,026	4,237
Net income	\$ 7,539	\$ 6,228
Net income per common share	\$3.91	\$3.23
Weighted average shares outstanding	1,926,414	1,926,414

The accompanying notes are an integral part of these financial statements.

FARMER BROS. CO.
CONSOLIDATED BALANCE SHEETS
(Unaudited)

	September 30, 1998	June 30, 1998
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 14,744	\$ 6,800
Short term investments	139,844	128,004
Accounts and notes receivable, net	18,048	18,006
Inventories	37,068	38,067
Income tax receivable	229	649
Deferred income taxes	2,776	2,776
Prepaid expenses and other	699	526
Total current assets	213,408	194,828
Property, plant and equipment, net	30,513	30,551
Notes receivable	3,988	3,988
Long term investments, net	45,466	55,801
Other assets	19,789	19,527
Deferred taxes	2,860	2,317
Total assets	\$316,024	\$307,012
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	\$ 4,608	\$ 5,605
Accrued payroll expenses	4,485	4,876
Other	10,384	5,678
Total current liabilities	19,477	16,159
Accrued postretirement benefits	16,349	15,941
Commitments and contingencies	-	-
Shareholders' equity:		
Common stock, \$1.00 par value, authorized 3,000,000 shares; issued and outstanding 1,926,414 shares	1,926	1,926
Additional paid-in capital	568	568
Retained earnings	277,586	271,395
Accumulated other comprehensive income	118	1,023
Total shareholders' equity	280,198	274,912
Total liabilities and shareholders' equity	\$316,024	\$307,012

The accompanying notes are an integral part of these financial statements.

FARMER BROS. CO.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	For the three months ended September 30,	
	1998	1997
Cash flows from operating activities:		
Net Income	\$ 7,539	\$ 6,228
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	1,403	1,347
Deferred income taxes	(23)	(24)
Net (gain) on investments	(285)	(167)
Changes in assets and liabilities:		
Accounts and notes receivable	(51)	(74)
Inventories	999	332
Income tax receivable	420	2,119
Prepaid expenses and other assets	(455)	(382)
Accounts payable	(997)	1,609
Accrued payroll expenses and other liabilities	4,315	2,083
Other long term liabilities	408	356
Total adjustments	5,734	7,199
Net cash provided by operating activities	\$ 13,273	\$ 13,427

The accompanying notes are an integral part of these financial statements.

FARMER BROS. CO
CONSOLIDATED STATEMENTS OF CASH FLOWS
(CONTINUED)
(Unaudited)

	For the three months ended September 30,	
	1998	1997
Net cash provided by operating activities:	\$ 13,273	\$ 13,427
Cash flows from investing activities:		
Purchases of property, plant and equipment	(1,350)	(339)
Proceeds from sales of property, plant and equipment	28	72
Purchases of investments	(161,413)	(83,646)
Proceeds from sales of investments	158,745	61,073
Notes issued	54	-
Notes repaid	63	10
Net cash used in investing activities	(3,981)	(22,830)
Cash flows from financing activities:		
Dividends paid	(1,348)	(1,156)
Net cash used in financing activities	(1,348)	(1,156)
Net increase (decrease) in cash and cash equivalents	7,944	(10,559)
Cash and cash equivalents at beginning of period	6,800	34,174
Cash and cash equivalents at end of quarter	\$ 14,744	\$ 23,615
Supplemental disclosure of cash flow information:		
Income tax payments	\$ 54	\$ 29

The accompanying notes are an integral part of these financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

A. Unaudited Financial Statements

The accompanying unaudited financial statements have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. It is Management's opinion that all adjustments of a normal recurring nature necessary for a fair presentation of the financial position of the Company and the results of operations and cash flows for the interim periods have been made.

B. Investments

The Company hedges interest rate risk in its portfolio of preferred stock. Deferred losses associated with the hedge are \$3,314,000 and \$2,600,000 at September 30 and June 30, 1998, respectively.

(In thousands)

	Cost	Gross Unrealized Loss	Gross Unrealized Gain	Fair Value
September 30, 1998				
Current Assets				
Commercial Paper	\$ 98,803	-	568	\$ 99,371
U.S. Government Obligations	40,473	(27)	27	\$ 40,473
	\$139,276	(27)	595	\$139,844
Non-Current Assets				
Municipal debt	\$ 1,695	(26)	-	\$ 1,669
Preferred stocks	36,412	(251)	3,299	39,460
Liquid asset fund and other	5,285	(1,000)	52	4,337
	\$43,392	(1,277)	3,351	\$45,466

(In thousands)

	Cost	Gross Unrealized Loss	Gross Unrealized Gain	Fair Value
June 30, 1998				
Current Assets				
Commercial Paper	\$ 95,838	-	594	\$ 96,432
U.S. Government Obligations	31,608	(36)	-	31,572
	\$127,446	(36)	594	\$128,004
Non-Current Assets				
U.S. Government Obligations	\$ 9,725	(151)	-	\$ 9,574
Municipal debt	1,695	(11)	-	1,684
Preferred stocks	36,504	(52)	3,978	40,430
Liquid asset fund and other	4,067	-	46	4,113
	\$ 51,991	(214)	4,024	\$ 55,801

B. Investments, CONTINUED

The contractual maturities of debt securities classified as current and non-current available for sale are as follows:

Maturities (In thousands)	Fair Value	
	09/30/98	06/30/98
Within 1 year	\$139,844	\$128,004
After 1 year through 5 years	1,669	11,258
	\$141,513	\$139,262

Gross realized gains from available for sale securities were \$830,000 and \$255,000 at September 30, 1998 and 1997, respectively.

C. Inventories (In thousands)

	Processed	Unprocessed	Total
September 30, 1998			
Coffee	\$ 3,244	\$10,642	\$13,886
Allied products	12,223	4,348	16,571
Coffee brewing equipment	1,982	4,629	6,611
	\$17,449	\$19,619	\$37,068
June 30, 1998			
Coffee	\$ 4,119	\$10,406	\$ 14,525
Allied products	12,025	5,079	17,104
Coffee brewing equipment	2,191	4,247	6,438
	\$18,335	\$19,732	\$ 38,067

D. Comprehensive Income

Effective July 1, 1998, the Company adopted Statement of Financial Accounting Standards (SFAS 130) "Reporting Comprehensive Income". SFAS 130 requires disclosure of total non-stockholder changes in equity in interim periods and additional disclosures of the components of non-stockholder changes in equity on an annual basis. Total non-stockholder changes in equity includes all changes in equity during a period except those resulting from investments by and distributions to shareholders.

(In thousands)	For the three months ended September 30,	
	1998	1997
Net income	\$7,539	\$6,228
Unrealized investment gains (losses), net	(905)	156
Total comprehensive income	\$6,634	\$6,384

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

Registrant's financial condition is substantially the same as at its most recent fiscal year end. The volatile market for green coffee always has an effect on operating results. The lower cost of green coffee in the current period has resulted in lower roast coffee prices. Gross profit margins in the current period have been consistent, but sales volume continues to decline. Registrant has been able to stabilize operating expenses.

Net sales for the first quarter of fiscal 1999 decreased 9% to \$54,035,000 from \$59,497,000 in the same quarter of fiscal 1998. Gross profit increased 6% during the first quarter of fiscal 1998 to \$31,115,000 or 58% of sales, as compared to \$29,326,000 or 49% of sales, in the same quarter of the prior fiscal year.

Operating expenses, composed of selling and general and administrative expenses, reached \$21,794,000 in the most recent quarter, compared to \$21,674,000 in the same quarter of fiscal 1998. Other income increased 15% to \$3,244,000 in the first quarter of fiscal 1999 as compared to \$2,813,000 in the same quarter of the prior fiscal year, primarily the result of higher interest income.

Income before taxes increased 20% to \$12,565,000 or 23% of sales, in the first quarter of the 1999 fiscal year as compared to \$10,465,000 or 18% of sales in the same quarter of fiscal 1998. Net income for the first quarter of fiscal 1999 increased 21% to \$7,539,000 or \$3.91 per common share, from \$6,228,000 or \$3.23 per common share, recorded in the first quarter of fiscal 1998.

Quarterly Summary of Results (In thousands of dollars)

	09/30/97	12/31/97	03/31/98	06/30/98	09/30/98
Net sales	59,497	64,062	58,951	57,582	54,035
Gross profit	29,326	36,161	32,249	34,388	31,115
Operating income	7,652	13,377	10,067	9,859	9,321
Net income	6,228	9,782	8,020	9,370	7,539

(As a percentage of sales)

	09/30/97	12/31/97	03/31/98	06/30/98	09/30/98
Net sales	100.00	100.00	100.00	100.00	100.00
Gross profit	49.29	56.45	54.70	59.72	57.58
Operating income	12.86	20.88	17.08	17.12	17.25
Net income	10.47	10.05	13.60	16.27	13.95

(In dollars)

	09/30/97	12/31/97	03/31/98	06/30/98	09/30/98
EPS	3.23	5.08	4.16	4.86	3.91

Year 2000 Issues

There have been no material changes from the fiscal year end.

Item 2a. Market Risk Disclosures

Financial Markets

Securities are recorded at fair value and unrealized gains or losses have been recorded as a separate component of shareholders equity. The Company maintains two distinct portfolios of securities, both portfolios are classified as available for sale.

The Company's portfolio of investment grade money market instruments includes bankers acceptances, discount commercial paper, federal agency issues and treasury securities. As of September 30, 1998, over 98% of these funds were invested in instruments with maturities shorter than one year. The remaining balance matures during fiscal 2000. This portfolio's interest rate risk is unhedged. Its average maturity is approximately 90 days and a 100 basis point move in the Fed Funds Rate would not have a material effect on Registrant's results of operations.

The Company is exposed to market value risk arising from changes in interest rates on its portfolio of preferred securities. The Company reviews the interest rate sensitivity of these securities and (a) enters into "short positions" in futures contracts on U.S. Treasury securities or (b) holds put options on such futures contracts in order to reduce the impact of certain interest rate changes on such preferred stocks.

Specifically, the Company attempts to manage the risk arising from changes in the general level of interest rates. The Company does not transact in futures contracts or put options for speculative purposes.

The following table demonstrates the impact of varying interest rate changes based on the preferred stock holdings, futures and options positions, and market yield and price relationships at September 30, 1998. This table is predicated on an instantaneous change in the general level of interest rates and assumes predictable relationships between the prices of preferred securities holdings, the yields on U.S. Treasury securities, and related futures and options.

Interest Rate Changes
(In thousands)

	Market Value of Preferred Securities	Value of Futures and Options	Total Portfolio	Change in Market Value of Total Portfolio
- -200 basis points ("b.p.")	\$47,617.7	\$ 0.0	\$47,617.7	\$ 4,534.5
- -100 b.p.	45,448.5	0.4	45,448.9	2,365.7
Unchanged	42,890.0	193.2	43,083.2	-
+100 b.p.	39,906.6	2,212.4	42,119.0	(964.2)
+200 b.p.	36,829.0	5,121.7	41,950.7	(1,132.5)

The number and type of futures and options contracts entered into depends on, among other items, the specific maturity and issuer redemption provisions for each preferred security held, the slope of the Treasury yield curve, the expected volatility of Treasury yields, and the costs of using futures and/or options. At September 30, 1998 and 1997 the hedge consisted entirely of put options on the U.S. Treasury Bond futures contract.

Item 2a. Market Risk Disclosures, (CONTINUED)

Commodity Price Changes

The Company is exposed to commodity price risk arising from changes in the market price of green coffee. Registrant prices its inventory on the LIFO basis. In the normal course of business, the Company enters into commodity purchase agreements with suppliers, and futures contracts to hedge exposure to inventory price fluctuations. The Company does not transact in futures contracts or put options for speculative purposes.

The following table demonstrates the impact of changes in the price of green coffee on inventory and hedge instruments at September 30, 1998. It assumes an immediate change in the price of green coffee, and the demonstrable relationship between the price of green coffee and the valuations of coffee index futures and put options and relevant commodity purchase agreements at September 30, 1998.

Commodity Risk Disclosure
(In thousands)

		September 30, 1998		
Coffee Cost	Coffee	Market Value of		Change in
Change	Inventory	Futures	Total	Market
		& Options		Value
- - 20%	\$13,886	\$ 748	\$14,634	\$ 554
unchanged	13,886	194	14,080	-
+ 20%	13,886	(360)	13,526	(554)

At September 30, 1998 the hedge consisted mainly of commodity futures and commodity purchase agreements with maturities shorter than three months.

PART II OTHER INFORMATION

Item 1. Legal proceedings. not applicable.

Item 2. Changes in securities. none.

Item 3. Defaults upon senior securities. none.

Item 4. Submission of matters to a vote of security holders. none.

Item 5. Other information. none.

Item 6. Exhibits and reports on Form 8-K.

(a) Exhibits.

(2) Plan of acquisition, reorganization, arrangement, liquidation or succession not applicable.

(4) Instruments defining the rights of security holders, including indentures. not applicable.

PART II OTHER INFORMATION (CONTINUED)

- | | |
|--|--------------------------|
| (11) Statement re computation of per share earnings. | not applicable. |
| (15) Letter re unaudited interim financial information. | not applicable. |
| (18) Letter re change in accounting principles. | not applicable. |
| (19) Report furnished to security holders | not applicable. |
| (22) Published report regarding matters submitted to vote of security holders. | not applicable. |
| (23) Consents of experts and counsel. | not applicable. |
| (24) Power of attorney. | not applicable. |
| (27) Financial Data Schedule | See attached Form EX-27. |
| (99) Additional exhibits. | not applicable. |
- (b) Reports on Form 8-K
Registrant filed a report reporting a change in accountant. April 14, 1997.

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: November 13, 1998

FARMER BROS. CO.
(Registrant)

John E. Simmons

John E. Simmons
Treasurer and
Chief Financial Officer

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