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Interstate Bakeries

Interstate Bakeries Corporation is a wholesale baker and distributor of fresh baked bread and sweet goods. (Wonder Bread, Hostess Twinkies). The company filed Chapter 11 Bankruptcy on 9/22/2004.

Institutional investors willing to assume the risk associated with a company in the early stages of a bankruptcy reorganization should consider Interstate Bakeries 6% convertible debt due 8/15/2014 priced at 85. The bankruptcy process should allow the company to restructure its asset base, break union contracts and prepare for future asset sales. *We expect a full recovery of principal and pre-petition interest for the holders of these bonds. Our recommendation is based on moderate improvement in financial variables such as EBITDA and a successful strategy for reorganization.*

Recent Events Leading to the Chapter 11 Bankruptcy Filing

IBC generated about \$3.5 billion in annual sales and \$192 million in EBITDA in fiscal year 2003. For the 40 weeks ended 3/6/04, net sales fell 2% to 2.66 billion. Net income fell 63% to \$11.7 million or \$.26 cents per share.

“IBC experienced volume declines in both branded cake and branded bread sales. During fiscal 2004 – ending May 29, 2004 – total unit volumes of branded bread declined by 3.7% from the comparable fiscal 2003 period. Unit volumes of branded sweet goods also declined by 3.7%.

IBC has not been able to adequately reduce its costs in response to decreased demand for its products due to their somewhat inflexible fixed cost structure. Approximately 80% of the company’s workers are employed under collective bargaining agreements, where wages are generally higher and the ability to implement productivity improvements and effect savings are restricted.

Bakery industry consolidation and more efficient production methods, including extended shelf life programs, have resulted in excess industry capacity. This excess industry capacity has made it more difficult to raise selling prices to offset increased costs of production.

The principal raw materials used to produce fresh bread and sweet goods, as well as gas, electricity and fuel used in the bakeries and trucks are all subject to substantial price fluctuations and increases.”*1

Important Disclosures Page 3

*1 Bankruptcy Creditors Service, Issue #1, DTD 9/23/04 page 5

Uncertainty caused by the company's recent bankruptcy filing has been magnified by:

- (1) An informal SEC investigation into accounting for workman's compensation reserves that led to a \$40 million increase in FY04 expense.
- (2) Problems filing its FY04 10-k on time.
- (3) Re-statement of 10-Q documents for both the second and third quarters (re-stated for increased worker's compensation expense). The delayed filings were caused in part by difficulties implementing a new SAP AG software accounting system.

The company announced a commitment for \$200 million in debtor-in-possession (DIP) financing from JPMorgan Chase Bank. With this credit facility in place, the company believes it has adequate resources to buy goods and services and fulfill obligations to employees and customers.

On September 21, 2004, James R. Elsesser resigned as CEO and was replaced by Antonio Alvarez of Alvarez & Marsal, LLC. A&M specializes in advisory & crisis management to troubled companies.

Projections and Estimates

In the fiscal year ending May 2003, IBC generated \$192 million of EBITDA. Trailing 12 month (3rd QTR 04) EBITDA is \$150 million. Using a multiple of 6 times EBITDA, IBC's enterprise value would be \$900 million. That would cover its \$750 million of debt (\$650 million in secured debt and \$100 million of recently issued convertible bonds) and leave about \$150 million for equity holders. With restructuring incentives EBITDA should increase as the company exits the bankruptcy process.

EBITDA (MIL)

2000	2001	2002	2003	AVG
\$282	\$258	\$269	\$192	\$250
Q103	Q203	Q303	Q403	TOTAL
\$72.8	\$55.2	\$35.2	\$28.2	\$191.4
Q104	Q204	Q304	Q404	TOTAL
\$48.4	\$43.3	\$31.1	N/A	N/A

*Source: Bloomberg Data

Recommendation

Institutional investors should consider Interstate Bakeries 6% convertible debt due 8/15/2014 priced at 85. We expect a full recovery of principal and pre-petition interest for the holders of these bonds. Our recommendation is based on moderate improvement in financial variables such as EBITDA and a successful strategy for reorganization.

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Disclosure SEC Regulation AC, NASD Rule 2711 (h)

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Analyst Certification Requirement

- This communication accurately reflects the analyst's personal views about the company.
- The analyst has not and will not receive compensation with respect to the issuance of this report

RISKS

- The company is currently operating under Chapter 11 bankruptcy protection. The ability of the company to exit from bankruptcy is uncertain, as is the timing of the filing of a plan of reorganization.
- Estimates for the ultimate recovery value of the securities discussed may not be realized.
- Spencer Clarke LLC has not sought legal opinions regarding any topics in this report.
- Special risks are associated with hostilities, acts of war, or terrorist attacks.
- See SEC filings for additional potential risks.
- Combined risk factors make our estimates statistically unreliable.

Ratings Systems Explanation

Buy: We generally expect "BUY" rated investments returns to be $\geq +20\%$ from date of the original recommendation

Neutral: We generally expect "NEUTRAL" rated investments returns to deviate $-20\% \leq CMV < +20\%$ from date of the original recommendation

Sell: We generally expect "SELL" rated investments returns to be $> -20\%$ from date of the original recommendation

CMV: Current Market Value

Spencer Clarke LLC
Ratings Distribution as of 10/18/04

	Number of Companies	Percent of Total
Buy	3	100
Neutral	0	0
Sell	0	0
Total	3	100

Companies for which Spencer Clarke LLC has performed
Investment Banking services in last 12 month as of 10/18/04

	Number of Companies	Percent of Total
Buy	0	0
Neutra	0	0
Sell	0	0
Total	0	0