INTERSTATE BAKERIES CORPORATION

Building for the future

1999 Annual Report

Interstate Bakeries Corporation is the largest wholesale baker and distributor of fresh delivered bread and snack cakes in the United States. The Company has three major divisions — the Western Division, headquartered in Phoenix, Arizona; the Central Division, headquartered in Kansas City, Missouri; and the Eastern Division, headquartered in Charlotte, North Carolina. The Company also sells dry products.

The Company operates 67 bakeries throughout the United States and employs more than 34,000 people. From these strategically dispersed bakeries, the Company's sales force delivers baked goods to more than 200,000 food outlets on approximately 11,000 delivery routes. The Company's products are distributed throughout the United States, primarily through its direct route system and approximately 1,500 Company-operated thrift stores, and to some extent through distributors.

The IBC product line is marketed under a number of well-known national and regional brands, which include *Wonder, Hostess, Home Pride, Drake's, Beefsteak, Bread du Jour, Dolly Madison, Butternut, Merita, Parisian, Colombo, Sunbeam, Millbrook, Eddy's, Holsum, Sweetheart, Cotton's Holsum, J.J. Nissen, Marie Callender's* and *Mrs. Cubbison's*. In addition, the Company is a baker and distributor of *Roman Meal* and *Sun Maid* bread.

Financial Highlights

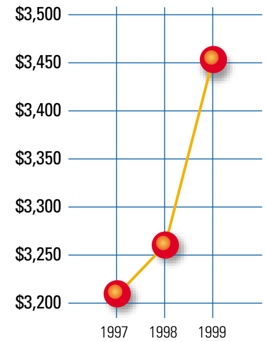
(In Thousands, Except Per Share Data)

	52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Statement of Income			
Net sales	$3,459,377	$3,265,842	$3,212,431
Operating income	224,477	231,592	191,143
% of net sales	6.5%	7.1%	6.0%
Net income	$ 126,155	$ 127,924	$ 97,177
% of net sales	3.6%	3.9%	3.0%
Per common share[1]:			
Net income (diluted basis)	$ 1.74	$ 1.71	$ 1.28
Book value	8.60	7.77	7.17
Common stock dividends	.28	.28	.27
Average diluted shares outstanding[1]	72,483	74,845	76,200

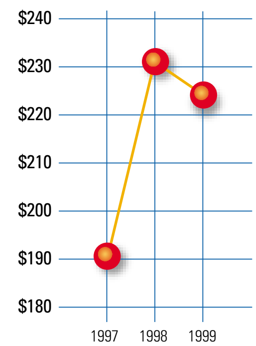
	May 29, 1999	May 30, 1998	May 31, 1997
Balance Sheet			
Total assets	$1,680,775	$1,549,986	$1,493,087
Long-term debt	369,000	261,000	251,000
Stockholders' equity	603,803	565,155	538,722
Debt to total capital	37.9%	31.6%	31.8%

(1) All per share and average shares outstanding amounts reflect a November 1997 two-for-one stock split.

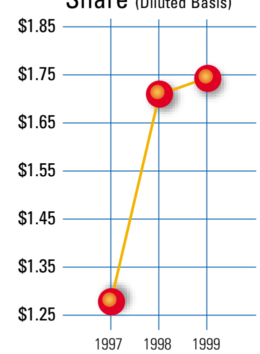
Net Sales
(In Millions)



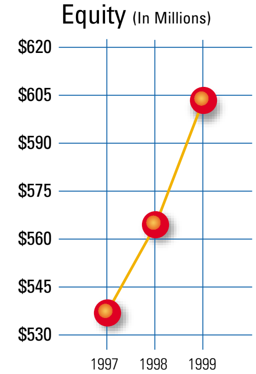
Operating Income
(In Millions)



Earnings Per Share (Diluted Basis)



Stockholders' Equity (In Millions)



Common Stock Information

The Company's common stock is listed on the New York Stock Exchange and is traded under the symbol IBC. The table below presents the high and low sales prices for the stock and cash dividends paid during fiscal 1999 and 1998:

Fiscal Year	Quarter	Stock Price High	Stock Price Low	Cash Dividends
1999	1	$34.8125	$24.8750	$ .0700
	2	34.0625	25.0000	.0700
	3	27.1875	23.2500	.0700
	4	23.5625	21.1875	.0700
1998	1	$32.1875	$27.3125	$ .0675
	2	36.7813	28.7813	.0700
	3	37.3750	32.0000	.0700
	4	33.6250	30.1875	.0700

The Company had approximately 6,000 shareholders on May 29, 1999.

To Our Fellow Shareholders and Employees:

Fiscal 1999 was a tough year. Nothing came easy. It was, in fact, as difficult a year to achieve our financial goals as we've had in this decade. Although net sales remained strong — topping the $1 billion mark during one quarter for the first time in our Company's history — isolated pricing skirmishes compressed our margins. Earnings per share

did show a modest improvement over the prior year, but in essence, our performance was flat. This failure to meet our projections, in tandem with other market factors, eroded investor confidence and deflated the price of our stock.

A disappointing year? Certainly, on one level. No year fully qualifies as a success if financial goals are not met. But in business as in chess, strategic moves often are made to produce results, not immediately, but rather 5, 10 or even 15 moves ahead in the game. In many ways, fiscal 1999 was on such a strategic chessboard. We sought out two value-building acquisitions and committed considerable resources to bakery modernization and development. We expanded the geographical reach of one of our choice cake brands, *Drake's,* and introduced a legendary sourdough bread, *Colombo,* to the Midwest .

Charting the financial year

Reflecting on the past year's financial achievements, one mark particularly stands out. For the first time, our snack cake brand portfolio — *Hostess, Dolly Madison* and the new *Drake's* — accounted for more than 50 percent of branded sales. Total net sales increased 5.9 percent to $3,459,377,000. Even after excluding acquisitions and disposed operations, net sales rose 1.3 percent and volume also improved.

We maintained our usual discipline on expenses, but a number of factors, including the competitive market conditions and start-up costs, compressed margins. Operating profit closed at $224,477,000, or 6.5 percent of net sales, compared to last year's $231,592,000, or 7.1 percent of net sales. Net income was $126,155,000, or 3.6 percent of net sales, just short of the prior year's record $127,924,000, or 3.9 percent of net sales. But we modestly improved earnings per share, reaching $1.74 (on a diluted basis), compared to the prior year's $1.71.

Our cash flow remained strong. We invested more than $100,000,000 toward modernization of production processes and new facilities. For example, by late summer, our new 280,000 square-foot *J.J.Nissen/ Wonder/Hostess* bakery in Biddeford, Maine, will be fully operational, allowing us to phase out four less productive plants in the New England region. It will be a showcase bakery, one of the world's largest and housing seven lines, two for bread and one each for buns and rolls, cakes, English muffins, donuts and pies. Biddeford is the cornerstone of our New England foundation. And fiscal year 1999 also saw the new Toledo, Ohio bakery come on-line. Underway is a major consolidation effort in the Pacific Northwest market area where production from three bread and roll bakeries will merge into a single, newly acquired bakery in Tacoma, Wash. We expect substantial cost savings there as well.

In addition, at the start of the new fiscal year, we further trimmed costs by closing our Minot, N.D., bakery and consolidating its bread production into our Billings, Mont., bakery. Similarly, our Roanoke, Va., *Rainbo* production was consolidated into the more efficient, much larger Charlotte, N.C., operation.

Also with the future in mind, we repurchased approximately three million shares of our common stock. We will continue that program as long as our shares offer a significant value.

Acquisitions

A key tactic of our overall growth strategy is to seek marketing opportunities through acquisition. Such was the case in our purchases of Drake's baking operation in Wayne N.J. and the My Bread Baking Co., located in New Bedford, Mass. Both immediately strengthened our ability to operate efficiently in the important northeastern U.S. market.

There was an additional plus to the *Drake's* acquisition that bears mentioning. *Drake's* is known for its well-established and popular *Devil Dogs, Ring Dings, Yodels* and *Yankee Doodles* snack cakes in the Northeast. *Drake's* cake also complements, rather than competes with, our regional *Dolly Madison* cake brand. Responding to this, we introduced *Drake's* cake on *Dolly Madison* sales routes in our Southeast and Midwest marketing regions, creating new markets for the unique brands without adding to fixed selling expenses. By using our established route system, we have the opportunity to develop *Drake's* into a major national brand. Snack cake is a high-impulse product category, and the more availability and access the consumer has, the better sales potential we have.

Brand Power

Fiscal 1999 was a record-setting sales year. In addition to increased sales from recently acquired baking operations, sales of established brands also rose with *Wonder* and *Hostess*, our powerhouse national brands, setting the pace. This was due in large part to our focus on Brand Power. We provide fresh, high-quality products people can trust to satisfy their need for safe, wholesome, great-tasting, convenient, baked goods.

But more importantly, these aren't just products. They are brands with a personality all their own. Nothing else in the market is truly like *Wonder* bread. Nothing else in the market is truly like a *Hostess Twinkie* or a *Hostess HoHo*. Our consumers believe that and our sales force believes that. We support that relationship with TV advertising campaigns that have proven to be effective. This spring, the *Hostess* TV campaign was awarded an "Effie" for effective advertising by the American Marketing Association, and earlier in the year, we won several "Golden Marbles" awards for excellence in children's advertising.

As the consumer landscape continues to evolve, the introduction of new products and the expansion of marketing areas — such as with *Drake's* — also will play an important role in our future success. This year we opened a new Toledo-area *Wonder* bread bakery that also produces hearth breads and rolls under the *Colombo* brand, and croutons and stuffing mix distributed under the *Marie Callender's* and *Mrs. Cubbison's* brands. This is the first time our *Colombo* brand has been produced outside California.

Looking Ahead

What does fiscal 2000 and beyond hold for us? The future will not lack challenges, of that we're sure. Admittedly, there are a host of factors over which we have minimal control. The commodity markets. The political environment. The changes in our competitors' strategies or tactics. But we have built a company that operates proactively to affect the controllable factors that impact performance. We succeed, and will continue to succeed, because we follow a set of tough-minded strategies grounded in a clear understanding of what is happening in the marketplace.

We enter the new fiscal year in excellent health. Our financial profile is outstanding. We are strong operationally and organizationally, with new leadership in some key positions. Our powerful brands and our committed people continue to give us great confidence in our ability to increase shareholder value.

Charles A. Sullivan
Chairman of the Board
and Chief Executive Officer

Our Key Business Strategies

- *Improve margin through development of powerhouse brands.*

Deliver value; produce trust. Our ability to develop and maintain a positive brand image is a major point of difference between our competitors and us. Brand building, and the subsequent investment in brand awareness, is an essential element to driving top-line growth.

- *Energize profitable growth through strategic acquisition and product line diversity.*

Acquisition candidates must complement our existing product lines, fill out our geographic presence and leverage our purchasing power, brand management capabilities and operating efficiencies. Through market research, we target significant niche markets with new products calculated to fit the need.

- *Stay ahead of the game through capital investment.*

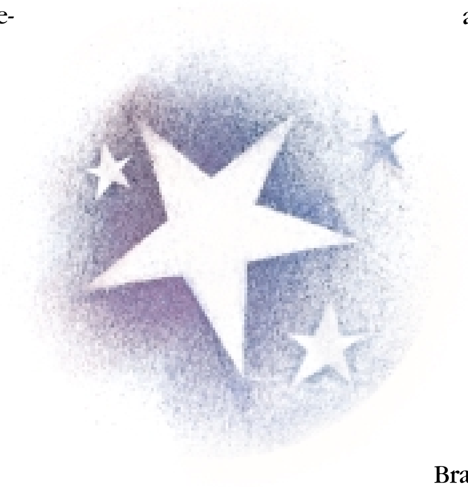
A powerful balance sheet gives us great flexibility toward achieving many of our long and short-term objectives. This strength allows us to move decisively to

NEW & FAMILIAR STARS MAKE OUR FUTURE BRIGHT

In the baking industry universe of bread and cake brands, the gleaming stars of our galaxy are among the most brilliant. Indeed, Interstate Bakeries Corporation's success story begins with Brand Power. Remember the *Wonder*? Since introducing the baking industry's first sliced bread loaf some four generations ago, *Wonder* has become America's favorite white bread with brand awareness greater than 90 percent. America's first choice easily outdistances its closest rival – our own *Home Pride* wheat – by nearly two to one. And our regional powerhouse bread brands – *Merita, Butternut and Millbrook* – are market leaders in many of their distribution areas. And what star shines brighter than *Hostess Twinkies*? None, unless it's a regional favorite like *Drake's Devil Dog*!

Icons & Images

Brand Power is about icons: the white icing squiggles of the *Hostess Cupcake* and the golden dreadnought shape of our famous *Twinkie*. The legendary round, crusty loaves of our *Parisian Fisherman's Wharf Sourdough*. Our brands create images that are among the most powerful in the industry. That is a tremendous asset. Supported by breakthrough television and radio advertising, our brands develop renewed vitality. That translates into profits for our Company. One out of every 25 items sold in the supermarket channel comes from the baking rack with total bread consumption in the U.S. approaching the $6 billion mark annually. More than a billion *Twinkies* and *Hostess Cupcakes* alone were consumed last year. Those are particularly positive trends for a company with as diverse and preferred product portfolio as ours.



Stellar Memories

Brand Power is all about tapping into a lifestyle: simple pleasures derived from biting into a *Gem* mini-donut for an on-the-go breakfast, or slapping a hot dog onto one of our buns at a picnic. Families have come to rely on our products to give them what they want, what they need and what they like. Our wheat, multi-grain and specialty breads, such as *Beefsteak Rye*, *Bread du Jour*, *Millbrook Cracked Wheat* and *Swirl Cinnamon Raisin*, command broad appeal. Hamburger and hot dog buns marketed under a variety of our strong national and regional brands respond to consumers' needs for inexpensive and convenient meals on the go.

There are growth opportunities with alternative bread products, such as *Mrs. Cubbison's* and *Marie Callender's* dry stuffing and croutons and *Colombo* breadsticks, as well as our regionally branded bagels and English muffins.

Promised Value

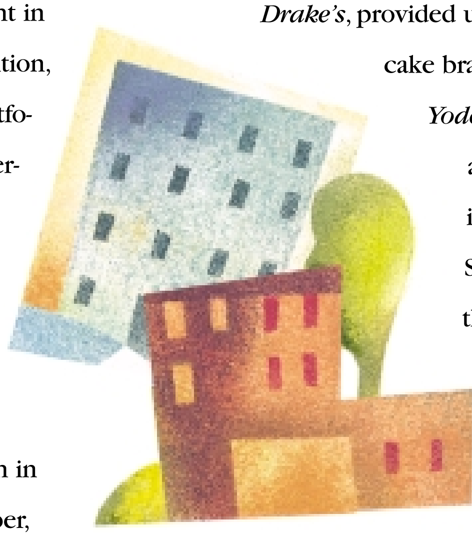
Brand Power is all about expectations and promises: providing the nutritious bread your kids love to eat and tasty snacks with a cream-filling surprise. Our brands connote value; they promise great flavor, quality, and variety – all delivered fresh at a fair price, day-in and day-out. Consumers trust our brands because over the years we have earned their trust. That ability to develop and maintain a positive brand image is a major point of difference between IBC and our competitors. It is our competitive advantage that drives our successful marketing strategy.

WISE ACQUISITIONS SHAPE OUR BUSINESS LANDSCAPE

The United States is the world's greatest consumer of goods, and Interstate Bakeries Corporation is the largest wholesale baking company serving that lucrative marketplace. From coast-to-coast, we deliver fresh bread and cake daily to more than 200,000 food outlets along some 11,000 delivery routes. But the consumer food industry is a relatively mature business sector, and top-line growth, essential to maximizing shareholder value, is often difficult to come by. Through the past decade, strategic, value-added acquisitions with their contribution to earnings have been the primary instrument for that growth. It will remain an important part of our growth plan for the future.

Merger Trend

The driving force behind this strategy is the need to be cost-effective in a market with diversifying needs. The American food industry is embroiled in dramatic change with mergers, acquisitions and realignments occurring more rapidly today than ever before. Such a fluid business environment favors large, national companies like IBC, and our Company has been, and will continue to be, an active participant in this consolidation trend. By acquisition, we've strengthened our brand portfolio and diversified our product offerings, adding strong bread brands such as *Parisian* and *Colombo*, as well as distinctive products like *Marie Callender's* croutons. In August, we purchased the well-respected Drake's baking operation in Wayne, N.J. More recently, in October, our Company acquired the My Bread Baking Co. of New Bedford, Mass.



Stellar Record

Over the years, IBC has produced a record of successfully assimilating acquired businesses into our overall operations. This is the result of our disciplined approach to acquisitions. We only seek out candidates that complement our existing product lines and provide us with unique, highly regarded brands. The candidates also must provide opportunities for profitable synergies and general economies of scale. And, finally, we seek an opportunity to leverage our purchasing power and brand management capabilities.

Tough Criteria

Our two recent acquisitions met those criteria. My Bread Baking and *Drake's* strengthened our Northeast operation, and particularly in the case of *Drake's*, provided us with four new powerhouse snack cake brands – *Devil Dogs, Ring Dings, Yodels* and *Yankee Doodles*. Once assimilated into our operations, we introduced the *Drake's* line to our Southeast and Midwest market area through judicious use of current distribution routes. *Drake's* cake, which complements our *Dolly Madison* products, is destined to become our Company's next national brand.

As consumer demand broadens, food companies like us must simplify preparation and distribution of our branded products. Simultaneously, we also must diversify our product offering. To achieve profitable growth and increase shareholder value, strategic acquisition will always be a key element of the IBC success formula.

THE RACE IS WON BY MAKING SMART DECISIONS

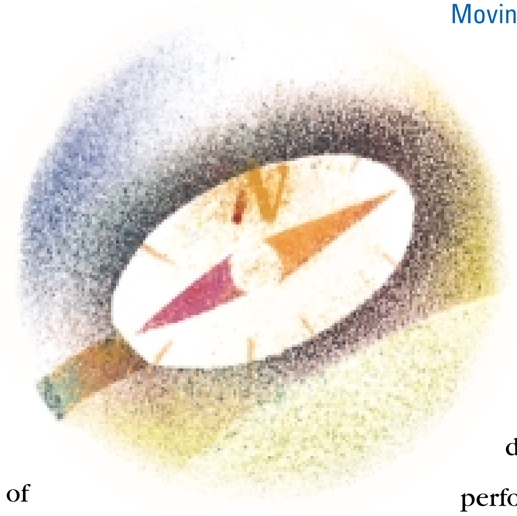
There is a difference between capital spending and capital investment. Capital spending is easy. Anybody can spend, but the cornerstone of a capital investment program is the discipline to spend on projects that yield an adequate return to increase shareholder value. The IBC program is disciplined and far-sighted. It is focused on continually reducing costs, providing our future operations with state of the art facilities that allow us to efficiently compete in a consolidating marketplace.

Capital investment

In this industry, the competitive edge is very thin, and you don't want to be caught short with less than a streamlined operation. We watch our pennies and are careful not to spend on projects with little likelihood to pay out in a reasonable time frame. IBC invested more than $100 million in capital projects during the past fiscal year to improve our plants, including bringing on-line our Company's two newest bakeries– a *Wonder* bread bakery near Toledo, Ohio, and a *J.J.Nissen/Wonder/Hostess* bakery in Biddeford, Maine.

New production lines

The 150,000 square-foot Ohio bakery celebrated its grand opening in October 1998. Capable of baking 250,000 loaves of bread a day, the bakery also produces croutons and dry stuffing under the *Marie Callender's* and *Mrs. Cubbison's* brands, as well as special *Colombo*-brand hearth breads. When fully operational this autumn, the 280,000 square-foot New England facility will be one of the largest baking plants in the world, replacing four less-efficient bakeries. Biddeford will house seven production lines — two for bread and one each for buns and rolls, cakes, English muffins, donuts and pies.



Impacting performance

Our capital investment budget for the new fiscal year is also ambitious. Among the major projects underway in fiscal 2000 is the upgrading of a 150,000 square-foot Tacoma, Wash., facility acquired earlier in the year. Fully operational, it will allow consolidation of bread and bun production from three smaller *Wonder* bread bakeries, dramatically cutting distribution and production costs in the Pacific Northwest.

Moving decisively in the right direction

In a consolidating business environment, size is of some importance, but making the right move in the right direction at the right time can make all the difference. Today's capital investment decisions impact tomorrow's performance. Therefore, we are committed to improving the efficient production and distribution of our quality-baked goods, not only day-in and day-out, but into the next millennium. We will continue to plot that course carefully and decisively. We will be ready for tomorrow's challenge.

SUCCESS IS IN THE DETAILS

In any competitive industry, the path to success is a set of tough-minded strategies grounded in a clear understanding of what's happening in the marketplace. This is particularly true in the food industry. We know from experience that today's consumers allow no room for compromise when it comes to satisfying their appetite for fresh-baked bread or cake. If we fail to please, then the edge goes to our competition.

Connecting with consumers

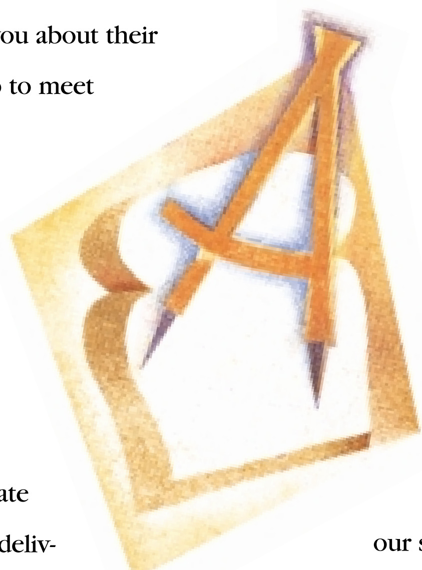
Other companies in the baking industry also have the know-how to make good bread and cake. And retail bakers in metropolitan areas bake some wonderful artisan baking products. Even consumers, if they have the time and inclination, can bake good bread and cake. We have seen bread machine use proliferate in recent years and cake mixes have long ago invested consumers with ability to bake off special treats in an instant. But the truth is, you become the leader when you listen to what consumers tell you about their needs, and then do a consistent job to meet those needs. Consumers define the quality of our bread and cakes. They always have been, and will always be, the final judge.

Ensuring freshness

Consumers' demand for freshness dictates the way in which we operate our business. We use a direct store delivery system. Every bread and cake route sales representative is provided with handheld computers that provide them with detailed sales and customer information, ensuring that the right product is in the right store on the right day. Our success is dependent on paying attention to these details each and every day on over 11,000 routes nationwide.

Processes & procedures

Baking is a simple process. It is a batch process. And since each new batch can be a little bit different than the one preceding it or the one after it, the business of baking becomes considerably more complex. The challenge: produce a fresh loaf of bread or a delicious donut or cake that's perfectly consistent in taste and texture whether it's baked in Los Angeles, Kansas City, Philadelphia or Emporia, Kan. And, more importantly, it must be perfectly consistent with the consumer's last purchase. How do we accomplish that feat? Follow a precise sequence of processes and procedures each and every day, at each and every one of our 67 bakeries. Our success relies on the abilities of our 12,500 production, sanitation and engineering employees to pay attention to these details every day. They are a critical part of our brand-building effort.



Employee empowerment

Simply put, one of the secrets to our success is individual accountability. We believe each person is responsible for the total operation, not just the job before them. A minor oversight can waste a thousand loaves in five minutes or damage a customer relationship that has taken years to develop, so we work to perfect the basics. We are a decentralized organization which allows us to pay better attention to these details. That effort results in the consistent quality that is the hallmark of our brands and the strength of the relationships we have built with our customers.

Five-Year Summary of Financial Data

(In Thousands, Except Per Share Data)

	52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997	52 Weeks Ended June 1, 1996[2]	53 Weeks Ended June 3, 1995
Statement of Income					
Net sales	$3,459,377	$3,265,842	$3,212,431	$2,878,180	$1,222,779
Operating income	224,477	231,592	191,143	78,758[3]	57,293
% of net sales	6.5%	7.1%	6.0%	2.7%	4.7%
Net income	$ 126,155	$ 127,924	$ 97,177	$ 24,463[3]	$ 20,697
% of net sales	3.6%	3.9%	3.0%	.8%	1.7%
Earnings per share:					
Basic [1]	$ 1.76	$ 1.74	$ 1.30	$ .35[3]	$ .53
Diluted [1]	1.74	1.71	1.28	.35[3]	.53
Common stock dividends per share [1]	.28	.28	.27	.25	.25
Weighted average common shares outstanding:					
Basic [1]	71,662	73,512	74,928	69,202	39,278
Diluted [1]	72,483	74,845	76,200	69,968	39,414
Balance Sheet					
Total assets	$1,680,775	$1,549,986	$1,493,087	$1,486,460	$ 598,441
Long-term debt, excluding current maturities	369,000	261,000	251,000	303,651	212,205
Stockholders' equity	603,803	565,155	538,722	460,247	198,037
Debt to total capital	37.9%	31.6%	31.8%	39.8%	51.7%

[1] All per share and average shares outstanding amounts reflect a November 1997 two-for-one stock split.

[2] Fiscal 1996 includes the operations of Continental Baking Company for 45 weeks from its acquisition on July 22, 1995.

[3] Fiscal 1996 includes a charge of $9,500,000 ($5,738,000 and $.08 per basic and diluted share on an after-tax basis) resulting from a payment due a union-administered, multi-employer pension plan which failed.

RESULTS OF OPERATIONS

Fiscal 1999 Compared With Fiscal 1998

Net sales for the fifty-two weeks ended May 29, 1999 were $3,459,377,000, an increase of $193,535,000 and 5.9% over net sales of $3,265,842,000 for the fifty-two weeks ended May 30, 1998. Excluding the effect of acquisitions and dispositions, net sales increased approximately 1.3% for the year. This adjusted increase reflects slight gains in branded unit volume, as well as narrowly higher selling prices realized during the latter part of the year.

Fiscal 1999's gross profit was $1,823,994,000, or 52.7% of net sales, up $100,072,000 from gross profit of $1,723,922,000, or 52.8% of net sales, in fiscal 1998. This stable margin performance reflects slightly lower ingredient costs for fiscal 1999, offset by higher labor and labor-related costs, as well as higher production-related costs of acquired operations.

Selling, delivery and administrative expenses totaled $1,489,472,000, or 43.1% of net sales, for fiscal 1999 compared to $1,389,627,000, or 42.6% of net sales, in fiscal 1998. This unfavorable variance was attributable to higher selling, delivery and administrative expenses, primarily labor and labor-related costs, as a percentage of net sales associated with acquired operations.

Depreciation and amortization increased $7,342,000, or 7.1%, to $110,045,000 in fiscal 1999 from $102,703,000 in fiscal 1998. This increase resulted from acquisitions, as well as the start-up of operations in the new Biddeford, Maine, and Northwood, Ohio, bakeries.

Based upon these factors, operating income for fiscal 1999 was $224,477,000, or 6.5% of net sales, a $7,115,000 decrease from fiscal 1998's operating income of $231,592,000, or 7.1% of net sales.

Interest expense for fiscal 1999 was $23,113,000, an increase of $4,489,000, or 24.1%, from fiscal 1998. Fiscal 1999's interest expense reflects higher average borrowing levels, primarily due to acquisitions, partially offset by lower average interest rates and increased interest capitalized on major capital projects.

The fiscal 1999 effective tax rate of 37.5%, as well as the fiscal 1998 rate of 40.1%, approximate the overall federal and state statutory rates.

Reflecting these results, net income for fiscal 1999 was $126,155,000, or $1.76 and $1.74 per basic and diluted share, respectively, compared to $127,924,000, or $1.74 and $1.71 per basic and diluted share, respectively, for fiscal 1998.

Fiscal 1998 Compared With Fiscal 1997

Net sales for the fifty-two weeks ended May 30, 1998 were $3,265,842,000, increasing $53,411,000 and 1.7% over net sales of $3,212,431,000 for the fifty-two weeks ended May 31, 1997. Excluding the impact of acquisitions and dispositions, net sales for fiscal 1998 were up only slightly over fiscal 1997. Selling prices remained relatively steady, as did overall unit volume. Branded units, after adjusting for acquisitions and dispositions, were up slightly more than 1% while non-branded units were down due to an emphasis on selling higher-margin, branded products.

Gross profit for fiscal 1998 was $1,723,922,000, representing 52.8% of net sales, an increase of $77,756,000 over gross profit of $1,646,166,000, or 51.2% of net sales, in fiscal 1997. This improvement in fiscal 1998 was attributable to lower ingredient costs, primarily flour, as well as favorable mix changes to higher-margin, branded products. These positive factors were partially offset by higher labor and labor-related costs experienced in fiscal 1998.

Selling, delivery and administrative expenses were $1,389,627,000, or 42.6% of net sales, for fiscal 1998 compared to $1,352,026,000, or 42.1% of net sales, for fiscal 1997. The 2.8% year-over-year dollar increase in selling, delivery and administrative expenses resulted from inflationary increases, primarily in labor and labor-related costs, as well as the impact of acquisitions, net of dispositions.

Reflecting these factors, operating income for fiscal 1998 rose $40,449,000, or 21.2%, to $231,592,000, representing 7.1% of net sales, from $191,143,000, or 6.0% of net sales, in fiscal 1997.

Interest expense decreased $3,968,000, or 17.6%, in fiscal 1998 to $18,624,000 from $22,592,000 in fiscal 1997. This decrease was due to somewhat lower average borrowing levels and interest rates, as well as increased interest capitalized on major capital projects during fiscal 1998.

The fiscal 1998 effective tax rate of 40.1% approximated the statutory rate, while the fiscal 1997 rate of 42.6% reflected the nondeductibility of amortization of various intangibles.

Based upon these overall results, net income for fiscal 1998 increased $30,747,000, or 31.6%, to $127,924,000 from $97,177,000 in fiscal 1997. Reflecting this increase, basic earnings per share improved 33.8% to $1.74 per share in fiscal 1998 from $1.30 per share in fiscal 1997, while diluted earnings per share improved 33.6% to $1.71 per share from $1.28 per share. Fiscal 1997 per share amounts were adjusted for a two-for-one stock split effected in the form of a stock dividend paid November 3, 1997, as well as the fiscal 1998 adoption of Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings per Share".

CAPITAL RESOURCES AND LIQUIDITY

The Company's primary source of liquidity is cash provided by operations which totaled $187,541,000 for fiscal 1999, a decrease of $14,081,000 from fiscal 1998's $201,622,000. This decrease was primarily due to higher working capital requirements. Cash generated by operations during fiscal 1999, along with net additional long-term borrowings of $108,000,000 and stock issuance proceeds of $9,726,000, was used to fund net capital expenditures of $100,413,000, common stock repurchases of $77,167,000, acquisitions of $106,180,000 and common stock dividends of $20,066,000.

For fiscal 2000, the Company anticipates cash needs of approximately $130,000,000, consisting of $85,000,000 of planned capital expenditures, $25,000,000 of required debt reduction and $20,000,000 of common stock dividends. The Company expects its fiscal 2000 cash needs to be funded by ongoing operations and borrowing capacity under its existing bank credit facility.

In addition, the Company will continue to evaluate among its investment alternatives the repurchase of additional shares of its common stock under its stock repurchase program.

YEAR 2000 COMPLIANCE

The Company is continuing to assess the impact that the turn of the century will have on its internal computer systems and overall operations. The Company has developed and is well into implementing a Company-wide Year 2000 plan (the "Plan"). The Plan consists of three major focus areas: information-technology ("IT") systems, critical corporate support areas and bakery critical systems and processes. The corporate and bakery focus areas are comprised of primarily non-IT systems and third-party considerations. The tasks common to each of these areas of focus are: (i) inventory and prioritization of all critical Year 2000 issues, (ii) assessment of compliance, (iii) remediation, (iv) testing and (v) design and implementation of contingency and business continuation plans.

The IT systems area focuses on the Company's internal computer hardware and software systems. All hardware, operating systems and business critical software programs have been remediated and the Company is currently in the final stages of testing for all operationally critical systems, replacement of personal computer hardware and software and development of contingency and business continuation plans for IT systems support. These final procedures should be completed by the end of September 1999.

All corporate support departments and bakery facilities have completed their inventory, assessment and remediation efforts with regard to all non-IT systems which include any hardware, software and associated embedded computer technologies that are used to operate Company facilities, equipment and other activities. The Company continues its efforts to test these non-IT systems and develop appropriate contingency plans with an estimated completion date for this phase of the Plan by the end of September 1999.

The Company, through its corporate support departments and individual bakery facilities, has identified, prioritized and is continuing to communicate with all critical business partners, including all third-party suppliers of goods and services, to ascertain the status of their Year 2000 compliance programs. The Company intends to monitor the progress of these critical third parties and test critical system interfaces, where appropriate.

The Company does not anticipate that the Year 2000 issues related to internally-controllable systems will significantly impact the overall business operations or financial results of the Company. However, the Company could face significant disruptions in business operations and financial losses if certain business-critical third parties, such as utility providers, telecommunication systems, transportation service providers or certain government entities, do not successfully complete their Year 2000 remediation plans. The Company is currently in the process of identifying and developing contingency plans for the most reasonably likely worst case scenarios. The Company expects to complete its analysis and contingency planning by September 1999.

The total cost of the Company's Plan is not expected to be material to the Company's financial position. The estimated total cost of the Plan is not expected to exceed $5 million, and is being funded through normal operating cash flows of the Company.

PENDING ACCOUNTING STANDARD

See Note 2 to the Company's consolidated financial statements for discussion regarding the pending accounting standard relating to derivative instruments and hedging activities.

FORWARD-LOOKING STATEMENTS

The Company or its representatives may from time-to-time provide information, in either written or oral form, which contains forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. In receiving and reviewing such information, it should be kept in mind that forward-looking statements are subject to certain risks and uncertainties which could cause actual results to differ materially from those discussed or projected. Factors which create these risks and uncertainties can be either internal to the Company or related to general external market conditions.

Consolidated Balance Sheet

	(In Thousands)	
	May 29, 1999	May 30, 1998
Assets		
Current assets:		
Accounts receivable, less allowance for doubtful accounts of $4,240,000 ($4,106,000 in 1998)	$ 216,984	$ 198,644
Inventories	65,861	66,427
Other current assets	65,905	69,387
Total current assets	348,750	334,458
Property and equipment:		
Land and buildings	385,495	343,339
Machinery and equipment	942,748	849,671
	1,328,243	1,193,010
Less accumulated depreciation	(425,327)	(344,130)
Net property and equipment	902,916	848,880
Intangibles	429,109	366,648
	$1,680,775	$1,549,986
Liabilities and Stockholders' Equity		
Current liabilities:		
Long-term debt payable within one year	$ 25,000	$ 25,000
Accounts payable	134,681	146,852
Accrued expenses	195,515	193,236
Total current liabilities	355,196	365,088
Long-term debt	369,000	261,000
Other liabilities	225,030	236,506
Deferred income taxes	127,746	122,237
Total long-term liabilities	721,776	619,743
Stockholders' equity:		
Preferred stock, par value $.01 per share; authorized - 1,000,000 shares; issued - none	–	–
Common stock, par value $.01 per share; authorized - 120,000,000 shares; issued - 79,630,000 shares (79,126,000 in 1998)	796	791
Additional paid-in capital	549,080	539,359
Retained earnings	256,807	150,718
Treasury stock, at cost - 9,412,000 shares (6,382,000 in 1998)	(202,880)	(125,713)
Total stockholders' equity	603,803	565,155
	$1,680,775	$1,549,986

See accompanying notes.

Consolidated Statement of Income

(In Thousands, Except Per Share Data)

	52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Net sales	$3,459,377	$3,265,842	$3,212,431
Cost of products sold	1,635,383	1,541,920	1,566,265
Selling, delivery and administrative expenses	1,489,472	1,389,627	1,352,026
Depreciation and amortization	110,045	102,703	102,997
	3,234,900	3,034,250	3,021,288
Operating income	224,477	231,592	191,143
Other income	(484)	(594)	(747)
Interest expense	23,113	18,624	22,592
	22,629	18,030	21,845
Income before income taxes	201,848	213,562	169,298
Provision for income taxes	75,693	85,638	72,121
Net income	$ 126,155	$ 127,924	$ 97,177
Earnings per share:			
Basic	$ 1.76	$ 1.74	$ 1.30
Diluted	$ 1.74	$ 1.71	$ 1.28

See accompanying notes.

Consolidated Statement of Cash Flows

	52 Weeks Ended May 29, 1999	(In Thousands) 52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Cash flows from operating activities:			
Net income	$ 126,155	$ 127,924	$ 97,177
Depreciation and amortization	110,045	102,703	102,997
Other	(6,764)	(12,226)	(7,171)
Change in operating assets and liabilities:			
Accounts receivable	(10,813)	507	(11,209)
Inventories	2,860	(1,042)	3,292
Other current assets	3,863	1,121	(1,761)
Accounts payable and accrued expenses	(37,805)	(17,365)	12,848
Cash from operating activities	187,541	201,622	196,173
Cash flows from investing activities:			
Acquisitions	(106,180)	(43,743)	(43,618)
Additions to property and equipment	(108,029)	(97,664)	(78,418)
Sale of assets	7,616	4,013	19,291
Other	(556)	2,263	(521)
Cash from investing activities	(207,149)	(135,131)	(103,266)
Cash flows from financing activities:			
Reduction of long-term debt	(92,000)	–	(126,205)
Addition to long-term debt	200,000	35,000	52,000
Common stock dividends paid	(20,066)	(20,434)	(19,857)
Stock option exercise proceeds and related tax benefits	9,726	10,630	13,636
Acquisition of treasury stock	(77,167)	(91,687)	(12,481)
Other	(885)	–	–
Cash from financing activities	19,608	(66,491)	(92,907)
Change in cash and cash equivalents	–	–	–
Cash and cash equivalents:			
Beginning of period	–	–	–
End of period	$ –	$ –	$ –
Cash payments made:			
Interest	$ 24,632	$ 19,859	$ 22,226
Income taxes	58,616	84,009	63,402

See accompanying notes.

Consolidated Statement of Stockholders' Equity

(In Thousands)

	Common Stock Issued: Number of Shares	Common Stock Issued: Par Value	Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Treasury Stock: Number of Shares	Treasury Stock: Cost
Balance June 1, 1996	77,470	$775	$515,109	$ (34,092)	(2,898)	$ (21,545)
Net income	–	–	–	97,177	–	–
Stock options exercised and related tax benefits	1,061	10	13,626	–	–	–
Dividends paid - $.27 per share	–	–	–	(19,857)	–	–
Treasury stock acquired	–	–	–	–	(519)	(12,481)
Balance May 31, 1997	78,531	785	528,735	43,228	(3,417)	(34,026)
Net income	–	–	–	127,924	–	–
Stock options exercised and related tax benefits	595	6	10,624	–	–	–
Dividends paid - $.28 per share	–	–	–	(20,434)	–	–
Treasury stock acquired	–	–	–	–	(2,965)	(91,687)
Balance May 30, 1998	79,126	791	539,359	150,718	(6,382)	(125,713)
Net income	–	–	–	126,155	–	–
Stock options exercised and related tax benefits	504	5	9,721	–	–	–
Dividends paid - $.28 per share	–	–	–	(20,066)	–	–
Treasury stock acquired	–	–	–	–	(3,030)	(77,167)
Balance May 29, 1999	79,630	$796	$549,080	$256,807	(9,412)	$(202,880)

See accompanying notes.

Notes to Consolidated Financial Statements

1. Acquisitions

On August 16, 1998, Interstate Bakeries Corporation (the "Company") acquired the assets of the Drake baking operation in Wayne, New Jersey ("Drake's"). Drake's employed over 800 people, distributed cake product throughout the northeastern United States and had annual net sales of approximately $115 million.

On October 4, 1998, the Company acquired the My Bread Baking Co. ("My Bread") operation in New Bedford, Massachusetts, in exchange for its Grand Junction, Colorado bakery and an additional cash payment. My Bread had annual net sales of approximately $37 million and employed over 400 people.

During fiscal 1998, the Company acquired the assets of the John J. Nissen Baking companies ("Nissen"), a major baker and distributor of fresh bread to the New England region. Nissen had annual net sales of approximately $115 million and employed 1,000 people.

During fiscal 1997, the Company purchased the assets comprising the San Francisco French Bread Company ("SFFB"). SFFB produced and distributed sourdough bread and rolls throughout Northern California and in the San Diego area, had net sales of approximately $95 million and employed 1,100 people. Also during fiscal 1997, the Company acquired the right to use the "Marie Callender's" trademark in conjunction with the manufacture, marketing, distribution and sale of croutons.

All of these acquisitions were accounted for as purchases. In addition, the My Bread exchange included a noncash portion not reflected in investing activities on the statement of cash flows for fiscal 1999 amounting to $14,365,000.

2. Description of Business and Significant Accounting Policies

Description of business - The Company is the largest baker and distributor of fresh bakery products in the United States.

Fiscal year end - The Company has a 52-53 week year that ends on the Saturday closest to the last day of May.

Principles of consolidation - The consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany accounts and transactions have been eliminated.

Inventories - Inventories are stated at the lower of cost or market. Specific invoiced costs are used with respect to ingredients and average costs are used for other inventory items.

The components of inventories are as follows:

	(In Thousands) May 29, 1999	May 30, 1998
Ingredients and packaging	$44,222	$43,534
Finished goods	15,936	16,996
Other	5,703	5,897
	$65,861	$66,427

Property and equipment - Property and equipment are recorded at cost and depreciated over estimated useful lives of 4 to 35 years, using the straight-line method for financial reporting purposes and accelerated methods for tax purposes.

Depreciation expense was $97,024,000, $91,296,000 and $89,507,000 for fiscal 1999, 1998 and 1997, respectively. Interest cost capitalized as part of the construction cost of capital assets was $3,084,000, $1,707,000 and $555,000 in fiscal 1999, 1998 and 1997, respectively.

Intangibles - Included in intangibles, which are being amortized using the straight-line method, are the following:

	Life	(In Thousands) May 29, 1999	May 30, 1998
Licenses and patents	9 years	$ 2,510	$ 2,510
Trademarks and tradenames	25-40 years	202,345	144,555
Excess of purchase cost over net assets acquired	40 years	314,699	296,473
Deferred financing cost and other-net	Term of loans	6,679	7,505
		526,233	451,043
Accumulated amortization		(97,124)	(84,395)
		$429,109	$366,648

Long-lived assets - Impairment losses are recognized when information indicates the carrying amount of long-lived assets, identifiable intangibles and goodwill related to those assets will not be recovered through future operations or disposal based upon a review of expected undiscounted cash flows. The Company currently expects the carrying amounts to be fully recoverable.

Interest rate swap agreements - The Company has from time to time entered into interest rate swaps with major banks to manage the balance of variable versus fixed rate debt based upon current and anticipated future market conditions. The differential to be paid or received is recognized over the term of the swap agreements as a component of interest expense. The risk associated with these agreements is limited to the cost of replacing these agreements at current market rates.

Statement of cash flows - For purposes of the statement of cash flows, the Company considers all investments purchased with an original maturity of three months or less to be cash equivalents.

Stock split - On September 23, 1997, the shareholders of the Company approved an increase in the number of authorized common shares to 120,000,000. On the same day, the Company's Board of Directors declared a two-for-one stock split effected in the form of a stock dividend payable November 3, 1997 to stockholders of record on October 15, 1997. All share and per share amounts presented reflect this stock split.

Earnings per share - During the third quarter of fiscal 1998, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings per Share." SFAS No. 128 replaced primary earnings per share with a dual presentation of basic and diluted earnings per share. Earnings per share amounts for prior periods were restated in accordance with this standard. Following is a reconciliation between basic and diluted weighted average shares outstanding used in the Company's earnings per share computations:

	(In Thousands)		
	52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Basic weighted average common shares outstanding	71,662	73,512	74,928
Effect of dilutive stock compensation	821	1,333	1,272
Diluted weighted average common shares outstanding	72,483	74,845	76,200

Use of estimates - The preparation of financial statements in conformity with generally accepted accounting principles 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 financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Pending accounting standard - SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities," was issued in June 1998. This statement establishes accounting and reporting standards for derivative instruments and for hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the statement of financial position and measure those instruments at fair value. This statement is effective for all quarters of fiscal years beginning after June 15, 2000. The Company is currently assessing the impact that the adoption of SFAS No. 133 will have on its consolidated financial statements.

3. Debt

Long-term debt consists of the following:

	(In Thousands)	
	May 29, 1999	May 30, 1998
Bank borrowings –		
Revolving credit loans (a)	$140,000	$207,000
6.43% Senior notes (b)	200,000	–
10.00% Senior notes (c)	54,000	79,000
	394,000	286,000
Less amounts payable within one year	(25,000)	(25,000)
	$369,000	$261,000

(a) Represents borrowings under an unsecured $350,000,000 revolving credit facility, including up to $150,000,000 available for letters of credit (with an unused amount of $67,000,000 at May 29, 1999), maturing in February 2002. The outstanding borrowings bear interest at variable rates generally equal to the London Interbank Offered Rate (LIBOR) plus from .20% to .63% (.20% at May 29, 1999), depending on certain financial ratios. The Company also pays a fee of between .08% and .23% (.08% at May 29, 1999) on the unused portion of the revolving credit facility. The overall weighted average interest rate on the bank borrowings was 5.23% and 5.96% at May 29, 1999 and May 30, 1998, respectively.

The credit facility agreement contains covenants which, among other matters (i) limit the Company's ability to incur indebtedness, merge, consolidate and acquire or sell assets, (ii) require the Company to satisfy certain ratios related to net worth, debt-to-capitalization and interest coverage and (iii) limit the payment of cash dividends on common stock and common stock repurchases to a total of $110,000,000 plus 75% of aggregate consolidated net income after fiscal 1998, with availability of $107,383,000 at May 29, 1999.

(b) Represents borrowings under a 6.43% senior note agreement with several major insurance companies entered into on September 10, 1998. The debt, which is unsecured, has a maturity date of September 2005. The note agreement contains covenants, which (i) limit the Company's ability to incur indebtedness, merge, consolidate and sell assets, and (ii) require the Company to satisfy certain ratios related to net worth and interest coverage. These covenants are comparable to those under the revolving credit facility.

(c) Represents 10.00% unsecured notes, with installments maturing in July 1999 and 2000. The note agreement includes covenants mirroring those of the revolving credit facility.

The fair value of all senior notes is estimated at $255,600,000 and $83,500,000 as of May 29, 1999 and May 30, 1998, respectively. The Company believes, based upon current terms, that the carrying value of all other long-term debt approximates fair value.

The scheduled repayment of long-term debt is as follows:

Fiscal Years Ending	(In Thousands)
2000	$ 25,000
2001	29,000
2002	140,000
2006	200,000
	$394,000

4. Commitments and Contingencies

Future minimum rental commitments for all noncancelable operating leases, exclusive of taxes and insurance, are as follows:

Fiscal Years Ending	(In Thousands)
2000	$ 62,778
2001	53,710
2002	41,661
2003	29,144
2004	17,525
Thereafter	24,820
	$229,638

Net rental expense under operating leases was $67,568,000, $59,817,000 and $53,792,000 for fiscal 1999, 1998 and 1997, respectively. The majority of the operating leases contain renewal options for varying periods. Certain leases include purchase options during or at the end of the lease term.

The Company is subject to various routine legal proceedings, environmental actions and other matters in the ordinary course of business, some of which may be covered in whole or in part by insurance. In management's opinion, none of these matters will have a material adverse effect on the Company's financial position, but could be material to the results of operations or cash flows for a particular quarter or annual period.

5. Income Taxes

The reconciliation of the provision for income taxes to the statutory federal rate is as follows:

	52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Statutory federal tax	**35.0%**	35.0%	35.0%
State income tax	**2.2**	4.9	5.1
Intangibles amortization	**1.2**	1.1	2.0
Other	**(0.9)**	(0.9)	0.5
	37.5%	40.1%	42.6%

The components of the provision for income taxes are as follows:

	(In Thousands) 52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Current:			
Federal	$62,227	$64,449	$54,057
State	5,829	13,811	11,789
	68,056	78,260	65,846
Deferred:			
Federal	6,702	5,176	4,985
State	935	2,202	1,290
	7,637	7,378	6,275
	$75,693	$85,638	$72,121

Temporary differences and carryforwards which give rise to the deferred income tax assets and liabilities are as follows:

	(In Thousands) May 29, 1999	May 30, 1998
Deferred tax assets:		
Payroll and benefits accruals	$ 18,635	$ 19,046
Self-insurance reserves	14,292	15,224
Other	16,778	17,563
Valuation allowance	–	–
	$ 49,705	$ 51,833
Deferred tax liabilities:		
Property and equipment	$138,776	$150,476
Intangibles	53,324	48,986
Self-insurance reserves	(28,532)	(33,412)
Payroll and benefits accruals	(38,267)	(39,250)
Environmental accruals	(7,099)	(9,407)
Other	9,544	4,844
	$127,746	$122,237

6. Employee Benefit Plans

The 1991 Employee Stock Purchase Plan, which is noncompensatory, allows all eligible employees to purchase common stock of the Company. The common stock can be either issued by the Company at market prices or purchased on the open market. At May 29, 1999, 232,000 shares were authorized but not issued under this plan.

SFAS No. 132, "Employers' Disclosures about Pension and Other Postretirement Benefits," was issued in February 1998. This statement revised employers' disclosures about pension and other postretirement benefit plans, but did not change the measurement or recognition of such plans. The Company adopted SFAS No. 132 during fiscal 1999 and certain prior year disclosures have been revised in accordance with the requirements of this new standard.

The Company sponsors a defined contribution retirement plan for eligible employees not covered by union plans. Contributions are based upon a percentage of annual compensation plus a percentage of voluntary employee contributions. Retirement expense related to this plan was $16,268,000, $16,134,000 and $15,543,000 for fiscal 1999, 1998 and 1997, respectively.

There are also in effect numerous negotiated pension plans covering employees participating by reason of union contracts. Expense for these plans was $107,220,000, $97,442,000 and $88,971,000 for fiscal 1999, 1998 and 1997, respectively.

In addition to providing retirement pension benefits, the Company provides health care benefits for eligible retired employees. Under the Company's plans, all nonunion employees, with 10 years of service after age 50, are eligible for retiree health care coverage between ages 60 and 65. Grandfathered nonunion employees and certain union employees who have bargained into the Company-sponsored health care plans are generally eligible after age 55, with 10 years of service, and have only supplemental benefits after Medicare eligibility is reached. Certain of the plans require contributions by retirees and spouses.

The components of the net postretirement benefit expense are as follows:

	(In Thousands)		
	52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Service cost	$2,089	$2,146	$2,237
Interest cost	6,675	6,791	6,977
Amortization of unrecognized prior service cost	320	297	292
Amortization of unrecognized net (gain) loss	–	(316)	429
Net postretirement benefit expense	$9,084	$8,918	$9,935

The aggregate change in the Company's accumulated postretirement benefit obligation ("APBO"), which is unfunded, is as follows:

	(In Thousands)	
	May 29, 1999	May 30, 1998
APBO at beginning of year	$90,254	$91,880
Service cost	2,089	2,146
Interest cost	6,675	6,791
Plan participants' contributions	1,756	1,679
Amendments	50	330
Actuarial (gain) loss	6,964	(5,769)
Acquisitions	268	1,829
Benefits paid	(10,000)	(8,632)
APBO at end of year	98,056	90,254
Unrecognized prior service cost	(2,473)	(2,743)
Unrecognized net gain (loss)	(4,246)	2,718
Accrued postretirement benefit	91,337	90,229
Less current portion	(8,650)	(7,650)
APBO included in other liabilities	$82,687	$82,579

In determining the APBO, the weighted average discount rate was assumed to be 7.0% for fiscal 1999 and 8.0% for fiscal 1998 and 1997. The assumed health care cost trend rate for fiscal 1999 was 8.5%, declining gradually to 6.5% over the next 6 years and to 5.5% after 15 years. A 1.0% increase in this assumed health care cost trend rate would increase the service and interest cost components of the net postretirement benefit expense for fiscal 1999 by approximately $1,059,000, as well as increase the May 29, 1999 APBO by approximately $9,629,000. Conversely, a 1.0% decrease in this rate would decrease the fiscal 1999 expense by approximately $847,000 and the May 29, 1999 APBO by approximately $8,139,000.

The Company also participates in a number of multi-employer plans which provide postretirement health care benefits to substantially all union employees not covered by Company-administered plans. Amounts reflected as benefit cost and contributed to such plans, including amounts related to health care benefits for active employees, totaled $154,670,000, $142,368,000 and $134,917,000 in fiscal 1999, 1998 and 1997, respectively.

7. Stock-Based Compensation

The 1996 Stock Incentive Plan (the "Plan") allows the Company to grant to employees and directors various stock awards, including stock options, which are granted at prices not less than the fair market value at the date of grant, and restricted stock. A maximum of 13,683,000 shares was approved to be issued under the Plan. On May 29, 1999, shares totaling 4,162,000 were authorized but not awarded under the Plan.

The stock options may be granted over a period not to exceed 10 years and generally vest from one to three years from the date of grant. The changes in outstanding options are as follows:

	(In Thousands) Shares Under Option	Weighted Average Exercise Price Per Share
Balance June 1, 1996	2,061	$ 7.76
Issued	2,246	18.50
Surrendered	(38)	16.71
Exercised	(1,040)	7.83
Balance May 31, 1997	3,229	15.10
Issued	2,648	33.90
Surrendered	(63)	22.39
Exercised	(553)	12.17
Balance May 30, 1998	5,261	24.78
Issued	1,030	26.60
Surrendered	(184)	29.81
Exercised	(504)	14.36
Balance May 29, 1999	5,603	$25.89

Stock options outstanding and exercisable on May 29, 1999 are as follows:

Range of Exercise Prices Per Share	(In Thousands) Shares Under Option	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life In Years
Outstanding:			
$ 6.13 - $10.63	509	$ 7.91	5.9
18.50 - 22.50	1,669	18.71	7.5
26.44 - 33.91	3,425	32.06	8.6
$ 6.13 - $33.91	5,603	$25.89	8.0
Exercisable:			
$ 6.13 - $10.63	509	$ 7.91	
18.50 - 22.50	951	18.50	
26.44 - 33.91	1,024	33.43	
$ 6.13 - $33.91	2,484	$22.48	

The Company applies Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB25"), and related interpretations in accounting for the Plan, and, therefore, no compensation expense has been recognized for stock options issued under the Plan. For companies electing to continue the use of APB25, SFAS No. 123, "Accounting for Stock-Based Compensation," requires proforma disclosures determined through the use of an option-pricing model as if the provisions of SFAS No. 123 had been adopted.

The weighted average fair value at date of grant for options granted during fiscal 1999, 1998 and 1997 was $8.80, $11.94 and $6.48 per share, respectively. The fair value of each option grant was estimated on the date of the grant using the Black-Scholes option-pricing model with the following assumptions:

	1999	1998	1997
Expected dividend yield	1.3%	.9%	1.0%
Expected volatility	28.5%	27.2%	26.5%
Risk-free interest rate	5.4%	6.0%	6.4%
Expected term in years	4	4	4

If the Company had adopted the provisions of SFAS No. 123, the impact on reported net income and earnings per share would have been as follows:

	52 Weeks Ended May 29, 1999	52 Weeks Ended May 30, 1998	52 Weeks Ended May 31, 1997
Net income (in thousands)	$10,621	$11,242	$ 4,050
Earnings per share:			
Basic	.15	.15	.05
Diluted	.15	.15	.05

During fiscal 1998, the Company also awarded 200,000 shares of restricted stock under the Plan, with a weighted average fair value at the date of grant of $33.91 per share. These restricted shares vest ratably after one, two and three years of continued employment. Compensation expense related to this award was $2,260,000 and $1,565,000 for fiscal 1999 and 1998, respectively.

On May 29, 1999, 10,197,000 total shares of common stock were reserved for issuance under various employee benefit plans.

8. Accrued Expenses and Other Liabilities

Included in accrued expenses are the following:

	(In Thousands) May 29, 1999	May 30, 1998
Payroll, vacation and other compensation	$57,838	$64,065
Self-insurance reserves	47,366	54,256
Pension and welfare	37,840	36,832
Taxes other than income	20,642	20,928

Included in other liabilities are the following:

	(In Thousands) May 29, 1999	May 30, 1998
Self-insurance reserves	$80,327	$86,182
Accumulated postretirement benefit obligation	82,687	82,579

9. Quarterly Financial Information (Unaudited)

Summarized quarterly financial information for the fiscal years ended May 29, 1999 and May 30, 1998 is as follows (each quarter represents a period of twelve weeks except the third quarters, which cover sixteen weeks):

	(In Thousands, Except Per Share Data)			
	First	Second	Third	Fourth
1999				
Net sales	$788,416	$814,593	$1,031,342	$825,026
Cost of products sold	371,806	389,354	488,976	385,247
Operating income	59,396	56,460	54,511	54,110
Net income	34,491	32,107	29,583	29,974
Earnings per share:				
Basic	.48	.45	.41	.42
Diluted	.47	.44	.41	.42
1998				
Net sales	$763,719	$754,167	$ 964,778	$783,178
Cost of products sold	362,155	352,130	457,054	370,581
Operating income	54,755	62,246	55,894	58,697
Net income	29,880	34,247	29,871	33,926
Earnings per share:				
Basic	.40	.47	.41	.46
Diluted	.39	.46	.40	.46

Independent Auditors' Report

To the Board of Directors and Stockholders
Interstate Bakeries Corporation

We have audited the accompanying consolidated balance sheets of Interstate Bakeries Corporation and its subsidiaries as of May 29, 1999 and May 30, 1998 and the related consolidated statements of income, stockholders' equity and cash flows for each of the three fiscal years in the period ended May 29, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of Interstate Bakeries Corporation and its subsidiaries as of May 29, 1999 and May 30, 1998, and the results of their operations and their cash flows for each of the three fiscal years in the period ended May 29, 1999 in conformity with generally accepted accounting principles.

Deloitte & Touche LLP

Kansas City, Missouri
July 14, 1999

Directors & Officers

BOARD OF DIRECTORS

CHARLES A. SULLIVAN
Chairman of the Board and
Chief Executive Officer
Interstate Bakeries Corporation
Kansas City, Missouri

MICHAEL J. ANDERSON
President and
Chief Executive Officer
The Andersons, Inc.
Maumee, Ohio

G. KENNETH BAUM
Chairman of the Board
George K. Baum Group, Inc.
Kansas City, Missouri

LEO BENATAR
Consultant
Benatar & Associates and
A.T. Kearney, Inc.
Atlanta, Georgia

E. GARRETT BEWKES, JR.
Consultant
PaineWebber Group, Inc.
New York, New York

ROBERT B. CALHOUN, JR.
Managing Director
Monitor Clipper Partners
Cambridge, Massachusetts

JAMES R. ELSESSER
Vice President and
Chief Financial Officer
Ralston Purina Company
St. Louis, Missouri

FRANK E. HORTON, PH.D.
Principal
Horton & Associates
Denver, Colorado

OFFICERS

Interstate Bakeries Corporation

CHARLES A. SULLIVAN
Chairman of the Board and
Chief Executive Officer

MICHAEL D. KAFOURE
President and
Chief Operating Officer

RAY SANDY SUTTON
Vice President, Corporate Secretary
and General Counsel

FRANK W. COFFEY
Senior Vice President
and Chief Financial Officer

JOHN F. McKENNY
Vice President and
Corporate Controller

PAUL E. YARICK
Vice President and Treasurer

LINDA L. THOMPSON
Assistant Secretary and
Director, Shareholder Relations

Interstate Brands Companies

CHARLES A. SULLIVAN
Chairman of the Board
and Chief Executive Officer

MICHAEL D. KAFOURE
President and
Chief Operating Officer

RAY SANDY SUTTON
Vice President, Corporate Secretary
and General Counsel

FRANK W. COFFEY
Senior Vice President
and Chief Financial Officer

ROBERT P. MORGAN
Executive Vice President
Central Division

JAMES R. WIDLER
Executive Vice President
Eastern Division

RICHARD D. WILLSON
Executive Vice President
Western Division

THOMAS S. BARTOSZEWSKI
Senior Vice President
Central Division - North

MICHAEL E. COLGAN
Senior Vice President
Eastern Division – North

TIMOTHY W. CRANOR
Senior Vice President
Central Division – South

MARK D. DIRKES
Senior Vice President
Corporate Marketing

BOBBY J. McCLELLAN
Senior Vice President
Eastern Division – South

BRIAN A. POULTER
Senior Vice President
Engineering

BRIAN E. STEVENSON
Senior Vice President
Purchasing

THOMAS E. WILSON
Senior Vice President
Western Division - South

THERESA S. COGSWELL
Vice President
Research and Development

RICHARD B. COOK
Vice President
Labor Relations

MELVIN H. GHEARING
Vice President
Retail Operations

MICHAEL R. HOLDGRAF
Vice President
Information Systems

GEORGE L. LAMPROS
Vice President
Bread Marketing

JOHN F. McKENNY
Vice President and
Corporate Controller

STAN W. OSMAN
Vice President
Cake Marketing

RONALD D. PARQUE
Vice President
Dry Products Division

TERRY A. STEPHENS
Vice President
National Account Sales

SCOTT A. WAY
Vice President
Internal Audit

PAUL E. YARICK
Vice President
and Treasurer

LINDA L. THOMPSON
Assistant Secretary

Corporate Information

Corporate Headquarters
12 East Armour Boulevard
P.O. Box 419627
Kansas City, Missouri 64141
(816) 502-4000

Subsidiaries
Interstate Brands Corporation
Interstate Brands West Corporation
Mrs. Cubbison's Foods, Inc.
IBC Trucking Corporation

Division Offices
Western – Phoenix, Arizona
Eastern – Charlotte, North Carolina
Central – Kansas City, Missouri
Dry Products – Montebello, California

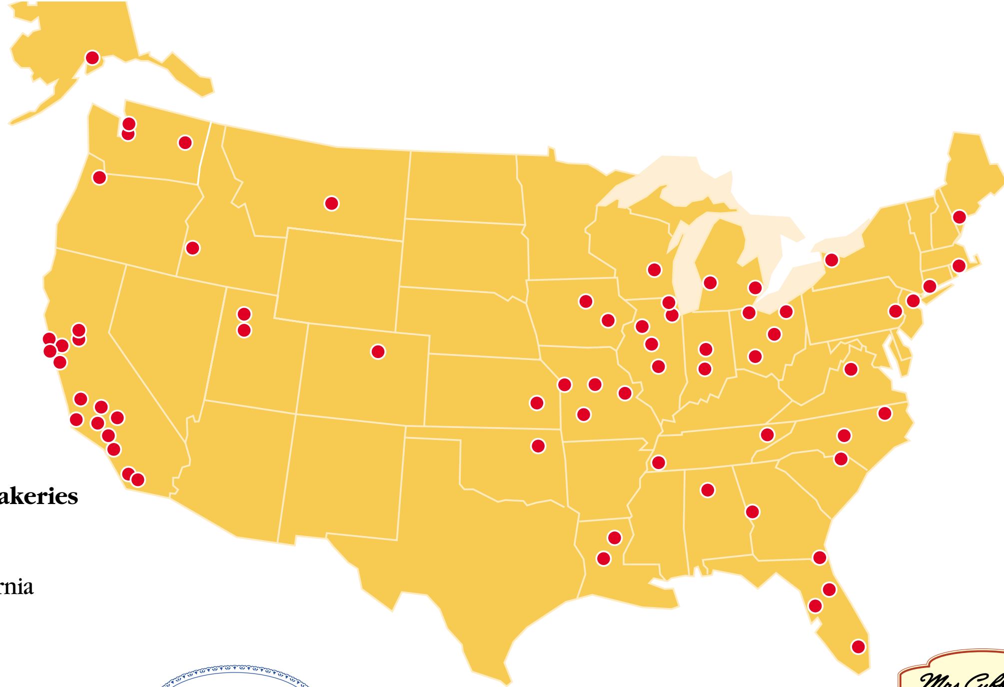
Common Stock
Listed on the New York Stock Exchange
Trading Symbol – IBC
Trade Journal Listing – IntstBaker

Transfer Agent & Registrar
UMB Bank, n.a.
928 Grand Avenue
Kansas City, Missouri 64106

10-K Report
A copy of the Company's 10-K report, as filed with the Securities and Exchange Commission, is available upon request to the Corporate Secretary at the Headquarters address.

Annual Meeting
The Annual Meeting of Stockholders of Interstate Bakeries Corporation will be held in the Atkins Auditorium of The Nelson-Atkins Museum of Art, 4525 Oak, Kansas City, Missouri at 10:00 a.m. Central Daylight Time on Tuesday, September 21, 1999.

INTERSTATE BAKERIES CORPORATION



Wonder Bread Bakeries
Anchorage, Alaska
Pomona, California
Sacramento, California
Tampa, Florida
Hodgkins, Illinois
Waterloo, Iowa
Kansas City, Missouri
Jamaica, New York
Akron, Ohio
Columbus, Ohio
Northwood, Ohio
Portland, Oregon
Salt Lake City, Utah
Richmond, Virginia
Seattle, Washington

Hostess Cake Bakeries
Schiller Park, Illinois
Detroit, Michigan
Seattle, Washington
Los Angeles, California

Wonder/Hostess Bakeries
San Francisco, California
Denver, Colorado
Indianapolis, Indiana
Davenport, Iowa
St. Louis, Missouri
Buffalo, New York
Tulsa, Oklahoma
Philadelphia, Pennsylvania
Memphis, Tennessee
Ogden, Utah
Spokane, Washington

J.J. Nissen/Wonder/Hostess Bakery
Biddeford, Maine

Butternut Bread Bakeries
Peoria, Illinois
Grand Rapids, Michigan
Boonville, Missouri
Springfield, Missouri
Cincinnati, Ohio
Decatur, Illinois
Minonk, Illinois

Merita Bread Bakeries
Birmingham, Alabama
Jacksonville, Florida
Orlando, Florida
Charlotte, North Carolina
Rocky Mount, North Carolina
Florence, South Carolina
Knoxville, Tennessee

Dolly Madison Cake Bakeries
Columbus, Georgia
Columbus, Indiana
Emporia, Kansas
Los Angeles, California

Eddy's Bread Bakery
Boise, Idaho

Drake's Bakery
Wayne, New Jersey

Millbrook Bread Bakeries
Glendale, California
Los Angeles, California
San Diego, California

Cotton's Bread Bakeries
Alexandria, Louisiana
Monroe, Louisiana

Parisian Bread Bakeries
San Diego, California
San Francisco, California

Sunbeam Bread Bakery
New Bedford, Massachusetts

Dry Products
Montebello, California

Sweetheart Bread Bakery
Billings, Montana

Braun's Bagel Bakery
Milwaukee, Wisconsin

Holsum Bread Bakery
Miami, Florida

DiCarlo Bread Bakery
San Pedro, California

Colombo Bread Bakeries
Castroville, California
Oakland, California
Sacramento, California

INTERSTATE
BAKERIES
CORPORATION

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