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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended: June 30, 2019

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

For the transition period from __________ to __________

Commission File Number: 000-17363

LIFEWAY FOODS, INC.
(Exact Name of Registrant as Specified in its Charter)

Illinois	**36-3442829**
(State or Other Jurisdiction of Incorporation or Organization)	*(I.R.S. Employer Identification No.)*

6431 West Oakton, Morton Grove, IL 60053
(Address of Principal Executive Offices, Zip Code)

(847) 967-1010
(Registrant's Telephone Number, Including Area Code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, no par value	**LWAY**	**Nasdaq Global Market**

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 ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data file required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ☒ No ☐

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

Large accelerated filer ☐	Accelerated filer ☐
Non-accelerated filer ☐	Smaller reporting company ☒
Emerging growth company ☐	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

Number of shares of Common Stock, no par value, outstanding as of August 6, 2019: 15,761,440

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PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
June 30, 2019 and December 31, 2018
(In thousands)

	June 30, 2019 (Unaudited)	December 31, 2018
Current assets		
Cash and cash equivalents	$ 3,022	$ 2,998
Accounts receivable, net of allowance for doubtful accounts and discounts & allowances of $1,220 at June 30, 2019 and December 31, 2018 respectively	7,570	6,276
Inventories, net	6,843	5,817
Prepaid expenses and other current assets	1,393	1,077
Refundable income taxes	1,278	2,748
Total current assets	**20,106**	**18,916**
Property, plant and equipment, net	**23,365**	**24,573**
Operating lease right-of-use asset	**966**	–
Intangible assets		
Goodwill & indefinite-lived intangibles	12,824	12,824
Other intangible assets, net	231	344
Total intangible assets	**13,055**	**13,168**
Other assets	**165**	150
Total assets	**$ 57,657**	**$ 56,807**
Current liabilities		
Accounts payable	$ 5,459	$ 4,570
Accrued expenses	4,141	2,777
Accrued income taxes	63	106
Total current liabilities	**9,663**	**7,453**
Line of credit	**4,677**	**5,995**
Operating lease liabilities	**584**	–
Deferred income taxes, net	**390**	**390**
Other long-term liabilities	**100**	**564**
Total liabilities	**15,414**	**14,402**
Stockholders' equity		
Preferred stock, no par value; 2,500 shares authorized; no shares issued or outstanding at June 30, 2019 and December 31, 2018, respectively	–	–
Common stock, no par value; 40,000 shares authorized; 17,274 shares issued; 15,761 and 15,814 outstanding at June 30, 2019 and December 31, 2018, respectively	6,509	6,509
Paid-in capital	2,230	2,303
Treasury stock, at cost	(12,477)	(12,970)
Retained earnings	45,981	46,563
Total stockholders' equity	**42,243**	**42,405**
Total liabilities and stockholders' equity	**$ 57,657**	**$ 56,807**

See accompanying notes to consolidated financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
For the six months ended June 30, 2019 and 2018
(Unaudited)
(In thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2019	**2018**	**2019**	**2018**
Net sales	**$ 23,153**	**$ 27,096**	**$ 47,768**	**$ 55,838**
Cost of goods sold	16,843	19,495	34,410	39,520
Depreciation expense	747	725	1,492	1,405
Total cost of goods sold	17,590	20,220	35,902	40,925
Gross profit	**5,563**	**6,876**	**11,866**	**14,913**
Selling expenses	2,691	3,383	5,830	7,401
General and administrative	2,898	2,996	6,390	6,701
Amortization expense	40	164	113	327
Total operating expenses	**5,629**	**6,543**	**12,333**	**14,429**
(Loss) income from operations	**(66)**	**333**	**(467)**	**484**
Other income (expense):				
Interest expense	(68)	(75)	(137)	(138)
Gain (loss) on sale of property and equipment	4	(1)	29	14
Other income, net	2	3	5	8
Total other income (expense)	(62)	(73)	(103)	(116)
(Loss) income before provision for income taxes	**(128)**	**260**	**(570)**	**368**
Provision for income taxes (benefit)	13	90	(41)	128
Net (loss) income	**$ (141)**	**$ 170**	**$ (529)**	**$ 240**
Earnings (loss) per common share:				
Basic	$ (0.01)	$ 0.01	$ (0.03)	$ 0.02
Diluted	$ (0.01)	$ 0.01	$ (0.03)	$ 0.02
Weighted average common shares:				
Basic	15,775	15,879	15,771	15,893
Diluted	15,775	15,992	15,771	16,026

See accompanying notes to consolidated financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Stockholders' Equity
For the Six Months Ended June 30, 2019 and 2018
(Unaudited)
(In thousands)

	Common Stock						
	Issued		In treasury				
	Shares	$	Shares	$	Paid-In Capital	Retained Earnings	Total Equity
Balance, January 1, 2018	**17,274**	**$ 6,509**	**(1,266)**	**$ (11,812)**	**$ 2,244**	**$ 49,649**	**$ 46,590**
Issuance of common stock in connection with stock-based compensation	–	–	22	203	(71)	–	132
Treasury stock purchased	–	–	(151)	(1,168)	–	–	(1,168)
Stock-based compensation	–	–	–	–	11	–	11
Net income	–	–	–	–	–	240	240
Balance, June 30, 2018	**17,274**	**$ 6,509**	**(1,395)**	**$ (12,777)**	**$ 2,184**	**$ 49,889**	**$ 45,805**
Balance, January 1, 2019	**17,274**	**$ 6,509**	**(1,460)**	**$ (12,970)**	**$ 2,303**	**$ 46,563**	**$ 42,405**
Cumulative impact of change in accounting principles, net of tax	–	–	–	–	–	(53)	(53)
Issuance of common stock in connection with stock-based compensation	–	–	103	878	(406)	–	472
Treasury stock purchased	–	–	(156)	(385)	–	–	(385)
Stock-based compensation	–	–	–	–	333	–	333
Net loss	–	–	–	–	–	(529)	(529)
Balance, June 30, 2019	**17,274**	**$ 6,509**	**(1,513)**	**$ (12,477)**	**$ 2,230**	**$ 45,981**	**$ 42,243**

See accompanying notes to consolidated financial statements

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Six Months Ended June 30, 2019 and 2018
(Unaudited)
(In thousands)

	2019	2018
Cash flows from operating activities:		
Net (loss) income	**$ (529)**	**$ 240**
Adjustments to reconcile net (loss) income to operating cash flow:		
Depreciation and amortization	1,605	1,732
Bad debt expense	3	20
Reserve for inventory obsolescence	210	271
Stock-based compensation	535	495
Non-cash interest expense	12	3
Deferred revenue	(48)	(48)
(Gain) on sale of property and equipment	(29)	(14)
(Increase) decrease in operating assets:		
Accounts receivable	(1,297)	66
Inventories	(1,235)	243
Refundable income taxes	1,470	(463)
Prepaid expenses and other current assets	(308)	(584)
Increase (decrease) in operating liabilities:		
Accounts payable	888	423
Accrued expenses	774	(153)
Accrued income taxes	(43)	(121)
Net cash provided by operating activities	**2,008**	**2,109**
Cash flows from investing activities:		
Purchases of property and equipment	(290)	(2,024)
Proceeds from sale of property and equipment	36	35
Purchase of investments	(15)	–
Net cash used in investing activities	**(269)**	**(1,989)**
Cash flows from financing activities:		
Purchase of treasury stock	(385)	(1,168)
Borrowings under revolving credit facility	–	6,050
Repayment of line of credit	(1,330)	–
Payment of deferred financing costs	–	(69)
Repayment of notes payable	–	(6,279)
Net cash used in financing activities	**(1,715)**	**(1,466)**
Net decrease in cash and cash equivalents	**24**	**(1,346)**
Cash and cash equivalents at the beginning of the period	2,998	4,978
Cash and cash equivalents at the end of the period	**$ 3,022**	**$ 3,632**
Supplemental cash flow information:		
Cash paid for income taxes, net of (refunds)	$ (1,469)	$ 712
Cash paid for interest	$ 149	$ 108
Non-cash investing activities		
Right-of-use assets recognized at ASU 2016-02 transition	$ 944	$ –
Operating lease liability recognized at ASU 2016-02 transition	$ 997	$ –
Right-of-use assets and operating lease liabilities recognized after ASU 2016-02 transition	$ 280	$ –

See accompanying notes to consolidated financial statements

Note 1 – Basis of Presentation

Basis of presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the U.S. ("U.S. GAAP") for interim financial information, and do not include all of the information and disclosures required for complete, audited financial statements. In the opinion of management, these statements include all adjustments necessary for a fair presentation of the results of all interim periods reported herein. The consolidated financial statements and related notes should be read in conjunction with the consolidated financial statements and related notes included in our Annual Report on Form 10-K as of and for the year ended December 31, 2018. Results of operations for interim periods are not necessarily indicative of the results to be expected for other interim periods or the full year.

A detailed description of our significant accounting policies can be found in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018.

Principles of consolidation

Our consolidated financial statements include the accounts of Lifeway Foods, Inc. and all its wholly owned subsidiaries (collectively "Lifeway" or the "Company"). All significant intercompany accounts and transactions have been eliminated.

Note 2 – Significant Accounting Policies

Use of estimates

The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Significant estimates made in preparing the consolidated financial statements include the reserve for promotional allowances, the valuation of goodwill and intangible assets, stock-based and incentive compensation, and deferred income taxes.

Revenue Recognition

We sell food and beverage products across select product categories to customers predominantly within the United States (see Note 12, Segments, Products and Customers). We also sell bulk cream, a byproduct of our fluid milk manufacturing process. In accordance with Accounting Standards Codification ("ASC") 606, Revenue from Contracts with Customers, we recognize revenue when control over the products transfers to our customers, which generally occurs upon delivery to our customers or their common carriers. We adopted this standard at the beginning of fiscal year 2018, with no significant impact to our financial position or results of operations, using the modified retrospective method. The amount of revenue recognized reflects the consideration to which we expect to be entitled to receive in exchange for these goods or services, using the five-step method required by ASC 606.

For the Company, the contract is the approved sales order, which may also be supplemented by other agreements that formalize various terms and conditions with customers. We apply judgment in determining the customer's ability and intention to pay, which is based on a variety of factors including the customer's historical payment experience or, in the case of a new customer, published credit and financial information pertaining to the customer.

Performance obligations promised in a contract are identified based on the goods or services that will be transferred to the customer, which is the delivery of food products which provide immediate benefit to the customer.

We account for product shipping and handling as fulfillment activities with revenues for these activities recorded within net revenue and costs recorded within cost of goods sold. Any taxes collected on behalf of government authorities are excluded from net revenues.

Variable consideration, which typically includes volume-based rebates, known or expected pricing or revenue adjustments, such as trade discounts, allowances for non-saleable products, product returns, trade incentives and coupon redemption, is estimated utilizing the most likely amount method.

Key sales terms, such as pricing and quantities ordered, are established on a frequent basis such that most customer arrangements and related incentives have a one year or shorter duration. As such, we do not capitalize contract inception costs. We do not have any significant deferred revenue or unbilled receivables at the end of a period. We generally do not receive noncash consideration for the sale of goods, nor do we grant payment financing terms greater than one year.

Advertising and promotional costs

Lifeway expenses advertising costs as incurred. For the six months ended June 30, 2019 and 2018 total advertising expenses were $1,864 and $2,585 respectively. For the three months ended June 30, 2019 and 2018 total advertising expenses were $776 and $1,196 respectively.

Recently Adopted Accounting Pronouncements

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which affects any entity that enters into a lease (as that term is defined in ASU 2016-02), with some specified scope exceptions. Under ASU 2016-02, companies can adopt the amended guidance using a modified retrospective transition approach, using an application date of either the beginning of the earliest comparative period presented or the beginning of the reporting period in which the companies first apply the new standard. We adopted this standard on January 1, 2019 using the application date of January 1, 2019, and elected certain practical expedients allowed under the standard. In July 2018, the FASB issued ASU No. 2018-11, Leases (842), Targeted Improvements, which provides an additional transition election to not restate comparative periods for the effects of applying the new standard. The guidance requires lessees to recognize right-of-use assets and lease liabilities in the balance sheet and disclose key information about leasing arrangements, such as information about variable lease payments and options to renew and terminate leases. The amended guidance will require both operating and finance leases to be recognized in the balance sheet. A lessee should recognize in the statement of financial position a liability to make lease payments (the lease liability) and a right-of-use asset representing its right to use the underlying asset for the lease term.

Lifeway elected certain of the practical expedients that are permitted under the transition guidance within ASU 2016-02 and related standards. Among other things, this practical expedient allowed us to carryforward the historical lease classification, and not reassess initial direct costs for any existing leases as of January 1, 2019 or reassess whether any expired or existing contracts are or contain leases. In addition, we elected to adopt the hindsight practical expedient to determine the reasonably certain lease term for existing leases. We made an accounting policy election to continue recording leases with an initial term of 12 months or less consistent with our prior financial reporting and elect the practical expedient to combine lease and non-lease components. We have revised our relevant policies and procedures, as applicable, to meet the new accounting, reporting and disclosure requirements of Topic 842 and have updated internal controls accordingly.

The main difference between the guidance in ASU 2016-02 and prior GAAP is the recognition of right-of-use assets and lease liabilities by lessees for those leases classified as operating leases under current GAAP. Recognition of the right-of-use assets and liabilities had a material impact to our consolidated balance sheets upon adoption. However, since all our leases are operating leases under ASC 840 and we will carryforward the historical lease classification, the new standard did not have a material impact on our Consolidated Statements of Operations, Consolidated Statements of Stockholders' Equity, or Consolidated Statements of Cash Flows. The adoption resulted in an increase of the right-of-use assets of approximately $944 and lease liabilities of $997, and an adjustment to beginning retained earnings of $53 as of January 1, 2019.

Recently Issued Accounting Pronouncements

We do not anticipate a material impact upon adoption from any accounting standards issued but not yet adopted.

Note 3 – Inventories, net

Inventories consisted of the following:

	June 30, 2019	December 31, 2018
Ingredients	$ 1,915	$ 1,580
Packaging	2,240	2,072
Finished goods	2,688	2,165
Total inventories	$ 6,843	$ 5,817

Note 4 – Property, Plant and Equipment, net

Property, plant and equipment consisted of the following:

	June 30, 2019	December 31, 2018
Land	$ 1,747	$ 1,747
Buildings and improvements	17,566	17,520
Machinery and equipment	29,830	29,692
Vehicles	806	937
Office equipment	850	838
Construction in process	583	546
	51,382	51,280
Less accumulated depreciation	(28,017)	(26,707)
Total property, plant and equipment, net	$ 23,365	$ 24,573

Note 5 – Goodwill and Intangible Assets

Goodwill & indefinite-lived intangible assets consisted of the following:

	June 30, 2019	December 31, 2018
Gross goodwill	$ 10,368	$ 10,368
Accumulated impairment losses	(1,244)	(1,244)
Goodwill	9,124	9,124
Brand names	3,700	3,700
Goodwill and indefinite-lived intangible assets	$ 12,824	$ 12,824

Finite-lived Intangible Assets

Other intangible assets, net consisted of the following:

	June 30, 2019	December 31, 2018
Recipes	$ 44	$ 44
Customer lists and other customer related intangibles	4,529	4,529
Customer relationship	985	985
Trade names	2,248	2,248
Formula	438	438
	8,244	8,244
Accumulated amortization	(8,013)	(7,900)
Other intangible assets, net	$ 231	$ 344

Note 6 – Accrued Expenses

Accrued expenses consisted of the following:

	June 30, 2019	December 31, 2018
Payroll and incentive compensation	$ 2,830	$ 1,937
Operating leases	429	–
Real estate taxes	365	398
Other	517	442
Total accrued expenses	$ 4,141	$ 2,777

Note 7 – Debt

Notes Payable

We had two variable rate term loans with an aggregate outstanding balance of $6,069 as of March 31, 2018. The term loans were subject to interest at the prime rate or at the LIBOR plus 2.5% and were collateralized by substantially all of Lifeway's assets. The two term loans were refinanced and paid in full on May 7, 2018. See Line of Credit below.

Line of Credit

On May 7, 2018, Lifeway entered into an Amended and Restated Loan and Security Agreement (the "Revolving Credit Facility") with its existing lender. The Revolving Credit Facility provides for a revolving line of credit up to a maximum of $10 million (the "Revolving Loan") with an incremental facility not to exceed $5 million (the "Incremental Facility" and together with the Revolving Loan, the "Loans"). The proceeds of the Loans were used to pay off Lifeway's existing debt with the lender under the Loan and Security Agreement, Revolving Note, and Term Note entered into on February 6, 2009, and for general working capital purposes. Upon closing, we retired all the then-outstanding term loans described above.

As of June 30, 2019, we had $4,677, net of $43 of unamortized deferred financing costs, outstanding under the Revolving Credit Facility. We had approximately $4,280 available under the Borrowing Base for future borrowings as of June 30, 2019.

All outstanding amounts under the Loans bear interest, at Lifeway's election, at either the lender Base Rate (the greater of either the Federal Funds Rate plus 0.5%, or the Prime Rate) or the LIBOR plus 2.50%, payable monthly in arrears. Lifeway is also required to pay a quarterly unused line fee and, in conjunction with the issuance of any letters of credit, a letter of credit fee. Lifeway's average interest rate on debt outstanding under our Revolving Credit Facility for the quarter ended June 30, 2019 was 5.04%.

The commitment under the Revolving Credit Facility matures May 7, 2021. The Revolving Credit Facility is presented as a long-term debt obligation as of June 30, 2019. The Loans and all other amounts due and owed under the Revolving Credit Facility and related documents are secured by substantially all of our assets.

Amounts available for borrowing under the Revolving Credit Facility equal the lesser of (i) the Borrowing Base (as defined below), or (ii) $10 million (plus the amount of any Incremental Facility requested by Lifeway and approved by lender), in each case, as the same is reduced by the aggregate principal amount outstanding under the Loans. "Borrowing Base" under the Revolving Credit Facility means, generally, an amount equal to our cash and cash equivalents plus our eligible accounts receivable and eligible inventory, less certain reserves, divided by 1.5.

The Revolving Credit Facility contains customary representations, warranties, and covenants on the part of Lifeway, including financial covenants requiring us to achieve a minimum EBITDA threshold for each of the fiscal quarters through December 31, 2018; maintain (a) a fixed charge coverage ratio of no less than 1.25 to 1.0, and (b) a Senior Debt to EBITDA ratio of not more than 3.00 to 1.0 at December 31, 2018 and for each of the succeeding fiscal quarters ending through the expiration date. The Revolving Credit Facility also provides for events of default, including failure to repay principal and interest when due and failure to perform or violation of the provisions or covenants of the agreement, as a result of which amounts due under the Revolving Credit Facility may be accelerated.

On April 10, 2019, effective March 31, 2019, Lifeway entered into the First Modification to the Amended and Restated Loan and Security Agreement (the "Modified Revolving Credit Facility") with its existing lender. Under the amendment, the Modified Revolving Credit Facility provides for a revolving line of credit up to a maximum of $9 million (the "Revolving Loan") with an incremental facility not to exceed $5 million (the "Incremental Facility" and together with the Revolving Loan, the "Loans").

All outstanding amounts under the Loans bear interest, based on a level of the Senior Debt to EBITDA ratio, at Lifeway's election, at either the lender Base Rate (the greater of either the Federal Funds Rate plus 0.0% to 0.5%, or the Prime Rate) or the LIBOR plus 2.25% to 3.00%, payable monthly in arrears. Lifeway is also required to pay a quarterly unused line fee and, in conjunction with the issuance of any letters of credit, a letter of credit fee.

As amended, the Modified Revolving Credit Facility contains customary representations, warranties, and covenants on the part of Lifeway, including financial covenants requiring us to achieve a minimum EBITDA threshold for each of the fiscal quarters through December 31, 2019, and maintain a fixed charge coverage ratio of no less than 1.25 to 1.00 for each of the fiscal quarters ending through the expiration date. The Modified Revolving Credit Facility also provides for events of default, including failure to repay principal and interest when due and failure to perform or violation of the provisions or covenants of the agreement, as a result of which amounts due under the Modified Revolving Credit Facility may be accelerated.

We were in compliance with the minimum EBITDA and fixed charge coverage ratio covenants at June 30, 2019.

Note 8 – Leases

Lifeway has operating leases for three retail stores for its Lifeway Kefir Shop subsidiary, certain machinery and equipment, and office space. All lease payments are fixed, not variable. Remaining lease terms for these leases range from less than 1 year to 5 years. Some of our leases include options to extend the leases for up to 5 years and have been included in our calculation of the right-of-use asset and lease liabilities. There are no residual value guarantees. We do not currently have leases which meet the finance lease classification as defined under ASC 842.

We do not record leases with an initial term of 12 months or less on the balance sheet. Expense for these short-term leases is recorded on a straight-line basis over the lease term. Total lease expense was $365 and $375 (including short term leases) for the six months ended June 30, 2019 and 2018, respectively. Total lease expense was $194 and $195 (including short term leases) for the three months ended June 30, 2019 and 2018, respectively.

Lifeway treats contracts as a lease when the contract conveys the right to use a physically distinct asset for a period of time in exchange for consideration, we direct the use of the asset and obtain substantially all the economic benefits of the asset.

Right-of-use assets and lease liabilities are measured and recognized based on the present value of the future minimum lease payments over the lease term at the commencement date. We have elected the practical expedient to combine lease and non-lease components into a single component for all of its leases. For many of our leases such as real estate leases, we are unable to determine an implicit rate; therefore, we use our incremental borrowing rate based on the information available at the commencement date in determining the present value of future payments for those leases. We include options to extend or terminate the lease in the measurement of the right-of-use asset and lease liability when it is reasonably certain that we will exercise such options. Lease expense for minimum lease payments is recognized on a straight-line basis over the lease term.

Future maturities of lease liabilities were as follows

Year	Operating Leases
Six months ended December 31, 2019	$ 289
2020	303
2021	227
2022	190
2023	71
Thereafter	7
Total lease payments	1,087
Less: Interest	(74)
Present value of lease liabilities	$ 1,013

The weighted-average remaining lease term for our operating leases was 2.9 years as of June 30, 2019. The weighted average discount rate of our operating leases was 5.33% as of June 30, 2019. Cash paid for amounts included in the measurement of lease liabilities was $292 for the six months ended June 30, 2019. Cash paid for amounts included in the measurement of lease liabilities was $145 for the three months ended June 30, 2019.

Note 9 – Commitments and contingencies

Litigation

Lifeway is engaged in various legal actions, claims, and proceedings arising in the normal course of business, including commercial disputes, product liabilities, intellectual property matters and employment-related matters resulting from our business activities.

We record accruals for outstanding legal matters when we believe it is probable that a loss will be incurred and the amount of such loss can be reasonably estimated. We evaluate, on a periodic basis, developments in legal matters that could affect the amount of any accrual and developments that would make a loss contingency both probable and reasonably estimable. If a loss contingency is not both probable and estimable, we do not establish an accrued liability. Currently, none of our accruals for outstanding legal matters are material individually or in the aggregate to our financial position and it is management's opinion that the ultimate resolution of these outstanding legal matters will not have a material adverse effect on our business, financial condition, results of operations, or cash flows. However, if we ultimately are required to make payments in connection with an adverse outcome, it is possible that it could have a material adverse effect on our business, financial condition, results of operations or cash flows.

Lifeway's contingencies are subject to substantial uncertainties, including for each such contingency the following, among other factors: (i) the procedural status of the case; (ii) whether the case has or may be certified as a class action suit; (iii) the outcome of preliminary motions; (iv) the impact of discovery; (v) whether there are significant factual issues to be determined or resolved; (vi) whether the proceedings involve a large number of parties and/or parties and claims in multiple jurisdictions or jurisdictions in which the relevant laws are complex or unclear; (vii) the extent of potential damages, which are often unspecified or indeterminate; and (viii) the status of settlement discussions, if any, and the settlement posture of the parties. Consequently, Lifeway cannot predict with any reasonable certainty the timing or outcome of such contingencies, and we are unable to estimate a possible loss or range of loss.

Note 10 – Income taxes

For each interim period, Lifeway estimates the effective tax rate ("ETR") expected to be applicable for the full year and applies that rate to income before provision for income taxes for the period. The effective tax rate for the six months ended June 30, 2019 was (7.2%) compared to 34.8% for the six months ended June 30, 2018. The effective tax rate for the three months ended June 30, 2019 was 9.9% compared to 34.6% for the three months ended June 30, 2018. Our effective tax rate may change from period to period based on recurring and non-recurring factors including the relative mix of pre-tax earnings (or losses), the underlying income tax rates applicable to various state and local taxing jurisdictions, settlement of tax audits, the impact of non-deductible items, changes in valuation allowances, and the expiration of the statute of limitations in relation to unrecognized tax benefits. We record discrete income tax items such as enacted tax rate changes and completed tax audits in the period in which they occur.

Note 11 – Stock-based and Other Compensation

In December 2015, Lifeway stockholders approved the 2015 Omnibus Incentive Plan, which authorized the issuance of an aggregate of 3.5 million shares to satisfy awards of stock options, stock appreciation rights, unrestricted stock, restricted stock, restricted stock units, performance shares and performance units to qualifying employees. Under the Plan, the Board or its Audit and Corporate Governance Committee approves stock awards to executive officers and certain senior executives, generally in the form of restricted stock or performance shares. The number of performance shares that participants may earn depends on the extent to which the corresponding performance goals have been achieved. Stock awards generally vest over a three-year performance or service period. At June 30, 2019, 3.381 million shares remain available under the Omnibus Incentive Plan. While we plan to continue to issue awards pursuant to the Plan at least annually, we may choose to suspend the issuance of new awards in the future and may grant additional awards at any time including issuing special grants of restricted stock, restricted stock units, and stock options to attract and retain new and existing executives.

Stock Options

The following table summarizes stock option activity during the six months ended June 30, 2019:

	Options	Weighted average exercise price	Weighted average remaining contractual life	Aggregate intrinsic value
Outstanding at December 31, 2018	41	$ 10.42	7.22	–
Granted	–	$ –		
Exercised	–	$ –		
Forfeited	–	$ –		
Outstanding at June 30, 2019	41	$ 10.42	6.72	$ –
Exercisable at June 30, 2019	39	$ 10.46	6.72	$ –

For the six months ended June 30, 2019 and 2018 total pre-tax stock-based compensation expense recognized in the consolidated statements of operations was $1 and $7, respectively. For the six months ended June 30, 2019 and 2018 tax-related benefits of $0 and $2 were also recognized. For the three months ended June 30, 2019 and 2018 total pre-tax stock-based compensation expense recognized in the consolidated statements of operations was $0 and $3, respectively. For the three months ended June 30, 2019 and 2018 tax-related benefits of $0 were also recognized. As of June 30, 2019, there is no remaining unearned compensation expense related to non-vested stock options.

Restricted Stock Awards

A Restricted Stock Award ("RSA") represents the right to receive one share of common stock in the future. RSAs have no exercise price. The grant date fair value of the awards is equal to our closing stock price on the grant date. The following table summarizes RSA activity during the six months ended June 30, 2019.

		RSA's
Outstanding at December 31, 2018		25
Granted		7
Shares issued upon vesting		–
Forfeited		–
Outstanding at June 30, 2019		32
Weighted average grant date fair value per share outstanding	$	4.19

We expense RSA's over the service period. For the six months ended June 30, 2019 and 2018 total pre-tax stock-based compensation expense recognized in the consolidated statements of operations was $52 and $4, respectively. For the six months ended June 30, 2019 and 2018 tax-related benefits of $14 and $1, respectively, were also recognized. For the three months ended June 30, 2019 and 2018 total pre-tax stock-based compensation expense recognized in the consolidated statements of operations was $27 and $3, respectively. For the three months ended June 30, 2019 and 2018 tax-related benefits of $7 and $1, respectively, were also recognized. As of June, 2019, the total remaining unearned compensation related to non-vested RSA's was $164, which is expected to be amortized over the weighted-average remaining service period of 1.40 years.

Long-Term Incentive Plan Compensation

Lifeway established long-term incentive-based compensation programs for fiscal year 2017 (the "2017 Plan"), fiscal year 2018 (the "2018 Plan"), and for fiscal year 2019 (the "2019 Plan") for certain senior executives and key employees (the "participants"). Under both the 2017 Plan and the 2018 Plan, long-term incentive compensation is based on Lifeway's achievement of certain sales and adjusted EBITDA performance levels versus respective targets established by the Board for each fiscal year. Under the 2019 Plan, long-term equity incentive compensation is based on Lifeway's achievement of four strategic milestones over a three-year period from Fiscal 2019 through Fiscal 2021.

2017 Plan

Under the 2017 Plan, collectively the participants had the opportunity to earn cash and equity-based incentive compensation in amounts ranging from $0 to $11,025 depending on Lifeway's performance levels compared to the respective targets and the participants performance compared to their individual objectives. The equity portion of the incentive compensation is payable in restricted stock that vests one-third in each of the three years from the 2017 grant dates. For the six months ended June 30, 2019 and 2018, $180 and $412 was expensed under the 2017 Plan as stock-based compensation expense in the consolidated statements of operations, respectively. For the three months ended June 30, 2019 and 2018, $53 and $126 was expensed under the 2017 Plan as stock-based compensation expense in the consolidated statements of operations, respectively. As of June 30, 2019, the total remaining unearned compensation related to the 2017 Plan was $156, of which $107 and $49 is expected to be recognized in 2019 and 2020, respectively, subject to vesting.

2018 Plan

Under the 2018 Plan, collectively the participants had the opportunity to earn cash and equity-based incentive compensation in amounts ranging from $0 to $11,200 depending on Lifeway's performance levels compared to the respective targets and the participants performance compared to their individual objectives. The equity portion of the incentive compensation was payable in restricted stock that vests one-third in each of the three years from the 2018 grant dates. For the six months ended June 30, 2018, $146 was expensed under the 2018 Plan, of which $76 was recorded as cash bonus expense and $70 was recorded as stock-based compensation expense in the consolidated statements of operations. For the three months ended June 30, 2018, $(25) was expensed under the 2018 Plan as stock-based compensation expense in the consolidated statements of operations. Due to the final fiscal 2018 financial results, there were no equity-based incentives awarded under the 2018 Plan.

2019 Plan

Under the 2019 Plan, collectively the participants have the opportunity to earn equity-based incentive compensation in amounts ranging from $0 to $1,776 depending on Lifeway's performance levels compared to the respective targets. The equity-based incentive compensation is payable in restricted stock that vests 50% of unvested shares in year one, 50% of unvested shares in year two, and 100% of remaining unvested shares in year three from the 2019 grant date. For the six months ended June 30, 2019, $68 was expensed under the 2019 Plan as stock-based compensation expense in the consolidated statements of operations. For the three months ended June 30, 2019, $33 was expensed under the 2019 Plan as stock-based compensation expense in the consolidated statements of operations.

2019 Retention Award

During Q1 2019, we awarded a special retention grant (the "2019 Retention Award") of restricted stock to senior executives and key employees (the "participants"). The equity-based incentive compensation is payable in restricted stock that vests one-third in March 2019, one-third in March 2020 and 2021. For the six months ended June 30, 2019, $211 was expensed under the 2019 Retention Award as stock-based compensation expense in the consolidated statements of operations. For the three months ended June 30, 2019, $54 was expensed under the 2019 Retention Award as stock-based compensation expense in the consolidated statements of operations.

Retirement Benefits

Lifeway has a defined contribution plan which is available to substantially all full-time employees. Under the terms of the plan, we match employee contributions under a prescribed formula. For the six months ended June 30, 2019 and 2018 total contribution expense recognized in the consolidated statements of operations was $181 and $229, respectively. For the three months ended June 30, 2019 and 2018 total contribution expense recognized in the consolidated statements of operations was $85 and $97, respectively.

Note 12 – Segments, Products and Customers

Lifeway's primary product is drinkable kefir, a cultured dairy product. Lifeway Kefir is tart and tangy, high in protein, calcium and vitamin D. Thanks to our exclusive blend of kefir cultures, each cup of kefir contains 12 live and active cultures and 15 to 20 billion beneficial CFU (Colony Forming Units) at the time of manufacture.

We manufacture (directly or through co-packers) our products under our own brand, as well as under private labels on behalf of certain customers. Lifeway offers approximately 20 varieties of our kefir products including more than 60 flavors. In addition to our core drinkable kefir products, we offer several lines of products developed through our innovation and development efforts. These include Kefir Cups, a strained, cupped version of our kefir; and Organic Farmer Cheese Cups, a cupped version of our soft cheeses, both served in resealable 5 oz. containers. We also offer Skyr, a strained cupped Icelandic yogurt; Plantiful, a plant-based probiotic beverage made from organic and non-GMO pea protein with 10 vegan kefir cultures; a line of probiotic supplements for adults and children; and a soft serve kefir mix.

Our product categories are:

- Drinkable Kefir, sold in a variety of organic and non-organic sizes, flavors, and types, including low fat, non-fat, whole milk, protein, BioKefir (a 3.5 oz. kefir with additional probiotic cultures), and Kefir with Oats.
- European-style soft cheeses, including farmer cheese in resealable cups.
- Cream and other, which consists primarily of cream, a byproduct of making our kefir.
- ProBugs, a line of kefir products in drinkable and frozen formats, designed for children.
- Other Dairy, which includes Cupped Kefir and Icelandic Skyr, a line of strained kefir and yogurt products in resealable cups.
- Frozen Kefir, available in both bars and pint-size containers.

Lifeway has determined that it has one reportable segment based on how our chief operating decision maker manages the business and in a manner consistent with the internal reporting provided to the chief operating decision maker. The chief operating decision maker, who is responsible for allocating resources and assessing our performance, has been identified collectively as the Chief Financial Officer, the Chief Operating Officer, the Chief Executive Officer, and Chairperson of the board of directors. Substantially all of our consolidated revenues relate to the sale of cultured dairy products that we produce using the same processes and materials and are sold to consumers through a common network of distributors and retailers in the United States.

Net sales of products by category were as follows for the six months ended June 30:

	2019		2018	
	$	%	$	%
Drinkable Kefir other than ProBugs	$ 36,613	77%	$ 42,378	76%
Cheese	5,557	11%	5,787	10%
Cream and other	2,446	5%	2,698	5%
ProBugs Kefir	1,460	3%	1,695	3%
Other dairy	902	2%	2,455	4%
Frozen Kefir (a)	790	2%	825	2%
Net Sales	$ 47,768	100%	$ 55,838	100%

(a) Includes Lifeway Kefir Shop sales

Net sales of products by category were as follows for the three months ended June 30:

	2019		2018	
	$	%	$	%
Drinkable Kefir other than ProBugs	$ 17,727	76%	$ 20,715	76%
Cheese	2,706	12%	2,853	11%
Cream and other	1,145	5%	1,206	4%
ProBugs Kefir	697	3%	743	3%
Other dairy	423	2%	1,118	4%
Frozen Kefir (a)	455	2%	461	2%
Net Sales	$ 23,153	100%	$ 27,096	100%

(a) Includes Lifeway Kefir Shop sales

Significant Customers – Sales are predominately to companies in the retail food industry located within the United States. Two major customers accounted for approximately 22% of net sales for the six months ended June 30, 2019 and 2018, respectively. Two major customers accounted for approximately 22% and 23% of net sales for the three months ended June 30, 2019 and 2018, respectively.

Note 13 – Related party transactions

Lifeway obtains consulting services from the Chairperson of its board of directors. Fees earned by the Chairperson are included in general and administrative expenses in the accompanying consolidated statements of operations and were $500 during each of the six months ended June 30, 2019 and 2018. Fees earned by the Chairperson are included in general and administrative expenses in the accompanying consolidated statements of operations and were $250 during each of the three months ended June 30, 2019 and 2018.

Lifeway is also a party to a royalty agreement with the Chairperson of its board of directors under which we pay the Chairperson a royalty based on the sale of certain Lifeway products, not to exceed $50 in any fiscal month. Royalties earned by the Chairperson are included in selling expenses in the accompanying consolidated statements of operations and were $298 and $300 during each of the six months ended June 30, 2019 and 2018, respectively. Royalties earned by the Chairperson are included in selling expenses in the accompanying consolidated statements of operations and were $148 and $150 during each of the three months ended June 30, 2019 and 2018, respectively.

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.

Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") in this Form 10-Q is provided as a supplement to, and should be read in conjunction with, our audited consolidated financial statements, the accompanying notes, and the MD&A included in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018 (the "Form 10-K"). Unless otherwise specified, any description of "our", "we", and "us" in this MD&A refer to Lifeway Foods, Inc. and our subsidiaries.

Cautionary Statement Regarding Forward-Looking Statements

In addition to historical information, this quarterly report contains "forward-looking" statements within the meaning of the "safe harbor" provisions of the Private Securities Litigation Reform Act of 1995. These statements may be identified by the use of words such as "anticipate," "believe," "could," "estimate," "expect," "from time to time," "future," "intend," "plan," "likely," "may," "ongoing," "realize," "should," "will," and similar terms or terminology, or the negative of such terms or other comparable terminology. Examples of forward-looking statements include, among others, statements we make regarding:

- Expectations of the effect on our financial condition of claims, litigation, environmental costs, contingent liabilities and governmental and regulatory investigations and proceedings;
- Strategy for acquisitions, customer retention, growth, product development, market position, financial results and reserves; Estimates of the amounts of sales allowances and discounts to our customers and consumers;
- Our belief that we will maintain compliance with our loan agreements and have sufficient liquidity to fund our business operations.

Forward-looking statements are neither historical facts nor assurances of future performance. Instead, they are based only on our current beliefs, expectations and assumptions regarding the future of our business, future plans and strategies, projections, anticipated events and trends, the economy and other future conditions. Because forward-looking statements relate to the future, they are subject to inherent uncertainties, risks and changes in circumstances that are difficult to predict and many of which are outside of our control. Our actual results and financial condition may differ materially from those indicated in the forward-looking statements. Therefore, you should not rely on any of these forward-looking statements. Important factors that could cause our actual results and financial condition to differ materially from those indicated in the forward-looking statements include, among others, the following:

- The impact of investigative and legal proceedings;
- Developments and changes in laws and regulations, including regulation of the dairy or food industries through legislative action and revised rules and standards applied by the Food & Drug Administration (FDA);
- Economic and financial conditions, including volatility in interest and exchange rates, commodity and equity prices, and the value of our assets;
- Changes in the price of milk and other key materials and disruptions in supply chains for these materials;
- Strategic actions, including acquisitions and dispositions and our success in launching new products;
- The impact on our competitive position if we do not maintain compliance with our loan agreements and/or sufficient liquidity to fund our business operations;
- Such other factors as discussed throughout Part I, Item 1 "Business"; Part I, Item 1A "Risk Factors"; and Part II, Item 7 "Management's Discussion and Analysis of Financial Condition and Results of Operations" of our Annual Report on Form 10-K for the year ended December 31, 2018 and that are described from time to time in our filings with the SEC.

These factors are not necessarily all of the important factors that could cause actual results to differ materially from those expressed in any of our forward-looking statements. Other unknown or unpredictable factors could also have material adverse effects on future results. We intend these forward-looking statements to speak only at the date made. Except as otherwise required to be disclosed in periodic reports required to be filed by public companies with the SEC pursuant to the SEC's rules, we have no duty to update these statements, and we undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Results of Operations

Three Months Ended June 30, 2019 Compared to Three Months Ended June 30, 2018

	June 30,		Change	
	2019	2018	$	%
Net sales	**$ 23,153**	**$ 27,096**	**$ (3,943)**	**(14.6%)**
Cost of goods sold	$ 16,843	$ 19,495	$ 2,652	
Depreciation expense	747	725	(22)	
Total cost of goods sold	**$ 17,590**	**$ 20,220**	**$ 2,630**	**13.0%**
Gross profit	**$ 5,563**	**$ 6,876**	**$ (1,313)**	**(19.1%)**
Gross Profit % to net sales	*24.0%*	*25.4%*		
Selling expenses	**$ 2,691**	**$ 3,383**	**$ 692**	**20.5%**
Selling expenses % to net sales	*11.6%*	*12.5%*		
General & administrative expenses	**$ 2,898**	**$ 2,996**	**$ 98**	**3.3%**
General & administrative % to net sales	*12.5%*	*11.1%*		
Amortization expense	**$ 40**	**$ 164**	**$ 124**	**75.6%**
Total operating expenses	**$ 5,629**	**$ 6,543**	**$ 914**	**14.0%**
Total operating expense % to net sales	*24.3%*	*24.1%*		
(Loss) income from operations	**$ (66)**	**$ 333**	**$ (399)**	**(119.8%)**
(Loss) income from operations % to net sales	*(0.3%)*	*1.2%*		

Net Sales

Net sales finished at $23,153 for the three-month period ended June 30, 2019, a decrease of $3,943 or 14.6% versus prior year. The net sales softness continued to reflect the overall lower consumption in the dairy and cultured dairy product categories. Versus prior year, the decline was primarily driven by lower volumes of our branded drinkable kefir and cupped kefir and Skyr sales, partially offset by the incremental volume of new item introductions.

Gross Profit

Gross profit as a percentage of net sales was 24.0% during the three-month period ended June 30, 2019. Gross profit percentage was 25.4% in the prior year. The decline versus the prior year was primarily due to the unfavorable impact of operating leverage that arises from lower net sales relative to fixed costs, partially offset by a reduction in variable costs. Additionally, depreciation expense increased reflecting the continued investment in manufacturing improvements.

Selling Expenses

Selling expenses decreased by $692 or 20.5% to $2,691 during the three-month period ended June 30, 2019 from $3,383 during the same period in 2018. The decrease versus prior year, primarily reflects a reduction in advertising and marketing programs with lower efficiency, and to a lesser extent compensation savings from organizational changes made in 2018, and broker commissions. Selling expenses as a percentage of net sales were 11.6% during the three-month period ended June 30, 2019 compared to 12.5% for the same period in 2018.

General and administrative expenses

General and administrative expenses decreased $98 or 3.3% to $2,898 during the three-month period ended June 30, 2019 from $2,996 during the same period in 2018. The decrease is primarily a result of lower compensation expense due to organizational changes made in 2018, and lower legal and professional fees, partially offset by increased incentive compensation.

Provision for Income Taxes

The provision for income taxes includes federal, state and local income taxes. Provision for income taxes was $13 during the three months ended June 30, 2019, compared to a provision for income taxes of $90 during the same period in 2018.

Our effective income tax rate (ETR) for the three months ended June 30, 2019 was 9.9% compared to an ETR of 34.6% in the same period last year. The lower effective tax rate was primarily due to the separate state tax rates, change in valuation allowance and non-deductible expense amounts being a higher percentage of pre-tax income. During the three-month period ended June 30, 2019, we recognized non-deductible compensation expense related to equity incentive awards. This resulted in a permanent rate effect and was considered in the estimated full year tax rate.

Section 162(m) of the Internal Revenue Code (the “Code”) limits the deductibility of compensation paid to certain of our executives. Under the Tax Cuts and Jobs Act (the “Act”) amendments to Section 162(m), no tax deduction in taxable years beginning after December 31, 2017 is allowed for compensation paid to any covered employee to the extent that the total compensation for that covered employee exceeds $1,000,000 in any taxable year. Although the Act eliminated the prior tax deduction under Section 162(m) for performance-based executive compensation, it included a transition rule under which the changes to Section 162(m) will not apply to awards made to our covered employees who had the right to participate in our 2015 Omnibus Incentive Plan pursuant to written binding contracts in effect as of November 2, 2017, as long as those contracts have not subsequently been modified in any material respect. Accordingly, subject to further guidance from the Treasury Department and the Internal Revenue Service (“IRS”), we expect that performance-based compensation paid to our executives under our Omnibus Plan will remain eligible for the Section 162(m) exemption in 2019.

Income taxes are discussed in Note 10 in the Notes to the Consolidated Financial Statements.

Net (Loss) Income

We reported a net loss of $(141) or $(0.01) per basic and diluted common share for the three-month period ended June 30, 2019 compared to net income of $170 or $0.01 per basic and diluted common share in the same period in 2018.

Six Months Ended June 30, 2019 Compared to Six Months Ended June 30, 2018

	June 30,		Change	
	2019	2018	$	%
Net sales	**$ 47,768**	**$ 55,838**	**$ (8,070)**	**(14.5%)**
Cost of goods sold	$ 34,410	$ 39,520	$ 5,110	
Depreciation expense	1,492	1,405	(87)	
Total cost of goods sold	**$ 35,902**	**$ 40,925**	**$ 5,023**	**12.3%**
Gross profit	**$ 11,866**	**$ 14,913**	**$ (3,047)**	**(20.4%)**
Gross Profit % to net sales	*24.8%*	*26.7%*		
Selling expenses	**$ 5,830**	**$ 7,401**	**$ 1,571**	**21.2%**
Selling expenses % to net sales	*12.2%*	*13.3%*		
General & administrative expenses	**$ 6,390**	**$ 6,701**	**$ 311**	**4.6%**
General & administrative % to net sales	*13.4%*	*12.0%*		
Amortization expense	**$ 113**	**$ 327**	**$ 214**	**65.4%**
Total operating expenses	**$ 12,333**	**$ 14,429**	**$ 2,096**	**14.5%**
Total operating expense % to net sales	*25.8%*	*25.8%*		
(Loss) income from operations	**$ (467)**	**$ 484**	**$ (951)**	**(196.5%)**
(Loss) income from operations % to net sales	*(1.0%)*	*0.9%*		

Net Sales

Net sales were $47,768 for the six-month period ended June 30, 2019, a decrease of $8,070 or 14.5% versus prior year. The net sales softness continued to reflect the overall lower consumption in the dairy and cultured dairy product categories. Versus prior year, the decline was primarily driven by lower volumes of our branded drinkable kefir and cupped kefir and Skyr sales, partially offset by the incremental volume of new item introductions.

Gross Profit

Gross profit as a percentage of net sales decreased to 24.8% during the six-month period ended June 30, 2019 from 26.7% during the same period in 2018. The lower gross profit percentage primarily reflects category sales softness, the unfavorable impact of operating leverage that arises from lower net sales relative to fixed costs, and increased freight costs, partially offset by a reduction in variable costs.

Selling Expenses

Selling expenses decreased by $1,571 or 21.2% to $5,830 during the six-month period ended June 30, 2019 from $7,401 during the same period in 2018. The decreased selling expenses primarily reflect the reduction in advertising and marketing programs with lower efficiency, compensation savings from organizational changes made in 2018, and broker commissions. Selling expenses as a percentage of net sales were 12.2% during the six-month period ended June 30, 2019 compared to 13.3% for the same period in 2018.

Provision for Income Taxes

The provision for income taxes includes federal, state and local income taxes. Benefit for income taxes was $41 during the six months ended June 30, 2019, compared to a provision for income taxes of $128 during the same period in 2018.

Our effective income tax rate (ETR) for the six months ended June 30, 2019 was (7.2%) compared to an ETR of 34.8% in the same period last year. The lower effective tax rate was primarily due to the separate state tax rates, change in valuation allowance and non-deductible expense amounts being a higher percentage of pre-tax income. During the six-month period ended June 30, 2019, we recognized non-deductible compensation expense related to equity incentive awards. This resulted in a permanent rate effect and was considered in the estimated full year tax rate.

Section 162(m) of the Code limits the deductibility of compensation paid to certain of our executives. Under the Act's amendments to Section 162 (m), no tax deduction in taxable years beginning after December 31, 2017 is allowed for compensation paid to any covered employee to the extent that the total compensation for that covered employee exceeds $1,000,000 in any taxable year. Although the Act eliminated the prior tax deduction under Section 162(m) for performance-based executive compensation, it included a transition rule under which the changes to Section 162(m) will not apply to awards made to our covered employees who had the right to participate in our 2015 Omnibus Incentive Plan pursuant to written binding contracts in effect as of November 2, 2017, as long as those contracts have not subsequently been modified in any material respect. Accordingly, subject to further guidance from the Treasury Department and the Internal Revenue Service ("IRS"), we expect that performance-based compensation paid to our executives under our Omnibus Plan will remain eligible for the Section 162(m) exemption in 2019.

Income taxes are discussed in Note 10 in the Notes to the Consolidated Financial Statements.

Net (Loss) Income

We reported a net loss of $(529) or $(0.03) per basic and diluted common share for the six-month period ended June 30, 2019 compared to net income of $240 or $0.02 per basic and diluted common share in the same period in 2018.

Liquidity and Capital Resources

We expect to meet our foreseeable liquidity and capital resource requirements through anticipated cash flows from operations; our revolving credit facility; and cash and cash equivalents. The success of our business and financing strategies will continue to provide us with the financial flexibility to take advantage of various opportunities as they arise.

Sources and Uses of Cash

Lifeway had a net increase in cash and cash equivalents of $24 during the six-month period ended June 30, 2019 compared to a net decrease in cash and cash equivalents of $1,346 in the same period in 2018. The drivers of the year over year change are as follows:

Net cash provided by operating activities was $2,008 during the six-month period ended June 30, 2019 compared to net cash provided by operating activities of $2,109 in the same period in 2018. The decrease in cash provided by operating activities reflects lower net income, partially offset by the change in working capital.

Net cash used in investing activities was $269 during the six-month period ended June 30, 2019 compared to net cash used in investing activities of $1,989 in the same period in 2018. The lower level of net cash used in investing activities in 2019 reflects lower capital spending. Capital spending was $290 during the six-month period ended June 30, 2019 compared to $2,024 in 2018. Our capital spending is focused in three core areas: growth, cost reduction, and facility improvements. Growth capital spending supports new product innovation and enhancements. Cost reduction spending supports manufacturing efficiency, safety and productivity.

Net cash used in financing activities was $1,715 during the six-month period ended June 30, 2019 compared to net cash used in financing activities of $1,466 in the same period in 2018. We utilized proceeds from our federal and state income tax refunds to repay $1,330 on our revolving line of credit during the first quarter of 2019. On November 1, 2017, Lifeway's Board approved an increase in the aggregate amount under our previously announced 2015 stock repurchase program (the "2017 Repurchase Plan Amendment"), by adding to (i.e., exclusive of the shares previously authorized under the 2015 stock repurchase program) the authorization the lesser of $5,185 or 625 shares. We repurchased approximately 156 shares of common stock at a cost of $385 during the six-month period ended June 30, 2019 under the 2017 Repurchase Plan Amendment. We may execute transactions from time to time in the open market or by private negotiation, in accordance with all applicable securities laws and regulations. We intend to hold repurchased shares in treasury for general corporate purposes, including issuances under our 2015 Omnibus Incentive Plan. Treasury shares are accounted for using the cost method.

Revolving credit facility

On April 10, 2019, effective March 31, 2019, Lifeway entered into the First Modification to the Amended and Restated Loan and Security Agreement (the "Modified Revolving Credit Facility") with its existing lender. Under the amendment, the Modified Revolving Credit Facility provides for a revolving line of credit up to a maximum of $9 million (the "Revolving Loan") with an incremental facility not to exceed $5 million (the "Incremental Facility" and together with the Revolving Loan, the "Loans").

All outstanding amounts under the Loans bear interest, based on a level of the Senior Debt to EBITDA ratio, at Lifeway's election, at either the lender Base Rate (the greater of either the Federal Funds Rate plus 0.0% to 0.5%, or the Prime Rate) or the LIBOR plus 2.25% to 3.00%, payable monthly in arrears. Lifeway is also required to pay a quarterly unused line fee and, in conjunction with the issuance of any letters of credit, a letter of credit fee.

As amended, the Modified Revolving Credit Facility contains customary representations, warranties, and covenants on the part of Lifeway, including financial covenants requiring us to achieve a minimum EBITDA threshold for each of the fiscal quarters through December 31, 2019, and maintain a fixed charge coverage ratio of no less than 1.25 to 1.0 each of the fiscal quarters ending through the expiration date. The Modified Revolving Credit Facility also provides for events of default, including failure to repay principal and interest when due and failure to perform or violation of the provisions or covenants of the agreement, as a result of which amounts due under the Modified Revolving Credit Facility may be accelerated. We were in compliance with the applicable covenants as of June 30, 2019

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

There have been no material changes to our market risk during the first quarter of 2019. For information regarding our exposure to certain market risk, see Part II, Item 7A, "Quantitative and Qualitative Disclosures About Market Risk", in the 2018 Form 10-K.

ITEM 4. CONTROLS AND PROCEDURES.

(a) Evaluation of Disclosure Controls and Procedures

Our evaluation of the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act was performed under the supervision and with the participation of our senior management, including our Chief Executive Officer and Chief Financial Officer. The purpose of disclosure controls and procedures is to ensure that information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosures.

As previously disclosed under "Item 9A—Controls and Procedures" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2018, we concluded that our internal control over financial reporting was not effective based on the material weakness in our controls over the review of the result of the annual step one goodwill impairment evaluation performed by the third party valuation expert that we engaged. Based on the material weakness, which we view as an integral part of our disclosure controls and procedures, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the quarter ended June 30, 2019, our disclosure controls and procedures were not effective. Nevertheless, based on a number of factors, including the performance of additional procedures by management designed to ensure the reliability of our financial reporting, we believe that the consolidated financial statements in this Quarterly Report on Form 10-Q fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with GAAP.

(b) Changes in Internal Control over Financial Reporting

Our remediation efforts began during the six months ended June 30, 2019. Remediation generally requires making changes to how controls are designed and implemented and then adhering to those changes for a sufficient period of time such that the effectiveness of those changes is demonstrated with an appropriate amount of consistency. We have begun to take certain remediation steps to address the material weakness referenced above and to improve our control over financial reporting. If not remediated these deficiencies could result in material misstatements to our consolidated financial statements.

In response to the material weakness described above, management is currently evaluating our policies and procedures related to the review of the analysis in goodwill impairment reports prepared by third-party valuation experts and plans to design and implement adequate internal controls and procedures to ensure that (i) goodwill impairment is properly reviewed, accounted for and disclosed, and (ii) management can more effectively evaluate analysis conducted by third-party valuation service providers that perform the step one goodwill impairment analysis.

There were no other changes in our internal control over financial reporting during the second quarter of 2019 that were identified in connection with management's evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 under the Exchange Act that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II – OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

From time to time we are engaged in litigation matters arising in the ordinary course of business. While the results of litigation and claims cannot be predicted with certainty, Lifeway believes that no such matter is reasonably likely to have a material adverse effect on our financial position or results of operations.

ITEM 1A. RISK FACTORS.

There have been no material changes to the Risk Factors disclosed in Part I, Item 1A of the 2018 Form 10-K.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

Issuer Purchases of Equity Securities

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

None.

ITEM 4. MINE SAFETY DISCLOSURE.

Not applicable.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS.

No.	Description	Form	Period Ending	Exhibit	Filing Date
10.1	First Modification to Amended and Restated Loan and Security Agreement dated as of April 10, 2019 among Lifeway Foods, Inc., Fresh Made, Inc., The Lifeway Kefir Shop, LLC, Lifeway Wisconsin, Inc., and CIBC Bank USA, as Lender.	10-K	12/31/18	10.10	4/15/19
31.1	Rule 13a-14(a)/15d-14(a) Certification of Julie Smolyansky	Filed Herewith			
31.2	Rule 13a-14(a)/15d-14(a) Certification of Eric Hanson	Filed Herewith			
32.1	Section 1350 Certification of Julie Smolyansky	Filed Herewith			
32.2	Section 1350 Certification of Eric Hanson	Filed Herewith			
99.1	Press release dated August 19, 2019 reporting Lifeway's financial results for the six months ended June 30, 2019.	Furnished Herewith			
101	Interactive Data Files	Filed Herewith			

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.

LIFEWAY FOODS, INC.

Date: August 19, 2019	By: /s/ Julie Smolyansky Julie Smolyansky Chief Executive Officer, President, and Director (Principal Executive Officer)
Date: August 19, 2019	By: /s/ Eric Hanson Eric Hanson Chief Financial & Accounting Officer (Principal Financial and Accounting Officer)

EXHIBIT 31.1

SECTION 302 CERTIFICATION OF C.E.O.
CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Julie Smolyansky, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lifeway Foods, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 19, 2019

By: /s/ Julie Smolyansky
Julie Smolyansky
Chief Executive Officer, President and Director
(Principal Executive Officer)

EXHIBIT 31.2

SECTION 302 CERTIFICATION OF C.F.O.
CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Eric Hanson, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lifeway Foods, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors:

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 19, 2019

By: /s/ Eric Hanson
Eric Hanson
Chief Financial Officer
(Principal Financial and Accounting Officer)

EXHIBIT 32.1

SECTION 906 CERTIFICATION OF C.E.O.
CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT
TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Lifeway Foods, Inc. (the "Company") for the period ended June 30, 2019 as filed with the SEC (the "Report"), the undersigned, in the capacity and on the date indicated below, hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to her knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 19, 2019

By: /s/ Julie Smolyansky
Julie Smolyansky
Chief Executive Officer, President and Director
(Principal Executive Officer)

EXHIBIT 32.2

SECTION 906 CERTIFICATION OF C.F.O.
CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT
TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Lifeway Foods, Inc. (the “Company”) for the period ended June 30, 2019 as filed with the SEC (the “Report”), the undersigned, in the capacity and on the date indicated below, hereby certifies pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

1. The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

2. The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: August 19, 2019

By: /s/ Eric Hanson
Eric Hanson
Chief Financial Officer
(Principal Financial and Accounting Officer)

Lifeway Foods, Inc. Announces Second Quarter 2019 Results

Reports Sequential Quarterly Profit Improvement

Morton Grove, IL — August 19, 2019—Lifeway Foods, Inc. (Nasdaq: LWAY) ("Lifeway" or "the Company"), the leading U.S. supplier of kefir and fermented probiotic products to support the microbiome, today reported financial results for the second quarter ended June 30, 2019.

"The improvement in sequential quarterly profit highlights the significant progress we've made to position Lifeway for long-term, sustainable growth," said Julie Smolyansky, CEO of Lifeway Foods, Inc. "The items debuted this year at trade shows are now hitting shelves, and we're encouraged by the exciting distribution growth of our newest offering, Plantiful, a line of vegan, plant-based probiotic beverages. Based on retailer shelf reset schedules for items already accepted, we are planning for marketing and advertising initiatives that align with the expanded distribution of our innovation portfolio. Our team is focused on long-term success by building increased brand awareness and consumer loyalty on our strong core product line, as well as the burgeoning prospects of our recent offerings."

About Lifeway Foods, Inc.

About Lifeway Foods, Inc. Lifeway Foods, Inc., which has been recognized as one of Forbes' Best Small Companies, is America's leading supplier of the probiotic, fermented beverage known as kefir. In addition to its line of drinkable kefir, the company also produces non-dairy Plantiful, cupped kefir and cheese, frozen kefir, specialty cheeses, probiotic supplements and a ProBugs line for kids. Lifeway's tart and tangy fermented dairy and non-dairy products are now sold across the United States, Mexico, Ireland and the United Kingdom. Learn how Lifeway is good for more than just you at **www.lifewaykefir.com**.

Forward-Looking Statements

All statements in this release (and oral statements made regarding the subjects of this release) contains "forward-looking statements" as defined in the Private Securities Litigation Reform Act of 1995 regarding, among other things, future operating and financial performance, product development, market position, business strategy and objectives. These statements use words, and variations of words, such as "believe," "ahead," "remain," "build," "generate," "progress," "innovate," "continue." Other examples of forward looking statements may include, but are not limited to, (i) statements of Company plans and objectives, including the introduction of new products, or estimates or predictions of actions by customers or suppliers, (ii) statements of future economic performance, and (III) statements of assumptions underlying other statements and statements about Lifeway or its business. You are cautioned not to rely on these forward-looking statements. These statements are based on current expectations of future events and thus are inherently subject to uncertainty. If underlying assumptions prove inaccurate or known or unknown risks or uncertainties materialize, actual results could vary materially from Lifeway's expectations and projections. These risks, uncertainties, and other factors include: price competition; the decisions of customers or consumers; the actions of competitors; changes in the pricing of commodities; the effects of government regulation; possible delays in the introduction of new products; and customer acceptance of products and services. A further list and description of these risks, uncertainties, and other factors can be found in Lifeway's Annual Report on Form 10-K for the fiscal year ended December 31, 2018, and the Company's subsequent filings with the SEC. Copies of these filings are available online at https://www.sec.gov, http://lifewaykefir.com/investor-relations/, or on request from Lifeway. Information in this release is as of the dates and time periods indicated herein, and Lifeway does not undertake to update any of the information contained in these materials, except as required by law. Accordingly, YOU SHOULD NOT RELY ON THE ACCURACY OF ANY OF THE STATEMENTS OR OTHER INFORMATION CONTAINED IN ANY ARCHIVED PRESS RELEASE.

Contact:
Lifeway Foods, Inc.
Phone: 847-967-1010
Email: info@lifeway.net

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Balance Sheets
June 30, 2019 and December 31, 2018
(In thousands)

	June 30, 2019 (Unaudited)	December 31, 2018
Current assets		
Cash and cash equivalents	$ 3,022	$ 2,998
Accounts receivable, net of allowance for doubtful accounts and discounts & allowances of $1,220 at June 30, 2019 and December 31, 2018 respectively	7,570	6,276
Inventories, net	6,843	5,817
Prepaid expenses and other current assets	1,393	1,077
Refundable income taxes	1,278	2,748
Total current assets	**20,106**	**18,916**
Property, plant and equipment, net	**23,365**	**24,573**
Operating lease right-of-use asset	**966**	–
Intangible assets		
Goodwill & indefinite-lived intangibles	12,824	12,824
Other intangible assets, net	231	344
Total intangible assets	**13,055**	**13,168**
Other assets	**165**	150
Total assets	**$ 57,657**	**$ 56,807**
Current liabilities		
Accounts payable	$ 5,459	$ 4,570
Accrued expenses	4,141	2,777
Accrued income taxes	63	106
Total current liabilities	**9,663**	**7,453**
Line of credit	**4,677**	**5,995**
Operating lease liabilities	**584**	–
Deferred income taxes, net	**390**	**390**
Other long-term liabilities	**100**	**564**
Total liabilities	**15,414**	**14,402**
Stockholders' equity		
Preferred stock, no par value; 2,500 shares authorized; no shares issued or outstanding at June 30, 2019 and December 31, 2018, respectively	–	–
Common stock, no par value; 40,000 shares authorized; 17,274 shares issued; 15,761 and 15,814 outstanding at June 30, 2019 and December 31, 2018, respectively	6,509	6,509
Paid-in capital	2,230	2,303
Treasury stock, at cost	(12,477)	(12,970)
Retained earnings	45,981	46,563
Total stockholders' equity	**42,243**	**42,405**
Total liabilities and stockholders' equity	**$ 57,657**	**$ 56,807**

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Operations
For the six months ended June 30, 2019 and 2018
(Unaudited)
(In thousands, except per share data)

	Three Months Ended June 30, 2019	Three Months Ended June 30, 2018	Six Months Ended June 30, 2019	Six Months Ended June 30, 2018
Net sales	**$ 23,153**	**$ 27,096**	**$ 47,768**	**$ 55,838**
Cost of goods sold	16,843	19,495	34,410	39,520
Depreciation expense	747	725	1,492	1,405
Total cost of goods sold	17,590	20,220	35,902	40,925
Gross profit	**5,563**	**6,876**	**11,866**	**14,913**
Selling expenses	2,691	3,383	5,830	7,401
General and administrative	2,898	2,996	6,390	6,701
Amortization expense	40	164	113	327
Total operating expenses	**5,629**	**6,543**	**12,333**	**14,429**
(Loss) income from operations	**(66)**	**333**	**(467)**	**484**
Other income (expense):				
Interest expense	(68)	(75)	(137)	(138)
Gain (loss) on sale of property and equipment	4	(1)	29	14
Other income, net	2	3	5	8
Total other income (expense)	(62)	(73)	(103)	(116)
(Loss) income before provision for income taxes	**(128)**	**260**	**(570)**	**368**
Provision for income taxes	13	90	(41)	128
Net (loss) income	**$ (141)**	**$ 170**	**$ (529)**	**$ 240**
Earnings (loss) per common share:				
Basic	$ (0.01)	$ 0.01	$ (0.03)	$ 0.02
Diluted	$ (0.01)	$ 0.01	$ (0.03)	$ 0.02
Weighted average common shares:				
Basic	15,775	15,879	15,771	15,893
Diluted	15,775	15,992	15,771	16,026

LIFEWAY FOODS, INC. AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Six Months Ended June 30, 2019 and 2018
(Unaudited)
(In thousands)

	2019	2018
Cash flows from operating activities:		
Net (loss) income	**$ (529)**	**$ 240**
Adjustments to reconcile net (loss) income to operating cash flow:		
Depreciation and amortization	1,605	1,732
Bad debt expense	3	20
Reserve for inventory obsolescence	210	271
Stock-based compensation	535	495
Non-cash interest expense	12	3
Deferred revenue	(48)	(48)
(Gain) on sale of property and equipment	(29)	(14)
(Increase) decrease in operating assets:		
Accounts receivable	(1,297)	66
Inventories	(1,235)	243
Refundable income taxes	1,470	(463)
Prepaid expenses and other current assets	(308)	(584)
Increase (decrease) in operating liabilities:		
Accounts payable	888	423
Accrued expenses	774	(153)
Accrued income taxes	(43)	(121)
Net cash provided by operating activities	**2,008**	**2,109**
Cash flows from investing activities:		
Purchases of property and equipment	(290)	(2,024)
Proceeds from sale of property and equipment	36	35
Purchase of investments	(15)	–
Net cash used in investing activities	**(269)**	**(1,989)**
Cash flows from financing activities:		
Purchase of treasury stock	(385)	(1,168)
Borrowings under revolving credit facility	–	6,050
Repayment of line of credit	(1,330)	–
Payment of deferred financing costs	–	(69)
Repayment of notes payable	–	(6,279)
Net cash used in financing activities	**(1,715)**	**(1,466)**
Net decrease in cash and cash equivalents	**24**	**(1,346)**
Cash and cash equivalents at the beginning of the period	2,998	4,978
Cash and cash equivalents at the end of the period	**$ 3,022**	**$ 3,632**
Supplemental cash flow information:		
Cash paid for income taxes, net of (refunds)	$ (1,469)	$ 712
Cash paid for interest	$ 149	$ 108
Non-cash investing activities		
Right-of-use assets recognized at ASU 2016-02 transition	$ 944	$ –
Operating lease liability recognized at ASU 2016-02 transition	$ 997	$ –
Right-of-use assets and operating lease liabilities recognized after ASU 2016-02 transition	$ 280	$ –