PROCTER & GAMBLE CO
Form 10-Q
February 03, 2004

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 December 31, 2003 Commission file number 1-434

THE PROCTER & GAMBLE COMPANY
(Exact name of registrant as specified in its charter)

Ohio	31-0411980
(State of incorporation)	(I.R.S. Employer Identification No.)

One Procter & Gamble Plaza, Cincinnati, Ohio	45202
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (513) 983-1100

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 [X] No [ ]

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes [X] No [ ]

There were 1,292,396,101 shares of Common Stock outstanding as of December 31, 2003.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

The Consolidated Statement of Earnings of The Procter & Gamble Company and subsidiaries for the three and six months ended December 31, 2003 and 2002, the Consolidated Balance Sheet as of December 31, 2003 and June 30, 2003, and the Consolidated Statement of Cash Flows for the six months ended December 31, 2003 and 2002 follow. In the opinion of management, these unaudited consolidated financial statements contain all adjustments necessary to present fairly the financial position, results of operations and cash flows for the interim periods reported. However, such financial statements may not be indicative necessarily of annual results.

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF EARNINGS

Amounts in millions except per share amounts

	Three Months Ended December 31		Six Months December
	2003	2002	2003
NET SALES	$ 13,221	$ 11,005	$ 25,416
Cost of products sold	6,324	5,490	12,203
Marketing, research, administrative and other expense	4,155	3,267	7,828
OPERATING INCOME	2,742	2,248	5,385
Interest expense	149	143	290
Other non-operating income, net	29	74	69
EARNINGS BEFORE INCOME TAXES	2,622	2,179	5,164
Income taxes	804	685	1,585
NET EARNINGS	$ 1,818	$ 1,494	$ 3,579
PER COMMON SHARE:			
Basic net earnings	$ 1.38	$ 1.13	$ 2.71
Diluted net earnings	$ 1.30	$ 1.06	$ 2.56
Dividends	$ 0.45	$ 0.41	$ 0.91
AVERAGE COMMON SHARES OUTSTANDING - DILUTED	1,400.4	1,402.6	1,399.6

See accompanying Notes to Consolidated Financial Statements

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEET

Amounts in millions

ASSETS	December 31 2003	June 30 2003
CURRENT ASSETS		
Cash and cash equivalents	$ 4,943	$ 5,912
Investment securities	351	300
Accounts receivable	4,447	3,038
Inventories		
Materials and supplies	1,322	1,095
Work in process	375	291
Finished goods	2,924	2,254
Total Inventories	4,621	3,640
Deferred income taxes	877	843
Prepaid expenses and other	1,926	1,487

receivables		
TOTAL CURRENT ASSETS	17,165	15,220
PROPERTY, PLANT AND EQUIPMENT		
Buildings	5,210	4,729
Machinery and equipment	19,188	18,222
Land	665	591
	25,063	23,542
Accumulated depreciation	(11,020)	(10,438)
NET PROPERTY, PLANT AND EQUIPMENT	14,043	13,104
NET GOODWILL AND OTHER INTANGIBLE ASSETS		
Goodwill	16,528	11,132
Trademarks and other intangible assets	4,182	2,375
NET GOODWILL AND OTHER INTANGIBLE ASSETS	20,710	13,507
OTHER NON-CURRENT ASSETS	1,944	1,875
TOTAL ASSETS	$ 53,862	$ 43,706
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	$ 2,822	$ 2,795
Accrued and other liabilities	6,446	5,512
Taxes payable	2,454	1,879
Debt due within one year	5,885	2,172
TOTAL CURRENT LIABILITIES	17,607	12,358
LONG-TERM DEBT	12,636	11,475
DEFERRED INCOME TAXES	1,898	1,396
OTHER NON-CURRENT LIABILITIES	3,149	2,291
TOTAL LIABILITIES	35,290	27,520
SHAREHOLDERS' EQUITY		
Preferred stock	1,554	1,580
Common stock - shares outstanding Dec 31 1,292.4	1,292	
June 30 1,297.2		1,297
Additional paid-in capital	3,250	2,931
Reserve for ESOP debt retirement	(1,296)	(1,308)
Accumulated other comprehensive income	(1,219)	(2,006)
Retained earnings	14,991	13,692
TOTAL SHAREHOLDERS' EQUITY	18,572	16,186
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$ 53,862	$ 43,706

See accompanying Notes to Consolidated Financial Statements

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
CONSOLIDATED STATEMENT OF CASH FLOWS

Amounts in millions	Six Months Ended December 31	
	2003	2002
CASH AND CASH EQUIVALENTS, BEGINNING OF PERIOD	$ 5,912	$ 3,427
OPERATING ACTIVITIES		
Net earnings	3,579	2,958
Depreciation and amortization	857	844
Deferred income taxes	233	166
Change in:		
Accounts receivable	(452)	(117)
Inventories	(74)	(89)
Accounts payable and accruals	(183)	73
Other operating assets & liabilities	(144)	151
Other	145	340
TOTAL OPERATING ACTIVITIES	3,961	4,326
INVESTING ACTIVITIES		
Capital expenditures	(810)	(616)
Proceeds from asset sales	124	117
Acquisitions, net of cash acquired	(5,358)	0
Change in investment securities	(69)	(8)
TOTAL INVESTING ACTIVITIES	(6,113)	(507)
FINANCING ACTIVITIES		
Dividends to shareholders	(1,245)	(1,129)
Change in short-term debt	2,791	(1,188)
Additions to long-term debt	1,405	1,187
Reduction of long-term debt	(993)	(50)
Proceeds from stock options	233	58
Purchase of treasury shares	(1,046)	(1,025)
TOTAL FINANCING ACTIVITIES	1,145	(2,147)
EFFECT OF EXCHANGE RATE CHANGES ON CASH AND CASH EQUIVALENTS	38	7
CHANGE IN CASH AND CASH EQUIVALENTS	(969)	1,679
CASH AND CASH EQUIVALENTS, END OF PERIOD	$ 4,943	$ 5,106

See accompanying Notes to Consolidated Financial Statements

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. These statements should be read in conjunction with the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2003. The results of operations for the three-month and six-month periods ended December 31, 2003 are not indicative necessarily of annual results.

2. Comprehensive Income - Total comprehensive income is comprised primarily of net earnings, net currency translation gains and losses, impacts of net investment and cash flow hedges and net unrealized gains and losses on securities. Total comprehensive income for the three months ended December 31, 2003 and 2002 was $2,429 million and $1,783 million, respectively. For the six months ended December 31, 2003 and 2002, total comprehensive income was $4,366 million and $3,143 million, respectively.

3. Segment Information - The basis for presenting segment results generally is consistent with overall Company reporting. The primary difference relates to partially-owned operations, where segment reporting reflects such investments as consolidated subsidiaries with applicable adjustments to comply with U.S. GAAP in the Corporate segment. The Corporate segment also includes both operating and non-operating elements such as financing and investment activities, certain employee benefit costs, intangible asset amortization, certain restructuring charges, segment eliminations, prior year results of certain divested businesses and other general corporate items. Additionally, for interim periods certain non-recurring tax impacts are reflected on a discrete basis for management and segment reporting purposes, but are eliminated in Corporate to arrive at the Company's effective tax rate for the quarter.

SEGMENT INFORMATION (Amounts in millions)

Three Months Ended December 31	Fabric & Home Care	Baby & Family Care	Beauty Care	Health Care	Snacks & Beverages	Cor
Net Sales						
2003	$ 3,407	$ 2,673	$ 4,492	$ 1,908	$ 931	
2002	3,102	2,526	2,997	1,567	881	
Earnings Before Income Taxes						
2003	843	444	1,047	500	188	
2002	768	443	731	374	168	
Net Earnings						
2003	570	281	681	333	122	
2002	514	276	507	253	110	

Six Months Ended December 31	Fabric & Home Care	Baby & Family Care	Beauty Care	Health Care	Snacks & Beverages	Cor
Net Sales						
2003	$ 6,800	$ 5,280	$ 8,245	$ 3,636	$ 1,827	
2002	6,234	4,952	6,120	2,977	1,703	
Earnings Before Income Taxes						
2003	1,675	916	1,960	906	350	
2002	1,577	843	1,535	649	290	
Net Earnings						
2003	1,132	576	1,297	609	231	
2002	1,061	517	1,055	449	201	

4. Acquisitions - Acquisitions during the six months ended December 31, 2003 consist primarily of the Company's September 2003 acquisition of a controlling interest in Wella AG (Wella). Through a stock purchase agreement with the majority shareholders of Wella and a tender offer made on the remaining shares, the Company acquired a total of 81% of Wella's outstanding shares, including 99% of Wella's outstanding voting class shares, for a total purchase price of 4.67 billion Euros, excluding acquisition costs (approximately $5.1 billion based on exchange rates on the date of the transactions). The Wella business consists of professional hair care, retail hair care, and cosmetics and fragrances divisions with over $3 billion in annual net sales. The operating results of the Wella business are reported in the Company's Beauty Care business segment.

The acquisition of Wella's shares has been accounted for as a purchase business combination in accordance with Statement of Financial Accounting Standards (SFAS) No. 141, "Business Combinations." Accordingly, the Company's consolidated financial statements include the results of Wella from the date on which the Company acquired control (September 2, 2003).

The Company is in the process of obtaining independent appraisals for the purpose of allocating the purchase price to the individual assets acquired and liabilities assumed. This will result in potential adjustments to the carrying values of Wella's recorded assets and liabilities, the establishment of certain intangible assets, the determination of the useful lives of intangible assets, some of which may have indefinite lives not subject to amortization, and the determination of the amount of any residual value that will be allocated to goodwill. The preliminary allocation of the purchase price included in the current period balance sheet is based on the current best estimates of management and is subject to revision based on final determination of fair values. The Company also is completing its analysis of collaboration plans that may result in additional purchase price allocation adjustments. The Company anticipates the valuations and other studies will be substantially completed in the fourth quarter of the fiscal year.

The following table provides pro forma results of operations for the six months ended December 31, 2003 and 2002 and for the three months ended December 31, 2002, as if Wella had been acquired as of the beginning of each fiscal year presented. The pro forma results include certain adjustments, including adjustments to convert Wella's historical financial information from International Accounting Standards (IAS) into accounting principles generally accepted in the United States of America (U.S. GAAP), estimated interest impacts from funding of the acquisition and estimated amortization of identifiable intangible assets. However, pro forma results do not include any anticipated cost savings or other effects of the Wella acquistion. Accordingly, such amounts are not necessarily indicative of the results that would have occurred if the acquisition had occurred on the dates indicated or that may result in the future.

PRO FORMA RESULTS (Amounts in millions)

	Six Months Ended December 31		Three Months Ended
	2003	2002	December 31, 2002
Net Sales	$25,932	$23,508	$11,936
Net Earnings	3,550	2,995	1,532

Diluted net earnings per common share	2.54	2.13	1.09

5. Goodwill and Intangible Assets - Goodwill as of December 31, 2003 is allocated by reportable segment as follows (amounts in millions):

	Fabric & Home Care	Baby & Family Care	Beauty Care	Health Care
Goodwill, June 30, 2003	$460	$884	$6,600	$2,908
Acquisition (Note 4)			4,465	143
Translation & Other	4	53	704	26
Goodwill, December 31, 2003	$464	$937	$11,769	$3,077

The increase in goodwill within the Beauty Care segment is primarily due to the preliminary allocation of goodwill related to the acquisition of Wella and translation. The increase in goodwill within Health Care is primarily due to a small acquisition.

Identifiable intangible assets as of December 31, 2003 are comprised of:

Amounts in Millions

	Gross Carrying Amount	Accumulated Amortization
Amortizable intangible assets	$2,269	$517
Non-amortizable intangible assets	2,599	169
Total identifiable intangible assets	$4,868	$686

Amortizable intangible assets consist principally of patents, technology and trademarks. The non-amortizable intangible assets consist primarily of trademarks. Gross amortizable intangible assets increased by $962 million during the six months ended December 31, 2003, primarily due to intangibles from the Wella acquisition, translation and several small brand acquisitions. Non-amortizable intangibles increased by $933 million during the six months ended December 31, 2003 primarily due to trademarks from the Wella acquisition and translation. These estimated allocations of the Wella purchase price to specific assets acquired, including identifiable intangibles, are subject to revision based on the final determination of fair values, as discussed in footnote 4.

The amortization of intangible assets for the three and six months ended December 31, 2003 is $47 million and $81 million, respectively.

6. Pro Forma Stock-Based Compensation - The Company has stock-based compensation plans under which stock options are granted to key managers and directors at the market price on the date of grant. In prior years, the majority of grants to key managers were issued in the quarter ended September 30. While certain grants were issued during the six months ended December 31, 2003, the Company will issue the fiscal 2004 key manager grants in the quarter ended March 31, 2004. Grants issued since September 2002 are vested after three years and have a ten-year life. Grants issued

from 1999 through 2002 are fully exercisable after three years and have a fifteen-year life. The Company also makes other grants to employees, for which vesting terms and option lives differ.

Pursuant to SFAS No. 123, "Accounting for Stock-Based Compensation," the Company has elected to account for its employee stock option plans under APB Opinion No. 25, "Accounting for Stock Issued to Employees," which recognizes expense based on the intrinsic value at date of grant. As stock options have been issued with exercise prices equal to the market value of the underlying shares on the grant date, no compensation cost has resulted. Had compensation cost for all options granted been determined based on the fair value at grant date consistent with SFAS No. 123, the Company's net earnings and earnings per share would have been as follows:

	Three Months Ended December 31		Six Months Ended December 31	
	2003	2002	2003	2002
Net earnings				
As reported	$1,818	$1,494	$3,579	$2,958
Pro forma expense	65	101	147	205
Pro forma	1,753	1,393	3,432	2,753
Net earnings per common share				
Basic				
As reported	$1.38	$1.13	$2.71	$2.23
Pro forma adjustments	(0.05)	(0.08)	(0.11)	(0.16)
Pro forma	1.33	1.05	2.60	2.07
Diluted				
As reported	1.30	1.06	2.56	2.10
Pro forma adjustments	(0.05)	(0.07)	(0.12)	(0.14)
Pro forma	1.25	0.99	2.44	1.96

The assumptions used to calculate the fair value of options granted are evaluated and revised, as necessary, to reflect market conditions and experience.

7. Medicare Prescription Drug Act - The Medicare Prescription Drug, Improvement and Modernization Act of 2003 was signed into law on December 8, 2003. This Act introduced both a Medicare prescription-drug benefit and a federal subsidy to sponsors of retiree health-care plans that provide a benefit at least "actuarially equivalent" to the Medicare benefit. The Act will not have a material impact on the Company's accumulated postretirement benefit obligation or net postretirement benefit costs, due primarily to the relative size of the expected federal subsidy, the Company's assumption that its prescription benefits are at least as beneficial as those provided under Medicare, and the Company's expectation that the Act will not materially impact participation rates or per capita claims costs. Accordingly, the effects of the Act will be factored into the Company's normal year-end measurement process for other post-employment benefit (OPEB) plans, which will decrease the Company's postretirement benefit obligation reported at June 2004 and periodic net postretirement benefit costs beginning in fiscal 2005. Specific authoritative guidance on the accounting for the federal subsidy is pending and that guidance, if issued after the effects of the Act are reflected in the measurement of the accumulated postretirement benefit obligation or net postretirement benefit costs, could require a subsequent change to such reported information.

8. Other New Pronouncements - In January and December 2003, the FASB issued FASB Interpretation No. 46 (FIN 46) and No. 46, revised (FIN 46R), "Consolidation of Variable Interest Entities". These statements, which address preceived weaknesses in accounting for entities commonly known as special-purpose or off-balance-sheet, require consolidation of certain interests or arrangements by virtue of holding a controlling financial

interest in such entities. Certain provisions of FIN 46R related to interests in special purpose entities were applicable for the period ended December 31, 2003. The Company must apply FIN 46R to their interests in all entities subject to the interpretation as of the first interim or annual period ending after March 15, 2004. Adoption of this new method of accounting for variable interest entities did not and is not expected to have a material impact on the Company's consolidated results of operations and financial position.

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

OVERVIEW

The Company markets approximately 300 products in more than 160 countries around the world in five distinct business segments: Fabric and Home Care, Beauty Care, Baby and Family Care, Health Care and Snacks and Beverages.

During the first six months of the fiscal year through December 31, 2003, the Company delivered strong top line results and double-digit earnings growth, despite widespread competitive activity. All business segments posted volume and earnings growth. Results include the impact of the Wella acquisition which was completed in September 2003. Sales grew ahead of volume due to positive foreign exchange impacts, partially offset by mix (driven by high growth in developing markets) and pricing activity. Earnings increased due to the scale benefit of volume, the completion of the Company's restructuring program which had $211 million of after tax charges in the base period, and lower manufacturing costs. Earnings growth was partially offset by continued marketing investments in the base business and in support of product initiatives.

Going forward, business and market uncertainties may affect results. For a discussion of key factors that could impact and must be managed by the Company, please refer to Management's Discussion and Analysis in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 2003.

RESULTS OF OPERATIONS - Three Months Ended December 31, 2003

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
(Amounts in Millions Except Per Share Amounts)
Consolidated Earnings Information

	Three Months Ended December 31		
	2003	2002	% CHG
NET SALES	$ 13,221	$ 11,005	20 %
COST OF PRODUCTS SOLD	6,324	5,490	15 %
GROSS MARGIN	6,897	5,515	25 %
MARKETING, RESEARCH, ADMINISTRATIVE & OTHER	4,155	3,267	27 %
OPERATING INCOME	2,742	2,248	22 %
TOTAL INTEREST EXPENSE	149	143	
OTHER NON-OPERATING INCOME, NET	29	74	
EARNINGS BEFORE INCOME TAXES	2,622	2,179	20 %
INCOME TAXES	804	685	
NET EARNINGS	1,818	1,494	22 %
EFFECTIVE TAX RATE	30.7%	31.4%	

PER COMMON SHARE:			
BASIC NET EARNINGS	$ 1.38	$ 1.13	22 %
DILUTED NET EARNINGS	$ 1.30	$ 1.06	23 %
DIVIDENDS	$ 0.45	$ 0.41	
AVERAGE DILUTED SHARES OUTSTANDING	1,400.4	1,402.6	

COMPARISONS AS A % OF NET SALES			Basis Pt Chg
COST OF PRODUCTS SOLD	47.8%	49.9%	
GROSS MARGIN	52.2%	50.1%	210
MARKETING, RESEARCH, ADMINISTRATIVE & OTHER	31.4%	29.7%	
OPERATING MARGIN	20.7%	20.4%	30
EARNINGS BEFORE INCOME TAXES	19.8%	19.8%	
NET EARNINGS	13.8%	13.6%	

Unit volume for the quarter increased 19 percent, with all business segments and geographic regions reporting unit volume growth. Excluding the impact of acquisitions and divestitures, primarily Wella, unit volume increased nine percent. Beauty Care led the business segments with unit volume growth of 45 percent. Excluding acquisitions and divestitures, Beauty Care volume increased 10 percent. Health Care and Fabric and Home Care volume increased 17 and nine percent, respectively. Developing markets delivered strong, double-digit unit volume growth.

Net sales increased 20 percent to $13.22 billion. Foreign exchange had a positive impact of four percent due primarily to the strengthening of the Euro, Canadian dollar, British pound and Japanese yen, offset by weakening of the Mexican Peso and Venezuelan Bolivar. Mix was driven primarily by continued high growth in developing markets, including China and Latin America. Pricing activity, largely in response to competition, reduced sales by one percent. Pricing includes responses to competitive actions across multiple categories including family care in North America and Fabric and Home Care in Europe and the Middle East. The table below identifies the drivers to net sales changes versus the prior year quarter by business segment:

	Volume					
	With Acquisitions/ Divestitures	Without Acquisitions/ Divestitures	FX	Price	Mix/Other	Tot Imp
FABRIC AND HOME CARE	9%	9%	4%	-1%	-2%	10%
BEAUTY CARE	45%	10%	5%	0%	0%	50%
BABY AND FAMILY CARE	4%	4%	5%	-1%	-2%	6%
HEALTH CARE	17%	17%	4%	1%	0%	22%
SNACKS AND BEVERAGES	1%	1%	4%	-2%	3%	6%
TOTAL COMPANY	19%	9%	4%	-1%	-2%	20%

Note: These sales percentage changes are approximations based on quantitative formulas that are consistently applied.

Net earnings increased 22 percent to $1.82 billion. Earnings growth was primarily driven by volume benefits, the completion of the prior year restructuring program (which included $98 million after tax in the base period) and lower manufacturing costs. These improvements were partially offset by

marketing investments to support base business growth and new initiatives.

Net earnings per share were $1.30, an increase of 23 percent, including a slightly accretive effect from Wella.

Gross margin expanded 210 basis points. Of this, 70 basis points ($75 million before tax) relates to restructuring charges in the prior period. Of the remaining 140 basis points of expansion, approximately half was driven by the addition of Wella, which has a higher gross margin than the base business. The remaining half was driven by the scale benefit of volume growth, the mix impact of higher volume in the Health and Beauty Care businesses, and product cost savings.

Marketing, Research, Administrative and Other Costs (MRA&O) as a percentage of net sales increased 170 basis points. The large majority of this basis point increase is due to Wella, reflecting a higher ratio of marketing expenses to sales than the base business and initial post-acquisition costs. The remaining increase in spending reflects investments behind the base business and support for initiatives. The addition of Wella and increased marketing investments more than offset the basis point improvement due to the non-recurrence of restructuring program charges ($57 million before tax) in the base period.

RESULTS OF OPERATIONS - Six Months Ended December 31, 2003

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
(Amounts in Millions Except Per Share Amounts)
Consolidated Earnings Information

	Six Months Ended December 31		
	2003	2002	% CHG
NET SALES	$ 25,416	$ 21,801	17 %
COST OF PRODUCTS SOLD	12,203	10,979	11 %
GROSS MARGIN	13,213	10,822	22 %
MARKETING, RESEARCH, ADMINISTRATIVE & OTHER	7,828	6,395	22 %
OPERATING INCOME	5,385	4,427	22%
TOTAL INTEREST EXPENSE	290	287	
OTHER NON-OPERATING INCOME, NET	69	177	
EARNINGS BEFORE INCOME TAXES	5,164	4,317	20 %
INCOME TAXES	1,585	1,359	
NET EARNINGS	3,579	2,958	21 %
EFFECTIVE TAX RATE	30.7%	31.5%	
PER COMMON SHARE:			
BASIC NET EARNINGS	$ 2.71	$ 2.23	22 %
DILUTED NET EARNINGS	$ 2.56	$ 2.10	22 %
DIVIDENDS	$ 0.91	$ 0.82	
AVERAGE DILUTED SHARES OUTSTANDING	1,399.6	1,404.9	

COMPARISONS AS A % OF NET SALES			Basis Pt Chg
COST OF PRODUCTS SOLD	48.0%	50.4%	
GROSS MARGIN	52.0%	49.6%	240
MARKETING, RESEARCH, ADMINISTRATIVE & OTHER	30.8%	29.3%	
OPERATING MARGIN	21.2%	20.3%	90
EARNINGS BEFORE INCOME TAXES	20.3%	19.8%	
NET EARNINGS	14.1%	13.6%	

Fiscal year to date, unit volume increased 16 percent. All business segments and geographic regions delivered unit volume growth. The lower growth rate year to date versus the October - December quarter reflects the acquisition of Wella in September. Excluding acquisitions and divestitures, unit volume increased nine percent through the first six months of the fiscal year. Volume growth was led by Beauty Care, up 33 percent, and Health Care, up 20 percent. Developing markets delivered double-digit volume growth with strong results in China and Central and Eastern Europe.

For the first six months of the fiscal year, net sales increased 17 percent to $25.42 billion. Foreign exchange contributed three percent to sales growth. Pricing and mix combined for a negative two percent impact on sales growth. Pricing investments include activities to drive top line growth in multiple businesses and to respond to competition. Mix was driven primarily by strong growth in developing markets. The table below identifies the drivers to net sales changes fiscal year to date versus the prior year by business segment:

	Volume					
	With Acquisitions/ Divestitures	Without Acquisitions/ Divestitures	FX	Price	Mix/Other	Total Impact
FABRIC AND HOME CARE	9%	8%	3%	-1%	-2%	9%
BEAUTY CARE	33%	9%	4%	-1%	-1%	35%
BABY AND FAMILY CARE	5%	5%	4%	-1%	-1%	7%
HEALTH CARE	20%	20%	3%	0%	-1%	22%
SNACKS AND BEVERAGES	2%	2%	4%	-1%	2%	7%
TOTAL COMPANY	16%	9%	3%	-1%	-1%	17%

Note: These sales percentage changes are approximations based on quantitative formulas that are consistently applied.

Fiscal year to date earnings increased 21 percent to $3.58 billion. Earnings growth was driven by volume benefits, the completion of the restructuring program (which included $211 million of after tax charges in the prior year period) and product cost savings. Earnings growth was partially offset by continued marketing investments in the base business and in support of initiatives. Net earnings per share increased 22 percent to $2.56 compared to $2.10 in the base period.

Gross margin fiscal year to date was 52.0 percent compared to 49.6 percent in the prior year, an increase of 240 basis points. The gross margin improvement was driven by the scale benefit of volume, the reduction of before tax charges related to the completed restructuring program of $163 million, the addition of Wella which has a higher gross margin than the base business, the mix shift to the Health and Beauty Care segments (which have higher gross margins than the Company average) and base business product cost savings. These improvements were partially offset by the impact of pricing and higher commodity costs.

Marketing, Research, Administrative and Other Costs (MRA&O) fiscal year to date increased to 30.8 percent from 29.3 percent of net sales in the comparable base period, an increase of 150 basis points. The majority of the increase is due to Wella, reflecting a higher ratio of marketing expenses to sales than the base business and initial post-acquisition costs. Marketing investments were made to drive growth on the base business and in support of initiatives. The spending increases associated with Wella and marketing investments more than offset the reduction in prior year restructuring program charges of $120 million before tax.

BUSINESS SEGMENT DISCUSSION

The following tables provide supplemental information on net earnings and the underlying drivers of net sales changes by business segment for the quarter ended December 31, 2003 and fiscal year to date:

THE PROCTER & GAMBLE COMPANY AND SUBSIDIARIES
(Amounts in Millions Except Per Share Amounts)
Consolidated Earnings Information

	Three Months Ended December 31, 2003				
	Net Sales	% Change Versus Year Ago	Earnings Before Income Taxes	% Change Versus Year Ago	N Earnin
FABRIC AND HOME CARE	$ 3,407	10%	$ 843	10%	$ 5
BEAUTY CARE	4,492	50%	1,047	43%	6
BABY AND FAMILY CARE	2,673	6%	444	0%	2
HEALTH CARE	1,908	22%	500	34%	3
SNACKS AND BEVERAGES	931	6%	188	12%	1
TOTAL BUSINESS SEGMENT	13,411	21%	3,022	22%	1,9
CORPORATE	(190)	n/a	(400)	n/a	(16
TOTAL COMPANY	13,221	20%	2,622	20%	1,8

	Six Months Ended December 31, 2003				
	Net Sales	% Change Versus Year Ago	Earnings Before Income Taxes	% Change Versus Year Ago	N Earnin
FABRIC AND HOME CARE	$ 6,800	9%	$ 1,675	6%	$ 1,1
BEAUTY CARE	8,245	35%	1,960	28%	1,2
BABY AND FAMILY CARE	5,280	7%	916	9%	5
HEALTH CARE	3,636	22%	906	40%	6
SNACKS AND BEVERAGES	1,827	7%	350	21%	2
TOTAL BUSINESS SEGMENT	25,788	17%	5,807	19%	3,8
CORPORATE	(372)	n/a	(643)	n/a	(2
TOTAL COMPANY	25,416	17%	5,164	20%	3,5

FABRIC AND HOME CARE

For the quarter, volume was up nine percent behind Tide, Gain, Era and the continued success of initiatives including Mr. Clean Magic Eraser and Swiffer Duster. Net sales increased 10 percent to $3.41 billion. Sales growth includes a positive four percent foreign exchange impact that was partially offset by negative pricing and mix. Mix was driven by continued strong growth in developing markets, particularly China and Central and Eastern Europe. Pricing

had a one percent impact on sales and represents primarily the continuation of prior period actions to maintain competitiveness. Net earnings increased 11 percent to $570 million driven primarily by volume, as lower manufacturing costs were offset by the profit impact of continued pricing actions.

For the first six months of the fiscal year, Fabric and Home Care volume increased nine percent. Net sales increased nine percent, including a positive foreign exchange impact of three percent. Mix and pricing impacts combined for a negative three percent impact on sales. Net earnings increased seven percent. Earnings growth lags sales growth for the first six months of the fiscal year due to a high base period comparison in the July - September quarter.

BEAUTY CARE

Total volume in the October - December quarter increased 45 percent including acquisitions and divestitures, primarily Wella. Excluding acquisitions and divestitures, Beauty Care volume increased 10 percent. Strong base business results were led by double-digit growth by the Pantene, Head & Shoulders and Herbal Essences hair care brands, Olay skin care and the Always feminine care brand. Net sales increased 50 percent to $4.49 billion, including a positive five percent foreign exchange impact. Net earnings were $681 million, an increase of 34 percent, due to strong top line growth, including Wella. Gross margin expansion was partially offset by the higher ratio of marketing expenses to sales for the Wella business, increased marketing investments in the North America hair care and skin care businesses and in support of initiatives (including Boss Intense, Lacoste Pour Femme, Rejoice in Greater China, Always/Alldays upgrades, Herbal Essences and Pantene in Western Europe and the geographic expansion of Olay Regenerist and Total Effects). The Wella acquisition was accretive to Beauty Care earnings. Interest and amortization expenses associated with Wella are included in Corporate.

For the six months ended December 31, Beauty Care volume increased 33 percent. Volume growth fiscal year to date reflects the Wella acquisition, completed in September, and double-digit increases in developing markets. Net sales increased 35 percent to $8.25 billion. A positive foreign exchange impact of four percent was partially offset by pricing and mix. Net earnings increased 23 percent to $1.30 billion. Volume benefits and lower product costs were partially offset by additional marketing investments to support the base business and initiatives.

BABY AND FAMILY CARE

For the quarter ended December 31, volume increased four percent behind strong growth in baby care - primarily in Western Europe and developing markets. Family care volume was flat due, in part, to high promotional spending levels by key competitors. Net sales increased six percent to $2.67 billion. Foreign exchange was a positive impact of five percent; the impact of volume on sales was partially offset by pricing and mix. Mix was primarily driven by strong growth in mid-tier diaper products in developing markets. Pricing had a negative one percent effect on sales in response to increased competitive promotional activity in North America family care. Earnings grew two percent against strong base period results (21 percent increase) to $281 million. Earnings in baby care increased due to volume and cost savings, largely offset by the aforementioned pricing investments and rising commodity costs in family care.

Fiscal year to date, Baby and Family Care volume increased five percent. Baby care volume increased high single-digits, while family care volume increased low single-digits. Net sales increased seven percent to $5.28 billion, including a positive foreign exchange impact of four percent. Price and mix combined for a negative two percent impact. Earnings were $576 million, an increase of 11 percent, as profit growth behind volume and product cost savings was partially offset by pricing investments and increased commodity costs.

HEALTH CARE

Health Care unit volume increased 17 percent during the October - December quarter driven by the continued success of Actonel, Prilosec OTC and oral care. Vicks also posted strong unit volume growth due to the early cough/cold season in North America. Net sales increased 22 percent to $1.91 billion aided by a positive four percent foreign exchange impact and one percent for pricing. Net earnings were $333 million, an increase of 32 percent, on strong volume, lower manufacturing costs and margin expansion due to product mix. Marketing spending increased versus the base period primarily behind continued support of Prilosec OTC, Crest Whitestrips and Crest Night Effects. While double-digit top line growth is expected for the fiscal year, Prilosec OTC volume in the remaining quarters is expected to reflect consumption levels following the successful launch in September and continued strong results in October - December quarter.

Fiscal year to date, Health Care volume increased 20 percent. Net sales were $3.64 billion, an increase of 22 percent. Sales growth was impacted by a positive three percent for foreign exchange. Mix was a negative one percent impact driven primarily by developing market growth. Net earnings increased 36 percent to $609 million. Earnings increased behind sales growth and margin expansion, including the impact of product cost savings.

SNACKS AND BEVERAGES

Snacks and Beverages unit volume increased one percent. Beverages volume increased two percent driven primarily by the Folgers AromaSeal initiative. Net sales increased six percent to $931 million driven primarily by a foreign exchange benefit of four percent. Volume and mix gains were partially offset by increased merchandising costs to support the continued high level of promotional activity in the coffee category. Manufacturing costs increased behind initiative start-up expenses. Net earnings increased 11 percent to $122 million behind sales growth and lower marketing and administrative spending.

For the first six months of the fiscal year, Snacks and Beverages volume increased two percent. Net sales increased seven percent to $1.83 billion, reflecting volume growth, a positive foreign exchange impact of four percent and combined mix and pricing of one percent. Net earnings in Snacks and Beverages increased 15 percent to $231 million.

CORPORATE

Corporate includes certain operating and non-operating activities, as well as eliminations to adjust management reporting principles to United States Generally Accepted Accounting Principles (U.S. GAAP). For the quarter, net sales were -$190 million compared to -$68 million in the prior period, primarily driven by eliminations due to stronger joint venture sales. Net earnings for the quarter were -$169 million compared to -$166 million in the comparable prior period. Results primarily reflect lower costs from the restructuring program offset by charges associated with Wella and hedging impacts. For the first six months of the fiscal year, Corporate net sales were -$372 million compared to -$185 million in the prior period. Net earnings for the six month period were -$266 million versus -$325 million in the same period year ago.

FINANCIAL CONDITION

Operating Activities

Cash generated from operating activities for the six months ended December 31, 2003 was $3.96 billion compared to $4.33 billion in the comparable prior period. Strong earnings, adjusted for non-cash items (depreciation, amortization and deferred income taxes) generated $4.67 billion of cash flow and were partially offset by increases in working capital.

Working capital increased by $0.9 billion during the period. Accounts receivable increased by $0.5 billion due mainly to strong December shipments. Accounts

payable decreased reflecting the Company's continued effort to accelerate payments to suppliers in order to maximize efficiencies and capture all discounts.

Cash generated from operating activities is down $0.4 billion versus the comparable prior year period. The impact of increased earnings in the current period were offset by a larger increase in working capital and the impact of dividends received from a joint venture in the base period.

Investing Activities

Investing activities in the current year decreased cash by $6.11 billion compared to a decrease of $0.5 billion in prior year period. The primary driver was the acquisition of Wella for approximately $5.10 billion. Additional current year acquisitions include Glide Dental Floss and fabric care brands in Western Europe and the Middle East. There was no acquisition activity in the comparable prior year period.

Capital spending increased to $810 million versus $616 million in the comparable prior period. Capital spending as a percent of sales increased slightly versus the comparable period, but was still below the Company's target of four percent.

Financing Activities

Financing activities in the current fiscal year to date increased cash by $1.14 billion, representing a year-over-year cash increase of $3.29 billion. Cash from financing includes an increase in short and long-term debt to support the Wella acquisition. The Company issued $1.38 billion aggregate principal amount of notes with varying maturity dates. Additionally, two bonds matured reducing long-term debt $993 million. The net change in long-term debt is an increase of $412 million versus June 30. Treasury share repurchases were roughly in line with the comparable base period. Treasury share repurchases through the remainder of the fiscal year are expected to be higher than the prior year. The Company purchased approximately $200 million of stock in the January - June 2003 period.

Current assets net of current liabilities declined by approximately $3.3 billion during the six months ended December 31, 2003. This decline was primarily caused by the issuance of commercial paper to partially fund the acquisition of Wella AG. The Company anticipates being able to support its short-term liquidity through cash generated from operations. The Company also has very strong long and short-term credit ratings which will enable it to refinance this debt at favorable rates in the commercial paper and bond markets. In addition, the Company has agreements with a diverse group of creditworthy financial institutions that, should they be needed, would provide sufficient credit funding to meet short-term financing requirements.

Item 4. Controls and Procedures

The Company's Chairman of the Board, President and Chief Executive, A.G. Lafley, and the Company's Chief Financial Officer, Clayton C. Daley, Jr., have evaluated the Company's internal controls and disclosure controls systems as of the end of the period covered by this report.

Messrs. Lafley and Daley have concluded that the Company's disclosure controls systems are functioning effectively to provide reasonable assurance that the Company can meet its disclosure obligations. The Company's disclosure controls system is based upon a global chain of financial, staff and general business reporting lines that converge in the world-wide headquarters of the Company in Cincinnati, Ohio. The reporting process is designed to ensure that information

required to be disclosed by the Company in the reports that it files or submits with the Commission is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. Consistent with SEC suggestion, the Company has a Disclosure Committee consisting of key Company personnel designed to review the accuracy and completeness of all disclosures made by the Company.

In connection with the evaluation described above, no changes in the Company's internal control over financial reporting occurred during the Company's second fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

(3-1) Amended Articles of Incorporation (Incorporated by reference to Exhibit (3-1) of the Company's Annual Report on Form 10-K for the year ended June 30, 2003).

(3-2) Regulations (Incorporated by reference to Exhibit (3-2) of the Company's Annual Report on Form 10-K for the year ended June 30, 2003).

(11) Computation of Earnings per Share.

(12) Computation of Ratio of Earnings to Fixed Charges.

(31) Rule 13a-14(a)/15d-14(a) Certifications.

(32) Section 1350 Certifications.

(b) Reports on Form 8-K

During the quarter ended December 31, 2003, the Company did not file any Current Reports on Form 8-K. During the quarter ended December 31, 2003, the Company furnished reports on Form 8-K pursuant to Item 9 ("Regulation FD Disclosure") dated October 14, 2003, relating to Chairman, President and Chief Executive A.G. Lafley's address to the shareholders at the Company's annual meeting; and dated December 11, 2003, relating to updating previously issued guidance for the October-December 2003 quarter and 2003/04 fiscal year. The Company also furnished reports on Form 8-K containing information pursuant to Item 12 ("Results of Operations and Financial Condition") dated October 27, 2003, relating to the announcement of earnings for the quarter ended September 30, 2003.

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.

THE PROCTER & GAMBLE COMPANY

/S/JOHN K. JENSEN

(John K. Jensen)
Vice President and Comptroller

February 3, 2004

Date

EXHIBIT INDEX

Exhibit No.		Page No.
(3-1)	Amended Articles of Incorporation (Incorporated by reference to Exhibit (3-1) of the Company's Annual Report on Form 10-K for the year ended June 30, 2003).	
(3-2)	Regulations (Incorporated by reference to Exhibit (3-2) of the Company's Annual Report on Form 10-K for the year ended June 30, 2003).	
(11)	Computation of Earnings per Share.	25
(12)	Computation of Ratio of Earnings to Fixed Charges.	26
(31)	Rule 13a-14(a)/15d-14(a) Certifications.	27-30
(32)	Section 1350 Certifications.	31-32