

COFFEE HOLDING CO INC  
Form 10-Q  
March 17, 2017

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: **January 31, 2017**

OR

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

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: **001-32491**

**Coffee Holding Co., Inc.**  
*(Exact name of registrant as specified in its charter)*

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Nevada  
(State or other jurisdiction of  
incorporation or organization)

11-2238111  
(I.R.S. Employer  
Identification No.)

3475 Victory Boulevard, Staten Island, New York 10314  
(Address of principal executive offices) (Zip Code)

**(718) 832-0800**  
(Registrant's telephone number including area code)

N/A

*(Former name, former address and former fiscal year, if changed from last report)*

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such 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, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date.

**5,863,302 shares of common stock, par value \$0.001 per share, are outstanding at March 4, 2017.**

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**PART I****ITEM 1 – FINANCIAL STATEMENTS.****COFFEE HOLDING CO., INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****JANUARY 31, 2017 AND OCTOBER 31, 2016**

	January 31, 2017	October 31, 2016
	<b>(Unaudited)</b>	
<b>- ASSETS -</b>		
<b>CURRENT ASSETS:</b>		
Cash	\$2,836,101	\$3,227,981
Accounts receivable, net of allowances of \$144,000 for 2017 and 2016	11,202,600	13,517,892
Inventories	14,483,524	14,276,290
Prepaid green coffee	506,983	435,577
Prepaid expenses and other current assets	456,116	535,456
Prepaid and refundable income taxes	284,599	481,977
Due from broker	173,671	134,722
Deferred income tax asset	116,731	81,545
<b>TOTAL CURRENT ASSETS</b>	<b>30,060,325</b>	<b>32,691,440</b>
Machinery and equipment, at cost, net of accumulated depreciation of \$4,996,541 and \$4,819,828 for 2017 and 2016, respectively	2,348,274	2,269,863
Customer list and relationships, net of accumulated amortization of \$53,625 and \$50,250 for the periods ended January 31, 2017 and 2016, respectively	216,375	219,750
Trademarks	180,000	180,000
Goodwill	1,017,905	1,017,905
Equity method investments	96,917	95,598
Deposits and other assets	554,133	549,337
<b>TOTAL ASSETS</b>	<b>\$34,473,929</b>	<b>\$37,023,893</b>
<b>- LIABILITIES, REDEEMABLE COMMON STOCK AND STOCKHOLDERS' EQUITY -</b>		
<b>CURRENT LIABILITIES:</b>		
Accounts payable and accrued expenses	\$3,302,535	\$4,062,573
Line of credit	4,758,475	6,958,375
Income taxes payable	2,272	1,050
<b>TOTAL CURRENT LIABILITIES</b>	<b>8,063,282</b>	<b>11,021,998</b>

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Deferred income tax liabilities	166,731	167,470
Deferred rent payable	233,508	231,216
Deferred compensation payable	499,563	489,668
<b>TOTAL LIABILITIES</b>	<b>8,963,084</b>	<b>11,910,352</b>
Redeemable common stock:		
Common stock subject to possible redemption, at \$200,004; 38,364 shares issued and outstanding at redemption value as of January 31, 2017 and October 31, 2016	200,004	200,004
<b>STOCKHOLDERS' EQUITY:</b>		
Coffee Holding Co., Inc. stockholders' equity:		
Preferred stock, par value \$.001 per share; 10,000,000 shares authorized; no shares issued and outstanding	-	-
Common stock, par value \$.001 per share; 30,000,000 shares authorized, 6,494,680 shares issued; 5,824,938 shares outstanding as of January 31 2017 and October 31, 2016	6,456	6,456
Additional paid-in capital	15,904,109	15,904,109
Retained earnings	12,254,010	11,878,228
Less: Treasury stock, 631,378 common shares, at cost as of January 31, 2017 and October 31, 2016	(3,249,590 )	(3,249,590 )
Total Coffee Holding Co., Inc. Stockholders' Equity	24,914,985	24,539,203
Noncontrolling interest	395,856	374,334
<b>TOTAL EQUITY</b>	<b>25,310,841</b>	<b>24,913,537</b>
<b>TOTAL LIABILITIES, REDEEMABLE COMMON STOCK AND STOCKHOLDERS' EQUITY</b>	<b>\$34,473,929</b>	<b>\$37,023,893</b>

See notes to Condensed Consolidated Financial Statements

**COFFEE HOLDING CO., INC.****CONDENSED CONSOLIDATED STATEMENTS OF INCOME****THREE MONTHS ENDED JANUARY 31, 2017 AND 2016****(Unaudited)**

	January 31, 2017	January 31, 2016
NET SALES	\$ 19,632,367	\$ 22,805,397
<b>COST OF SALES</b> (which include purchases of approximately \$.8 million and \$3.5 million for the three months ended January 31, 2017 and 2016, respectively, from a related party)	16,500,776	20,154,348
GROSS PROFIT	3,131,591	2,651,049
OPERATING EXPENSES:		
Selling and administrative	2,350,591	1,676,960
Officers' salaries	168,590	163,850
TOTAL	2,519,181	1,840,810
INCOME FROM OPERATIONS	612,410	810,239
OTHER INCOME (EXPENSE):		
Interest income	12,431	10,012
Gain (Loss) from equity method investments	1,319	(456 )
Interest expense	(57,742 )	(39,803 )
TOTAL	(43,992 )	(30,247 )
INCOME BEFORE PROVISION FOR INCOME TAXES AND NON-CONTROLLING INTEREST IN SUBSIDIARY	568,418	779,992
Provision for income taxes	171,113	302,564
NET INCOME BEFORE NON-CONTROLLING INTEREST IN SUBSIDIARY	397,305	477,428
Less: net income attributable to the non-controlling interest in subsidiary	(21,523 )	(37,859 )
NET INCOME ATTRIBUTABLE TO COFFEE HOLDING CO., INC.	\$ 375,782	\$ 439,569
Basic and diluted earnings per share	\$ 0.06	\$ 0.07
Weighted average common shares outstanding:		
Basic and diluted	5,863,302	6,162,207

See notes to Condensed Consolidated Financial Statements

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**COFFEE HOLDING CO., INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****THREE MONTHS ENDED JANUARY 31, 2017 AND 2016****(Unaudited)**

	January 31, 2017	January 31, 2016
<b>OPERATING ACTIVITIES:</b>		
Net income	\$397,305	\$477,428
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	180,090	135,402
Unrealized (gain) loss on commodities	(38,949 )	(1,551 )
(Gain) loss on equity method investments	(1,319 )	457
Deferred rent	2,292	2,290
Deferred income taxes	(35,925 )	634,850
Changes in operating assets and liabilities:		
Accounts receivable	2,315,292	(302,810 )
Inventories	(207,234 )	1,982,683
Prepaid expenses and other current assets	79,340	10,940
Prepaid green coffee	(71,406 )	46,872
Prepaid and refundable income taxes	197,378	257,850
Refund receivable		(613,438 )
Accounts payable and accrued expenses	(760,039 )	1,157,215
Deposits and other assets	5,099	
Income taxes payable	1,222	250
Net cash provided by operating activities	2,063,146	3,788,438
<b>INVESTING ACTIVITIES:</b>		
Purchases of machinery and equipment	(255,126 )	(214,930 )
Net cash used in investing activities	(255,126 )	(214,930 )
<b>FINANCING ACTIVITIES:</b>		
Advances under bank line of credit	1,000,100	600,000
Payment of dividend	-	(100,000 )
Principal payments under bank line of credit	(3,200,000)	(2,000,000)
Net cash used in financing activities	(2,199,900)	(1,500,000)
<b>NET (DECREASE) INCREASE IN CASH</b>	<b>(391,880 )</b>	<b>2,073,508</b>
<b>CASH, BEGINNING OF PERIOD</b>	<b>3,227,981</b>	<b>3,853,816</b>
<b>CASH, END OF PERIOD</b>	<b>\$2,836,101</b>	<b>\$5,927,324</b>

January	January
31,	31,
2017	2016

SUPPLEMENTAL DISCLOSURE OF CASH FLOW DATA:

Interest paid	\$61,823	\$72,463
Income taxes paid	\$3,846	\$23,052

See notes to Condensed Consolidated Financial Statements

**COFFEE HOLDING CO., INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 1 - BUSINESS ACTIVITIES:**

Coffee Holding Co., Inc. (the “Company”) conducts wholesale coffee operations, including manufacturing, roasting, packaging, marketing and distributing roasted and blended coffees for private labeled accounts and its own brands, and it sells green coffee. The Company also manufactures and sells coffee roasters. The Company’s core product, coffee, can be summarized and divided into three product categories (“product lines”) as follows:

***Wholesale Green Coffee:*** unroasted raw beans imported from around the world and sold to large and small roasters and coffee shop operators;

***Private Label Coffee:*** coffee roasted, blended, packaged and sold under the specifications and names of others, including supermarkets that want to have their own brand name on coffee to compete with national brands; and

***Branded Coffee:*** coffee roasted and blended to the Company’s own specifications and packaged and sold under the Company’s eight proprietary and licensed brand names in different segments of the market.

The Company’s private label and branded coffee sales are primarily to customers that are located throughout the United States with limited sales in Canada and certain countries in Asia. Such customers include supermarkets, wholesalers, and individually-owned and multi-unit retailers. The Company’s unprocessed green coffee, which includes over 90 specialty coffee offerings, is sold primarily to specialty gourmet roasters and to coffee shop operators in the United States with limited sales in Australia, Canada, England and China.

The Company’s wholesale green, private label, and branded coffee product categories generate revenues and cost of sales individually but incur selling, general and administrative expenses in the aggregate. There are no individual product managers and discrete financial information is not available for any of the product lines. The Company’s product portfolio is used in one business and it operates and competes in one business activity and economic environment. In addition, the three product lines share customers, manufacturing resources, sales channels, and marketing support. Thus, the Company considers the three product lines to be one single reporting segment.

**NOTE 2 - BASIS OF PRESENTATION:**

The following (a) condensed consolidated balance sheet as of October 31, 2016, which has been derived from audited financial statements, and (b) the unaudited interim condensed financial statements have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (the "SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles ("U.S. GAAP") have been condensed or omitted pursuant to those rules and regulations, although the Company believes that the disclosures made are adequate to make the information not misleading. It is suggested that these condensed consolidated financial statements be read in conjunction with the consolidated financial statements and the notes thereto included in the Company's latest shareholders' annual report on Form 10-K filed with the SEC on January 27, 2017 for the fiscal year ended October 31, 2016 ("Form 10-K").

In the opinion of management, all adjustments (which include normal and recurring nature adjustments) necessary to present a fair statement of the Company's financial position as of January 31, 2017, and results of operations for the three months ended January 31, 2017 and the cash flows for the three months ended January 31, 2017 as applicable, have been made.

**COFFEE HOLDING CO., INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 2 - BASIS OF PRESENTATION (cont'd):**

The results of operations for the three months ended January 31, 2017 are not necessarily indicative of the operating results for the full fiscal year or any future periods.

The condensed consolidated financial statements include the accounts of the Company, the Company's subsidiaries, Organic Products Trading Company, LLC ("OPTCO") and Sonofresco, LLC ("SONO") and Generations Coffee Company, LLC ("GCC"), the entity formed as a result of the Company's joint venture with Caruso's Coffee, Inc. The Company owns a 60% equity interest in GCC. All significant inter-company transactions and balances have been eliminated in consolidation.

**NOTE 3 - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS AFFECTING THE COMPANY:**

The FASB has issued ASU No. 2015-17, *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*, which changes how deferred taxes are classified on organizations' balance sheets.

The ASU eliminates the current requirement for organizations to present deferred tax liabilities and assets as current and noncurrent in a classified balance sheet. Instead, organizations will be required to classify all deferred tax assets and liabilities as noncurrent. The amendments apply to all organizations that present a classified balance sheet. For public companies, the amendments are effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods. For private companies, not-for-profit organizations, and employee benefit plans, the amendments are effective for financial statements issued for annual periods beginning after December 15, 2017, and interim periods within annual periods beginning after December 15, 2018. The adoption of this standard is not expected to have a material impact on the Company's consolidated financial position and results of operations.

In July 2015, the FASB issued ASU 2015-11, "Inventory (Topic 330): Simplifying the Measurement of Inventory," which applies to inventory that is measured using first-in, first-out ("FIFO") or average cost. Under the updated guidance, an entity should measure inventory that is within scope at the lower of cost and net realizable value, which is the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. Subsequent measurement is unchanged for inventory that is measured using last-in,

last-out (“LIFO”). This ASU is effective for annual and interim periods beginning after December 15, 2016, and should be applied prospectively with early adoption permitted at the beginning of an interim or annual reporting period. The Company is currently evaluating the impact of adopting this guidance.

The FASB issued ASU 2016-02, Leases (Topic 842). ASU 2016-01 requires that a lessee recognize the assets and liabilities that arise from operating leases. 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. For leases with a term of 12 months or less, a lessee is permitted to make an accounting policy election by class of underlying asset not to recognize lease assets and lease liabilities. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach.

**COFFEE HOLDING CO., INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 3 - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS AFFECTING THE COMPANY  
(cont'd):**

Public business entities should apply the amendments in ASU 2016-02 for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years (i.e., January 1, 2019, for a calendar year entity). Nonpublic business entities should apply the amendments for fiscal years beginning after December 15, 2019 (i.e., January 1, 2020, for a calendar year entity), and interim periods within fiscal years beginning after December 15, 2020. Early application is permitted for all public business entities and all nonpublic business entities upon issuance. The Company is currently evaluating the impact of adopting this guidance.

On March 17, 2016 the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2016-08 that amends the guidance for *Principle versus Agent Considerations (Reporting Revenue Gross versus Net)* in ASC 2014-09, *Revenue from Contracts with Customers (Topic 606)*, issued in May 2014. The ASU clarifies that the principal or agent determination is based on whether the entity controls the goods or services before they are transferred to its customer. Public entities must apply ASU 2016-08 to annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. Nonpublic entities will be required to adopt the amendments for annual reporting periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019. Earlier application is permitted for both types of entities only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period. Early adoption prior to that date is not permitted. The Company is evaluating the effect that ASU 2016-08 will have on its results of operations, financial position or cash flows.

In May 2014 the FASB issued ASU 2014-09, *Revenue from Contracts with Customers*, which is a new standard related to revenue recognition. Under the new standard, recognition of revenue occurs when a customer obtains control of promised services or goods in an amount that reflects the consideration to which the entity expects to receive in exchange for those goods or services. In addition, the standard requires disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from customer contracts. The standard must be adopted using either a full retrospective approach for all periods presented in the period of adoption or a modified retrospective approach. In July 2015, the FASB issued ASU 2015-14, *Revenue from Contracts with Customers - Deferral of the Effective Date*, which defers the implementation of this new standard to be effective for fiscal years beginning after December 15, 2017. Early adoption is permitted effective January 1, 2017. In March 2016, the FASB issued ASU 2016-08, *Principal versus Agent Considerations*, which clarifies the implementation guidance on principal versus agent considerations in the new revenue recognition standard pursuant to ASU 2014-09. In April 2016, the FASB issued ASU 2016-10, *Identifying Performance Obligations and Licensing*, and in May 2016, the FASB issued ASU 2016-12, *Narrow-Scope Improvements and Practical Expedients*, which amend certain aspects of the new revenue recognition standard pursuant to ASU 2014-09. We are currently evaluating which transition

approach we will utilize and the impact of adopting this accounting standard on our financial statements.

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**COFFEE HOLDING CO., INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 4 - PREPAID GREEN COFFEE:**

The balance represents advance payments made by OPTCO to several coffee growing cooperatives for the purchase of green coffee. Interest is charged to the cooperatives for these advances. Interest earned was \$12,431 and \$10,012 for the three months ended January 31, 2017 and 2016, respectively. The prepaid coffee balance was \$506,983 at January 31, 2017 and \$435,577 at October 31, 2016.

**NOTE 5 - ACCOUNTS RECEIVABLE:**

Trade accounts receivable are stated at the amount the Company expects to collect. The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. Management considers the following factors when determining the collectability of specific customer accounts: customer credit-worthiness, past transaction history with the customer, current economic industry trends, and changes in customer payment terms. Past due balances over 60 days and other higher risk amounts are reviewed individually for collectability. If the financial condition of the Company's customers were to deteriorate, adversely affecting their ability to make payments, additional allowances would be required. Based on management's assessment, the Company provides for estimated uncollectible amounts through a charge to earnings and a credit to a valuation allowance. Balances that remain outstanding after the Company has used reasonable collection efforts are written off through a charge to the valuation allowance and a credit to accounts receivable.

The reserve for sales discounts represents the estimated discount that customers will take upon payment. The reserve for other allowances represents the estimated amount of returns, slotting fees and volume based discounts estimated to be incurred by the Company from its customers. The allowances are summarized as follows:

	January 31, 2017	October 31, 2016
Allowance for doubtful accounts	\$65,000	\$65,000
Reserve for other allowances	35,000	35,000
Reserve for sales discounts	44,000	44,000
Totals	\$144,000	\$144,000



**COFFEE HOLDING CO., INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 6 - INVENTORIES:**

Inventories at January 31, 2017 and October 31, 2016 consisted of the following:

	January 31, 2017	October 31, 2016
Packed coffee	\$2,193,257	\$1,804,633
Green coffee	11,020,336	11,434,024
Roasters and parts	215,009	210,007
Packaging supplies	1,054,922	827,626
Totals	\$14,483,524	\$14,276,290

**NOTE 7 - COMMODITIES HELD BY BROKER:**

The Company has used, and intends to continue to use in a limited capacity, short term coffee futures and options contracts primarily for the purpose of partially hedging and minimizing the effects of changing green coffee prices and to reduce our cost of sales. The commodities held at broker represent the market value of the Company's trading account, which consists of options and future contracts for coffee held with a brokerage firm. The Company uses options and futures contracts, which are not designated or qualifying as hedging instruments, to partially hedge the effects of fluctuations in the price of green coffee beans. Options and futures contracts are recognized at fair value in the condensed consolidated financial statements with current recognition of gains and losses on such positions. The Company's accounting for options and futures contracts may increase earnings volatility in any particular period.

The Company has open position contracts held by the broker, which are summarized as follows:

January 31, 2017	October 31, 2016
---------------------	---------------------

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Option Contracts	\$34,711	\$(83,753 )
Future Contracts	138,960	218,475
Total Commodities	\$173,671	\$134,722

The Company classifies its options and future contracts as trading securities and accordingly, unrealized holding gains and losses are included in earnings and not reflected as a net amount as a separate component of stockholders' equity.

At January 31, 2017, the Company held 39 futures contracts (generally with terms of three to four months) for the purchase of 1,462,500 pounds of green coffee at a weighted average price of \$1.44 per pound. The fair market value of coffee applicable to such contracts was \$1.49 per pound at that date. At January 31, 2017, the Company did not have any options.

At October 31, 2016, the Company held 22 futures contracts (generally with terms of three to four months) for the purchase of 825,000 pounds of green coffee at a weighted average price of \$1.45 per pound. The fair market value of coffee applicable to such contracts was \$1.64 per pound at that date. At October 31, 2016, the Company did not have any options.

The Company recorded realized and unrealized gains and losses respectively, on these contracts as follows:

**COFFEE HOLDING CO., INC.****NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 7 - COMMODITIES HELD BY BROKER (cont'd):**

	Three Months Ended	
	January 31,	
	2017	2016
Gross realized gains	\$405,259	\$120,599
Gross realized losses	(460,018)	(532,372)
Unrealized gain	38,948	1,551
Total	\$(15,811)	\$(410,222)

**NOTE 8 - LINE OF CREDIT:**

On March 10, 2015, the Company entered into a loan modification agreement (the "Modification Agreement") with its lender Sterling National Bank ("Sterling") which modified the terms of the financing agreement with Sterling previously entered into on February 17, 2009 (the "Financing Agreement"). Prior to the Modification Agreement, the Financing Agreement, as amended, provided for a credit facility in which the Company had a revolving line of credit for a maximum of \$7,000,000 (the "Loan Facility"). On February 3, 2011, the Company amended the Financing Agreement to create a sublimit within the revolving line of credit in the form of a \$300,000 term loan for the benefit of GCC. The Financing Agreement was set to expire on March 31, 2015. Pursuant to the Modification Agreement, the Financing Agreement was modified to, among other things, (i) extend the term of the Financing Agreement until February 28, 2017; (ii) increase the maximum amount of the Loan Facility from \$7,000,000 to \$9,000,000; (iii) reduce the interest rate on the average unpaid balance of the line of credit from an interest rate equal to a per annum reference rate of 3.75% to an interest rate per annum equal to the Wall Street Journal Prime Rate; and (iv) require the Company to pay, upon the occurrence of certain termination events, a prepayment premium of 0.50% of the maximum amount of the credit facility in effect as of the date of the termination event. The line has been extended until March 31, 2017. The Company is currently negotiating the terms of a new facility with Sterling and the Company expects to enter into a new facility on or before March 31, 2017 or extend the line further until the terms of the new facility have been finalized.

Other than as described above, the Financing Agreement remains in full force and effect. Pursuant to the Modification Agreement, the Company is able to draw on the loan Facility up to an amount of 85% of eligible accounts receivable and 25% of eligible inventory consisting of green coffee beans and finished coffee not to exceed \$1,000,000. The Loan Facility is secured by all tangible and intangible assets of the Company.

The Loan Facility contains covenants that place annual restrictions on our operations, including covenants related to debt restrictions, capital expenditures, minimum deposit restrictions, tangible net worth, net profit, leverage, employee loan restrictions, distribution restrictions (common stock and preferred stock), dividend restrictions, and restrictive transactions. The Loan Facility also requires that the Company maintain a minimum working capital at all times. The Company was in compliance with all required financial covenants at January 31, 2017 and October 31, 2016.

As of January 31, 2017 and October 31, 2016, the outstanding balance under the bank line of credit was \$2,921,475 and \$5,121,375, respectively.

Also on March 10, 2015, the Company, as guarantor, and OPTCO (the “Borrower”), as borrower, entered into a new loan facility agreement with Sterling. The new loan facility is a revolving line of credit for a maximum of \$3,000,000 (the “New Loan Facility”). The New Loan Facility was set to expire on February 28, 2017 but has been extended until March 31, 2017. The Company is currently negotiating the terms of a new facility with Sterling and the Company expects to enter into a new facility on or before March 31, 2017 or extend the line further until the terms of the new facility have been finalized. The Borrower is able to draw on the New Loan Facility at an amount up to 85% of eligible accounts receivable, not to exceed 25% of all accounts of the Borrower. The New Loan Facility is payable monthly in arrears on the average unpaid balance of the line of credit at an interest rate per annum equal to the Wall Street Journal Prime Rate (currently 3.5%). The New Loan Facility is secured by all tangible and intangible assets of the Company. In connection with the New Loan Facility, the Company entered into a security agreement with Sterling and provided Sterling with a guarantee of the Borrower’s obligations. As of January 31, 2017 and October 31, 2016, the outstanding balance under the New Loan Facility was \$1,837,000.

**COFFEE HOLDING CO., INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 9 - INCOME TAXES:**

The Company accounts for income taxes pursuant to the asset and liability method which requires deferred income tax assets and liabilities to be computed for temporary differences between the financial statement and tax basis of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax laws and rates applicable to the periods in which the differences are expected to affect taxable income. Valuation allowances are established when necessary to reduce deferred tax assets to the amount expected to be realized. The income tax provision or benefit is the tax incurred for the period plus or minus the change during the period in deferred tax assets and liabilities.

The Company adopted FASB authoritative guidance for accounting for uncertainty in income taxes. As of January 31, 2017 and October 31, 2016, the Company did not have any unrecognized tax benefits or open tax positions. The Company's practice is to recognize interest and/or penalties related to income tax matters in income tax expense. As of January 31, 2017 and October 31, 2016, the Company had no accrued interest or penalties related to income taxes. The Company currently has no federal or state tax examinations in progress.

The Company files a U.S. federal income tax return and California, Colorado, New Jersey, New York, Kansas, Oregon, Rhode Island, South Carolina, Rhode Island, Virginia, Connecticut, Michigan and Texas state tax returns. The Company's federal income tax return is no longer subject to examination by the federal taxing authority for the years before fiscal 2013. The Company's California, Colorado and New Jersey income tax returns are no longer subject to examination by their respective taxing authorities for the years before fiscal 2010. The Company's Oregon and New York income tax returns are no longer subject to examination by their respective taxing authorities for the years before fiscal 2011.

**NOTE 10 - EARNINGS PER SHARE:**

The Company presents "basic" and "diluted" earnings per common share pursuant to the provisions included in the authoritative guidance issued by FASB, "Earnings per Share," and certain other financial accounting pronouncements. Basic earnings per common share were computed by dividing net income by the sum of the weighted-average number of common shares outstanding. Diluted earnings per common share is computed by dividing the net income by the weighted-average number of common shares outstanding plus the dilutive effect of common shares issuable upon exercise of potential sources of dilution.

The weighted average common shares outstanding used in the computation of basic and diluted earnings per share were 5,863,302 and 6,162,207 for the three months ended January 31, 2017 and 2016, respectively.

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**COFFEE HOLDING CO., INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 11 - ECONOMIC DEPENDENCY:**

Approximately 28% of the Company's sales were derived from four customers during the three months ended January 31, 2017. These customers also accounted for approximately \$3,744,000 of the Company's accounts receivable balance at January 31, 2017. Approximately 38% of the Company's sales were derived from one customer during the three months ended January 31, 2016. This customer also accounted for approximately \$3,942,000 of the Company's accounts receivable balance at January 31, 2016. Concentration of credit risk with respect to other trade receivables is limited due to the short payment terms generally extended by the Company, by ongoing credit evaluations of customers, and by maintaining an allowance for doubtful accounts that management believes will adequately provide for credit losses.

For the three months ended January 31, 2017, approximately 22% of the Company's purchases were from four vendors. These vendors accounted for approximately \$518,000 of the Company's accounts payable at January 31, 2017. For the three months ended January 31, 2016, approximately 52% of the Company's purchases were from four vendors. These vendors accounted for approximately \$3,348,000 of the Company's accounts payable at January 31, 2016. Management does not believe the loss of any one vendor would have a material adverse effect of the Company's operations due to the availability of many alternate suppliers.

**NOTE 12 - RELATED PARTY TRANSACTIONS:**

The Company has engaged its 40% partner in GCC as an outside contractor (the "Partner"). Included in contract labor expense are expenses incurred from the Partner during the three months ended January 31, 2017 and 2016 of \$111,062 and \$75,018, respectively, for the processing of finished goods.

An employee of one of the top four vendors is a director of the Company. Purchases from that vendor totaled approximately \$835,000 and \$3,533,000 for the three months ended January 31, 2017 and 2016, respectively. The corresponding accounts payable balance to this vendor was approximately \$0 and \$1,110,000 at January 31, 2017 and 2016, respectively.

In January 2005, the Company established the "Coffee Holding Co., Inc. Non-Qualified Deferred Compensation Plan." Currently, there is only one participant in the plan: Andrew Gordon, the Company's Chief Executive Officer. Within the plan guidelines, this employee is deferring a portion of his current salary and bonus. The assets are held in a separate trust. The deferred compensation payable represents the liability due to an officer of the Company. The

assets are included in the Deposits and other assets in the accompanying balance sheets. The deferred compensation asset and liability at January 31, 2017 and October 31, 2016 were \$499,563 and \$489,668, respectively.

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**COFFEE HOLDING CO., INC.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**JANUARY 31, 2017 AND 2016**

(Unaudited)

**NOTE 13 - STOCKHOLDERS' EQUITY:**

*Treasury Stock.* The Company utilizes the cost method of accounting for treasury stock. The cost of reissued shares is determined under the last-in, first-out method. The Company did not purchase any shares during the three months ended January 31, 2017. The Company purchased 337,269 shares for \$1,754,878 during the year ended October 31, 2016.

*Share Repurchase Program.* On January 24, 2014, the Company announced that the Board of Directors had approved a share repurchase program (the "2014 Share Repurchase Program") pursuant to which the Company may repurchase up to \$1 million of its outstanding shares of common stock from time to time on the open market and in privately negotiated transactions subject to market conditions, share price and other factors. The 2014 Share Repurchase Program may be discontinued or suspended at any time. The Company does not intend to make any further repurchases under the 2014 Share Repurchase Program and the 2014 Share Repurchase Program is terminated. As of October 31, 2016, pursuant to the terms of the 2014 Share Repurchase Program, the Company had repurchased 156,415 shares of outstanding common stock in an amount equal in value to \$995,729. On September 29, 2015, the Company announced that the Board of Directors had approved a share repurchase program (the "2015 Share Repurchase Program") pursuant to which the Company may repurchase up to \$2 million of the outstanding common stock from time to time on the open market and in privately negotiated transactions subject to market conditions, share price and other factors. The timing and amount of any shares repurchased will be determined based on the Company's evaluation of market conditions and other factors. The 2015 Share Repurchase Program may be discontinued or suspended at any time. Pursuant to the terms of the 2015 Share Repurchase Program, the Company purchased 337,269 shares during the year ended October 31, 2016 for \$1,754,878. Also pursuant to the terms of the 2015 Share Repurchase Program, the Company had repurchased 53,687 shares of outstanding common stock in an amount equal in value to \$226,850 during the year ended October 31, 2015.

**NOTE 15 - SUBSEQUENT EVENTS:**

On February 24, 2017, the Company acquired 100% of the capital stock of Comfort Foods, Inc. ("Comfort Foods"), a Massachusetts based medium sized coffee roaster, manufacturing both branded and private label coffee for retail and foodservice customers. The Company paid \$2.3 million in cash for 100% of the capital stock of Comfort Foods.

The initial accounting for the business combination is not yet complete, and the Company is still performing procedures to determine the appropriate accounting. As such, the Company is unable to make the following disclosures, (i) pro forma data, (ii) purchase price allocation, (iii) expenses of the acquisition, and (iv) revenue and earnings of the acquiree since the acquisition date.

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

### Cautionary Note on Forward-Looking Statements

Some of the matters discussed under the caption "Management's Discussion and Analysis of Financial Condition and Results of Operation" and elsewhere in this quarterly report include forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. We have based these forward-looking statements upon information available to management as of the date of this Form 10-Q and management's expectations and projections about future events, including, among other things:

- our dependency on a single commodity could affect our revenues and profitability;
- our success in expanding our market presence in new geographic regions;
- the effectiveness of our hedging policy may impact our profitability;
- the success of our joint ventures;
- our success in implementing our business strategy or introducing new products;
- our ability to attract and retain customers;
- our ability to obtain additional financing;
- the effects of competition from other coffee manufacturers and other beverage alternatives;
- the impact to the operations of our Colorado facility;
- general economic conditions and conditions which affect the market for coffee;
- the macro global economic environment;
- our ability to maintain and develop our brand recognition;
- the impact of rapid or persistent fluctuations in the price of coffee beans;
- fluctuations in the supply of coffee beans;
- the volatility of our common stock; and
- other risks which we identify in future filings with the Securities and Exchange Commission (the "SEC").

In some cases, you can identify forward-looking statements by terminology such as “may,” “should,” “could,” “predict,” “potential,” “continue,” “expect,” “anticipate,” “future,” “intend,” “plan,” “believe,” “estimate” and similar expressions (or the such expressions). Any or all of our forward looking statements in this quarterly report and in any other public statements we make may turn out to be wrong. They can be affected by inaccurate assumptions we might make or by known or unknown risks and uncertainties. Consequently, no forward-looking statement can be guaranteed. In addition, we undertake no responsibility to update any forward-looking statement to reflect events or circumstances, that occur after the date of this quarterly report.

## Overview

We are an integrated wholesale coffee roaster and dealer in the United States and one of the few coffee companies that offers a broad array of coffee products across the entire spectrum of consumer tastes, preferences and price points. As a result, we believe that we are well-positioned to increase our profitability and endure potential coffee price volatility throughout varying cycles of the coffee market and economic conditions.

Our operations have primarily focused on the following areas of the coffee industry:

- the sale of wholesale specialty green coffee;

- the roasting, blending, packaging and sale of private label coffee;

- the roasting, blending, packaging and sale of our eight proprietary brands of coffee; and

- sales of our tabletop coffee roasting equipment.

Our operating results are affected by a number of factors including:

- the level of marketing and pricing competition from existing or new competitors in the coffee industry;

- our ability to retain existing customers and attract new customers;

- our hedging policy;

- fluctuations in purchase prices and supply of green coffee and in the selling prices of our products; and

- our ability to manage inventory and fulfillment operations and maintain gross margins.

Our net sales are driven primarily by the success of our sales and marketing efforts and our ability to retain existing customers and attract new customers. For this reason, we have made, and will continue to evaluate, strategic decisions to invest in measures that are expected to increase net sales. These transactions include our acquisition of Premier Roasters, LLC, including equipment and a roasting facility in La Junta, Colorado, the addition of a west coast sales manager to increase sales of our private label and branded coffees to new customers, our joint venture with Caruso's Coffee, Inc. of Brecksville, Ohio, the transaction with OPTCO and our licensing arrangement with DTS8 Coffee Company, Ltd. On June 23, 2016, we formed our wholly-owned subsidiary, Sonofresco, LLC ("SONO"), a Delaware limited liability company. On June 29, 2016, we purchased through SONO, substantially all the assets, including equipment, inventory, customer list and relationships of Coffee Kinetics, LLC, a Washington limited liability company. On February 24, 2017, the Company acquired 100% of the capital stock of Comfort Foods, Inc. ("Comfort Foods"), a Massachusetts based medium sized coffee roaster, manufacturing both branded and private label coffee for retail and foodservice customers. The Company paid \$2.3 million in cash for 100% of the capital stock of Comfort Foods. We believe these efforts will allow us to expand our business.

Our net sales are affected by the price of green coffee. We purchase our green coffee from dealers located primarily within the United States. The dealers supply us with coffee beans from many countries, including Colombia, Mexico, Kenya, Indonesia, Brazil and Uganda. The supply and price of coffee beans are subject to volatility and are influenced by numerous factors which are beyond our control. For example, in Brazil, which produces approximately 40% of the world's green coffee, the coffee crops are historically susceptible to frost in June and July and drought in September, October and November. However, because we purchase coffee from a number of countries and are able to freely substitute one country's coffee for another in our products, price fluctuations in one country generally have not had a material impact on the price we pay for coffee. Accordingly, price fluctuations in one country generally have not had a material effect on our results of operations, liquidity and capital resources. Historically, because we generally have been able to pass green coffee price increases through to customers, increased prices of green coffee generally result in increased net sales.

The supply and price of coffee beans are subject to volatility and are influenced by numerous factors which are beyond our control. Historically, we have used, and intend to continue to use in a limited capacity, short-term coffee futures and options contracts primarily for the purpose of partially hedging the effects of changing green coffee prices. In addition, we acquired, and expect to continue to acquire, futures contracts with longer terms, generally three to four months, primarily for the purpose of guaranteeing an adequate supply of green coffee. Realized and unrealized gains or losses on options and futures contracts are reflected in our cost of sales. Gains on options and futures contracts reduce our cost of sales and losses on options and futures contracts increase our cost of sales. The use of these derivative financial instruments has generally enabled us to mitigate the effect of changing prices. We believe that, in normal economic times, our hedging policies remain a vital element to our business model not only in controlling our cost of sales, but also giving us the flexibility to obtain the inventory necessary to continue to grow our sales while trying to minimize margin compression during a time of historically high coffee prices. However, no strategy can entirely eliminate pricing risks and we generally remain exposed to losses on futures contracts when prices decline significantly in a short period of time, and we would generally remain exposed to supply risk in the event of non-performance by the counterparties to any of our futures contracts. Although we have had net gains on options and futures contracts in the past, we have incurred significant losses on options and futures contracts during some recent reporting periods. In these cases, our cost of sales has increased, resulting in a decrease in our profitability or increase in our losses. Such losses have and could in the future materially increase our cost of sales and materially decrease our profitability and adversely affect our stock price. See "Item 3, Quantitative and Qualitative Disclosures About Market

Risk. If our hedging policy is not effective, we may not be able to control our coffee costs, we may be forced to pay greater than market value for green coffee and our profitability may be reduced.” Failure to properly design and implement an effective hedging strategy may materially adversely affect our business and operating results. If the hedges that we enter do not adequately offset the risks of coffee bean price volatility or our hedges result in losses, our cost of sales may increase, resulting in a decrease in profitability or increased losses. As previously announced, as a result of the volatile nature of the commodities markets, we have and are continuing to scale back our use of hedging and short-term trading of coffee futures and options contracts, and intend to continue to use these practices in a limited capacity going forward.

### **Critical Accounting Policies and Estimates**

The preparation of financial statements and related disclosures in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Estimates are used for, but not limited to, the accounting for the allowance for doubtful accounts, inventories, assets held for sale, income taxes, commodities held and loss contingencies. Management bases its estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results could differ from these estimates under different assumptions or conditions.



We believe the following critical accounting policies, among others, may be impacted significantly by judgment, assumptions and estimates used in the preparation of the financial statements:

We recognize revenue in accordance with the relevant authoritative guidance. Revenue is recognized at the point title and risk of ownership transfers to its customers which is upon the shippers taking possession of the goods because i) title passes in accordance with the terms of the purchase orders and with our agreements with our customers, ii) any risk of loss is covered by the customers' insurance, iii) there is persuasive evidence of a sales arrangement, iv) the sales price is determinable and v) collection of the resulting receivable is reasonably assured. Thus, revenue is recognized at the point of shipment.

Our allowance for doubtful accounts is maintained to provide for losses arising from customers' inability to make required payments. If there is deterioration of our customers' credit worthiness and/or there is an increase in the length of time that the receivables are past due greater than the historical assumptions used, additional allowances may be required. For example, every additional one percent of our accounts receivable that becomes uncollectible, would decrease our operating income by approximately \$112,000 for the quarter ended January 31, 2017. The reserve for sales discounts represents the estimated discount that customers will take upon payment. The reserve for other allowances represents the estimated amount of returns, slotting fees and volume based discounts estimated to be incurred by us from our customers.

Inventories are stated at lower of cost (determined on a first-in, first-out basis) or market. Based on our assumptions about future demand and market conditions, inventories are subject to be written-down to market value. If our assumptions about future demand change and/or actual market conditions are less favorable than those projected, additional write-downs of inventories may be required. Each additional one percent of potential inventory writedown would have decreased operating income by approximately \$145,000 for the quarter ended January 31, 2017.

The commodities held at broker represent the market value of the Company's trading account, which consists of option and futures contracts for coffee held with a brokerage firm. We use options and futures contracts, which are not designated or qualifying as hedging instruments, to partially hedge the effects of fluctuations in the price of green coffee beans. Options and futures contracts are recognized at fair value in the consolidated financial statements with current recognition of gains and losses on such positions. We classify options and futures contracts as trading securities and accordingly, unrealized holding gains and losses are included in earnings. We record realized and unrealized gains and losses in our cost of sales in the statement of operations/income.

We account for income taxes in accordance with the relevant authoritative guidance. Deferred tax assets and liabilities are computed for temporary differences between the financial statement and tax basis of assets and liabilities that will result in taxable or deductible amounts in the future based on enacted tax rates in effect for the year in which the differences are expected to reverse. Deferred tax assets are reflected on the balance sheet when it is determined that it is more likely than not that the asset will be realized. Accordingly, our net deferred tax asset as of January 31, 2017 of \$116,731 may require a valuation allowance if we do not generate taxable income.

Our goodwill consists of the cost in excess of the fair market value of the acquired net assets of OPTCO and SONO, which has been integrated into a structure that does not provide the basis for separate reporting units. Consequently, we are a single reporting unit for goodwill impairment testing purposes. We also have intangible assets consisting of our customer list and relationships and trademarks acquired from OPTCO and SONO. At January 31, 2017 our balance sheet reflected goodwill and intangible assets as set forth below:

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	January 31, 2017
Customer list and relationships, net	\$216,375
Trademarks	180,000
Goodwill	1,017,905
	\$1,414,280

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Goodwill and the trademarks which are deemed to have indefinite lives are subject to annual impairment tests. Goodwill impairment tests require the comparison of the fair value and carrying value of reporting units. We assess the potential impairment of goodwill and intangible assets annually and on an interim basis whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Upon completion of such review, if impairment is found to have occurred, a corresponding charge will be recorded. The value assigned to the customer list and relationships is being amortized over a twenty year period.

Because the Company is a single reporting unit, the closing NASDAQ Capital Market price of our common stock as of the acquisition date was used as a basis to measure the fair value of goodwill. Goodwill and the intangible assets will be tested annually at the end of each fiscal year to determine whether they have been impaired. Upon completion of each annual review, there can be no assurance that a material charge will not be recorded. Impairment testing is required more often than annually if an event or circumstance indicates that an impairment or decline in value may have occurred.

### **Three Months Ended January 31, 2017 Compared to the Three Months Ended January 31, 2016**

**Net Sales.** Net sales totaled \$19,632,367 for the three months ended January 31, 2017, a decrease of \$3,173,030, or 13.9%, from \$22,805,397 for the three months ended January 31, 2016. The decrease in net sales reflects our reduced wholesale transactions with our largest wholesale green coffee customer of approximately \$7,645,000 which was partially offset by a gain of approximately \$4.4 million in sales of both branded and private label coffee to both new and existing customers.

**Cost of Sales.** Cost of sales for the three months ended January 31, 2017 was \$16,500,776, or 84.1% of net sales, as compared to \$20,154,348, or 88.4% of net sales, for the three months January 31, 2016. Cost of sales consists primarily of the cost of green coffee and packaging materials and realized and unrealized gains or losses on hedging activity. The decrease in cost of sales reflects lower commodity prices during the quarter and our reduced wholesale transactions with our largest wholesale green coffee customer.

**Gross Profit.** Gross profit for the three months ended January 31, 2017 was \$3,131,591, an increase of \$480,542 from \$2,651,049 for the three months ended January 31, 2016. Gross profit as a percentage of net sales increased to 16% for the three months ended January 31, 2017 from 11.6% for the three months ended January 31, 2016. The increase in gross profits was due to improved margins on our wholesale and roasted business.

**Operating Expenses.** Total operating expenses increased by \$678,371 to \$2,519,181 for the three months ended January 31, 2017 from \$1,840,810 for the three months ended January 31, 2016. The quarter ended January 31, 2017 included approximately \$245,000 of selling and administrative expenses from our subsidiary "SONO", which was not in

the January 31, 2016 numbers. Also, we incurred increases in shipping expenses of \$190,056, salary expense of \$69,534, commission expense of \$20,984, medical insurance expense of \$30,423, depreciation expense of \$22,439, professional fees of \$61,301 and bank charges of \$8,945. These increases are all the result of our reinvestment in our growth and expansion strategy.

**Other Income (Expense).** Other expense for the three months ended January 31, 2017 was \$43,992, an increase of \$13,745 from \$30,247 for the three months ended January 31, 2016. The increase in other expense was attributable to an increase in interest expense of \$17,939, partially offset by increases in interest income of \$2,419 and \$1,775 in our gain from our equity investments, during the three months ended January 31, 2017.

**Income Taxes.** Our provision for income taxes for the three months ended January 31, 2017 totaled \$171,113 compared to \$302,564 for the three months ended January 31, 2016. The change was attributable to the difference in the gain for the quarter ended January 31, 2017 versus the gain in the quarter ended January 31, 2016.

**Net Income.** We had net income of \$375,782 or \$0.06 per share basic and diluted, for the three months ended January 31, 2017 compared to net income of \$439,569, or \$0.07 per share basic and diluted for the three months ended January 31, 2016. The decrease in net income was due primarily to the reasons described above.

## **Liquidity and Capital Resources**

As of January 31, 2017, we had working capital of \$21,997,043, which represented a \$327,601 increase from our working capital of \$21,669,442 as of October 31, 2016, and total stockholders' equity of \$24,914,985 which increased by \$375,782 from our total stockholders' equity of \$24,539,203 as of October 31, 2016. Our working capital increased primarily due to increases of \$207,234 in inventories, \$71,406 in prepaid green coffee, \$38,949 in due from broker, \$35,186 in deferred tax asset and decreases of \$760,039 in accounts payable and accrued expenses and \$2,199,900 in our line of credit, which were partially offset by decreases of \$391,880 in cash, \$2,315,292 in accounts receivable, \$79,340 in prepaid expenses and other current assets, \$197,378 in prepaid income taxes. As of January 31, 2017, the outstanding balance on our line of credit was \$4,758,475 compared to \$6,958,375 as of October 31, 2016. Total stockholders' equity increased due to our net income.

On March 10, 2015, we entered into a loan modification agreement (the “Modification Agreement”) with our lender Sterling National Bank (“Sterling”) which modified the terms of the financing agreement with Sterling previously entered into on February 17, 2009 (the “Financing Agreement”). Prior to the Modification Agreement, the Financing Agreement, as amended, provided for a credit facility in which we had a revolving line of credit for a maximum of \$7,000,000 (the “Loan Facility”). On February 3, 2011, we amended the Financing Agreement to create a sublimit within the revolving line of credit in the form of a \$300,000 term loan for the benefit of GCC. The Financing Agreement was set to expire on March 31, 2015. Pursuant to the Modification Agreement, the Financing Agreement was modified to, among other things, (i) extend the term of the Financing Agreement until February 28, 2017; (ii) increase the maximum amount of the Loan Facility from \$7,000,000 to \$9,000,000; (iii) reduce the interest rate on the average unpaid balance of the line of credit from an interest rate equal to a per annum reference rate of 3.75% to an interest rate per annum equal to the Wall Street Journal Prime Rate; and (iv) require us to pay, upon the occurrence of certain termination events, a prepayment premium of 0.50% of the maximum amount of the credit facility in effect as of the date of the termination event. The line has been extended until March 31, 2017. We are currently negotiating the terms of a new facility with Sterling and we expect to enter into a new facility on or before March 31, 2017 or extend the line further until the terms of the new facility have been finalized.

Other than as described above, the Financing Agreement remains in full force and effect. Pursuant to the Modification Agreement, we are able to draw on the loan Facility up to an amount of 85% of eligible accounts receivable and 25% of eligible inventory consisting of green coffee beans and finished coffee not to exceed \$1,000,000. The Loan Facility is secured by all tangible and intangible assets of the Company.

The Loan Facility contains covenants that place annual restrictions on our operations, including covenants related to debt restrictions, capital expenditures, minimum deposit restrictions, tangible net worth, net profit, leverage, employee loan restrictions, distribution restrictions (common stock and preferred stock), dividend restrictions, and restrictive transactions. The Loan Facility also requires that we maintain a minimum working capital at all times. The Company was in compliance with all required financial covenants at January 31, 2017 and October 31, 2016.

As of January 31, 2017 and October 31, 2016, the outstanding balance under the bank line of credit was \$2,921,475 and \$5,121,375, respectively.

Also on March 10, 2015, we, as guarantor, and OPTCO (the “Borrower”), as borrower, entered into a new loan facility agreement with Sterling. The new loan facility is a revolving line of credit for a maximum of \$3,000,000 (the “New Loan Facility”). The New Loan Facility was set to expire on February 28, 2017 but has been extended until March 31, 2017. We are currently negotiating the terms of a new facility with Sterling and we expect to enter into a new facility on or before March 31, 2017 or extend the line further until the terms of the new facility have been finalized. The Borrower is able to draw on the New Loan Facility at an amount up to 85% of eligible accounts receivable, not to exceed 25% of all accounts of the Borrower. The New Loan Facility is payable monthly in arrears on the average unpaid balance of the line of credit at an interest rate per annum equal to the Wall Street Journal Prime Rate (currently 3.5%). The New Loan Facility is secured by all tangible and intangible assets of the Company. In connection with the New Loan Facility, the Company entered into a security agreement with Sterling and provided Sterling with a

guarantee of the Borrower's obligations.

As of January 31, 2017 and October 31, 2016, the outstanding balance under the New Loan Facility was \$1,837,000.

For the three months ended January 31, 2017, our operating activities provided net cash of \$2,063,146 as compared to the three months ended January 31, 2016 when operating activities provided net cash of \$3,788,438. The decreased cash flow from operations for the three months ended January 31, 2017 was primarily due to our net income of \$397,305, \$670,775 of deferred income taxes, \$1,982,683 of inventories and \$760,039 of accounts payable and accrued expenses.

For the three months ended January 31, 2017, our investing activities used net cash of \$255,126 as compared to the three months ended January 31, 2016 when net cash used by investing activities was \$214,930. The increase in our uses of cash in investing activities was due to our increased outlays for equipment during quarter ended January 31, 2017.

For the three months ended January 31, 2017, our financing activities used net cash of \$2,199,900 compared to net cash used in financing activities of \$1,500,000 for the three months ended January 31, 2016. The change in cash flow from financing activities for the three months ended January 31, 2017 was due to our increased principal payments on our line of credit of \$799,900.

We expect to fund our operations, including paying our liabilities, funding capital expenditures and making required payments on our indebtedness, through January 31, 2018 with cash provided by operating activities and the use of our credit facility. In addition, an increase in eligible accounts receivable and inventory would permit us to make additional borrowings under our line of credit.

### **Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements that have or are reasonably likely to have a current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

### **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

Market risks relating to our operations result primarily from changes in interest rates and commodity prices as further described below.

***Interest Rate Risks.*** We are subject to market risk from exposure to fluctuations in interest rates. As of January 31, 2017, our debt consisted of \$4,758,475 of variable rate debt under our revolving line of credit. Our line of credit provides for a maximum of \$12,000,000 and is payable monthly in arrears on the average unpaid balance of the line of credit at an interest rate equal to a per annum reference rate (currently 3.5%). This loan is secured by all tangible and intangible assets of the Company.

***Commodity Price Risks.*** The supply and price of coffee beans are subject to volatility and are influenced by numerous factors which are beyond our control. Historically, we have used, and intend to continue to use in a limited capacity, short-term coffee futures and options contracts primarily for the purpose of partially hedging the effects of changing green coffee prices, as further explained in Note 7 of the Notes to the Condensed Consolidated Financial Statements in this Report. In addition, we acquired, and expect to continue to acquire, futures contracts with longer terms, generally three to four months, primarily for the purpose of guaranteeing an adequate supply of green coffee. Realized and unrealized gains or losses on options and futures contracts are reflected in our cost of sales. Gains on options and futures contracts reduce our cost of sales and losses on options and futures contracts increase our cost of sales. The use of these derivative financial instruments has generally enabled us to mitigate the effect of changing prices. We believe that, in normal economic times, our hedging policies remain a vital element to our business model not only in controlling our cost of sales, but also giving us the flexibility to obtain the inventory necessary to continue to grow our sales while trying to minimize margin compression during a time of historically high coffee prices. However, no strategy can entirely eliminate pricing risks and we generally remain exposed to losses on futures contracts when prices decline significantly in a short period of time, and we would generally remain exposed to supply risk in the event of non-performance by the counterparties to any of our futures contracts. Although we have had net gains on

options and futures contracts in the past, we have incurred significant losses on options and futures contracts during some recent reporting periods. In these cases, our cost of sales has increased, resulting in a decrease in our profitability or increase our losses. Such losses have and could in the future materially increase our cost of sales and materially decrease our profitability and adversely affect our stock price. See “Item 1A – Risk Factors - If our hedging policy is not effective, we may not be able to control our coffee costs, we may be forced to pay greater than market value for green coffee and our profitability may be reduced” in our Annual Report on Form 10-K for the fiscal year ended October 31, 2016 filed with the SEC on January 27, 2017. Failure to properly design and implement an effective hedging strategy may materially adversely affect our business and operating results. If the hedges that we enter do not adequately offset the risks of coffee bean price volatility or our hedges result in losses, our cost of sales may increase, resulting in a decrease in profitability or increased losses. As previously announced, as a result of the volatile nature of the commodities markets, we have and are continuing to scale back our use of hedging and short-term trading of coffee futures and options contracts, and intend to continue to use these practices in a limited capacity going forward.

At January 31, 2017, the Company held 39 futures contracts (generally with terms of three to four months) for the purchase of 1,462,500 pounds of green coffee at a weighted average price of \$1.44 per pound. The fair market value of coffee applicable to such contracts was \$1.49 per pound at that date. At January 31, 2017, the Company did not have any options.

At October 31, 2016, the Company held 22 futures contracts (generally with terms of three to four months) for the purchase of 825,000 pounds of green coffee at a weighted average price of \$1.45 per pound. The fair market value of coffee applicable to such contracts was \$1.64 per pound at that date. At October 31, 2016, the Company did not have any options.



#### **ITEM 4. CONTROLS AND PROCEDURES**

Management, which includes our President, Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) as of the end of the period covered by this report. Based upon that evaluation, our President, Chief Executive Officer and Chief Financial Officer concluded that the disclosure controls and procedures were effective to ensure that information required to be disclosed in the reports that we file and submit under the Exchange Act is (i) recorded, processed, summarized and reported as and when required and (ii) accumulated and communicated, as is appropriate, to our management, including our principal executive officer and financial officer to allow timely decisions regarding required disclosure.

There have been no changes in our internal control over financial reporting identified in connection with the evaluation that occurred during our last fiscal quarter that has materially affected, or that is reasonably likely to materially affect, our internal control over financial reporting.

**PART II - OTHER INFORMATION**

**ITEM 1. LEGAL PROCEEDINGS.**

We are not a party to, and none of our property is the subject of, any pending legal proceedings other than routine litigation that is incidental to our business. To our knowledge, no governmental authority is contemplating initiating any such proceedings.

**ITEM 1A. RISK FACTORS.**

There were no material changes during the quarter ended January 31, 2017 to the Risk Factors disclosed in Item 1A “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended October 31, 2016 filed with the SEC on January 27, 2017.

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

None.

**ITEM 3. DEFAULTS UPON SENIOR SECURITIES.**

None.

**ITEM 4. MINE SAFETY DISCLOSURES.**

None.

**ITEM 5. OTHER INFORMATION.**

None.

**ITEM 6. EXHIBITS.**

- 31.1 Principal Executive Officer and Principal Financial Officer's Certification furnished pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32.1 Principal Executive Officer and Principal Financial Officer's Certification furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

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**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 and in the capacities indicated on March 17, 2017.

**Coffee Holding Co., Inc.**

Date: March 17, 2017 By: */s/ Andrew Gordon*

Andrew Gordon President

Chief Executive Officer and Chief Financial Officer

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