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INTERNATIONAL FLAVORS & FRAGRANCES INC
Form 10-Q
August 07, 2006

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT UNDER SECTION 13 OF

THE SECURITIES EXCHANGE ACT OF 1934

For Quarterly Period Ended June 30, 2006

Commission file number 1-4858

INTERNATIONAL FLAVORS & FRAGRANCES INC.

(Exact name of registrant as specified in its charter)

New York

13-1432060

(State or other jurisdiction of
incorporation or organization)

(IRS Employer
Identification No.)

521 West 57th Street, New York, N.Y. 10019-2960
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code (212) 765-5500

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Sections 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding twelve months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes [] No []

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer [] Accelerated filer [] Non-accelerated filer []

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes [] No []

Number of shares outstanding as of August 3, 2006: 90,670,305

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

INTERNATIONAL FLAVORS & FRAGRANCES INC. CONSOLIDATED BALANCE SHEET (DOLLARS IN THOUSANDS) (Unaudited)

ASSETS	6/
<hr style="border-top: 1px dashed black;"/>	
Current Assets:	
Cash and cash equivalents	\$
Short-term investments	3
Trade receivables	(
Allowance for doubtful accounts	2
Inventories: Raw materials	2
Work in process	2
Finished goods	-----
Total Inventories	4
Deferred income taxes	-----
Other current assets	-----
Total Current Assets	9
<hr style="border-top: 1px dashed black;"/>	
Property, Plant and Equipment, at cost	1,0
Accumulated depreciation	(5)

	4
<hr style="border-top: 1px dashed black;"/>	
Goodwill	6
Intangible Assets, net	-----
Other Assets	2
<hr style="border-top: 1px dashed black;"/>	
Total Assets	\$ 2,4
<hr style="border-top: 3px double black;"/>	
LIABILITIES AND SHAREHOLDERS' EQUITY	
<hr style="border-top: 1px dashed black;"/>	
Current Liabilities:	
Bank borrowings, overdrafts and current portion of long-term debt	\$ 3
Accounts payable	1
Accrued payrolls and bonuses	-----
Dividends payable	-----
Income taxes	-----
Restructuring and other charges	1
Other current liabilities	-----
Total Current Liabilities	7
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Other Liabilities:	
Long-term borrowings	4
Deferred gains	-----
Retirement liabilities	2
Other liabilities	1

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Total Other Liabilities	8
<hr/>	
Commitments and Contingencies (Note 9)	
Shareholders' Equity:	
Common stock 12 1/2 (cent) par value; authorized 500,000,000 shares; issued 115,761,840 shares	
Restricted Stock	
Capital in excess of par value	
Retained earnings	1,8
Accumulated other comprehensive income:	
Cumulative translation adjustment	(
Accumulated losses on derivatives qualifying as hedges (net of tax)	(
Minimum pension liability adjustment (net of tax)	(1
<hr/>	
Treasury stock, at cost - 24,820,919 shares in 2006 and 23,047,349 shares in 2005	1,7 (8
<hr/>	
Total Shareholders' Equity	9
<hr/>	
Total Liabilities and Shareholders' Equity	\$ 2,4 =====

See Notes to Consolidated Financial Statements

INTERNATIONAL FLAVORS & FRAGRANCES INC.
CONSOLIDATED STATEMENT OF INCOME
(AMOUNTS IN THOUSANDS EXCEPT PER SHARE AMOUNTS)
(Unaudited)

	3 Mo
	200
<hr/>	
Net sales	\$ 530
<hr/>	
Cost of goods sold	302
Research and development expenses	45
Selling and administrative expenses	87
Amortization of intangibles	3
Restructuring and other charges (income)	
Interest expense	6
Other (income) expense, net	
<hr/>	
	445
<hr/>	
Income before taxes on income	84
Taxes on income	23
<hr/>	
Net income	61
<hr/>	
Other comprehensive income:	
Foreign currency translation adjustments	9
Accumulated gains (losses) on derivatives qualifying as hedges (net of tax)	(18
<hr/>	
Comprehensive income	\$ 52

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	=====
Net Income per share - basic	\$
Net Income per share - diluted	\$
Average number of shares outstanding - basic	90
Average number of shares outstanding - diluted	91
Dividends declared per share	\$0
	6

	200

Net sales	\$1,041

Cost of goods sold	597
Research and development expenses	91
Selling and administrative expenses	173
Amortization of intangibles	7
Restructuring and other charges	
Interest expense	11
Other (income) expense, net	

	881

Income before taxes on income	160
Taxes on income	45

Net income	114
Other comprehensive income:	
Foreign currency translation adjustments	14
Accumulated gains (losses) on derivatives qualifying as hedges (net of tax)	(17)

Comprehensive income	\$ 111
	=====
Net Income per share - basic	\$
Net Income per share - diluted	\$
Average number of shares outstanding - basic	91
Average number of shares outstanding - diluted	91
Dividends declared per share	\$0

See Notes to Consolidated Financial Statements

INTERNATIONAL FLAVORS & FRAGRANCES INC.
CONSOLIDATED STATEMENT OF CASH FLOWS
(DOLLARS IN THOUSANDS)
(Unaudited)

	6 Months E

	2006

Cash flows from operating activities:	
Net income	\$ 114,872
Adjustments to reconcile to net cash provided by operations:	
Depreciation and amortization	44,602
Deferred income taxes	329
Gain on disposal of assets	(3,881)
Changes in assets and liabilities:	

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Current receivables	(60,327)
Inventories	1,163
Current payables	(2,336)
Changes in other assets, net	16,358
Changes in other liabilities, net	10,185

Net cash provided by operations	120,965

Cash flows from investing activities:	
Net change in short-term investments	25
Additions to property, plant and equipment	(19,806)
Proceeds from disposal of assets	6,504

Net cash used in investing activities	(13,277)

Cash flows from financing activities:	
Cash dividends paid to shareholders	(33,990)
Net change in bank borrowings and overdrafts	(32,508)
Net change in commercial paper outstanding	281,521
Repayments of long-term debt	(499,306)
Proceeds from issuance of stock under equity compensation plans	23,146
Purchase of treasury stock	(91,315)

Net cash (used in) provided by financing activities	(352,452)

Effect of exchange rate changes on cash and cash equivalents	2,052

Net change in cash and cash equivalents	(242,712)
Cash and cash equivalents at beginning of year	272,545

Cash and cash equivalents at end of period	\$ 29,833
	=====
Interest paid	\$ 24,051
Income taxes paid	\$ 19,594

See Notes to Consolidated Financial Statements

Notes to Consolidated Financial Statements

These interim statements and management's related discussion and analysis should be read in conjunction with the consolidated financial statements and their related notes and management's discussion and analysis of results of operations and financial condition included in the Company's 2005 Annual Report on Form 10-K. These interim statements are unaudited. In the opinion of the Company's management, all adjustments, including normal recurring accruals, necessary for a fair presentation of the results for the interim periods have been made.

Note 1. New Accounting Pronouncements:

In June 2006, the FASB issued Interpretation No. 48 ("FIN 48"), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109 ("SFAS No. 109"). FIN 48 clarifies the application of SFAS No. 109 to the accounting for income taxes by prescribing the minimum threshold a tax position must meet before being recognized in the financial statements. Under FIN 48, the financial statement effects of a tax position are initially recognized when it is more likely than not, based on its technical merits, the position will be sustained upon examination. A tax position that meets the more likely than not recognition threshold is initially and subsequently measured as the largest amount of

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benefit, determined on a cumulative probability basis that is more likely than not to be realized upon ultimate settlement with the taxing authority. This interpretation is effective for fiscal years beginning after December 15, 2006. The Company is currently assessing the potential impact of this interpretation on its financial position and results of operations.

Note 2. Net Income Per Share:

Net income per share is based on the weighted average number of shares outstanding. A reconciliation of the shares used in the computation of basic and diluted net income per share is as follows:

(Shares in thousands)	Three Months Ended June 30,		Six Mont
	2006	2005	2006
Basic	90,869	93,876	91,202
Assumed conversion under stock plans	918	1,379	795
Diluted	91,787	95,255	91,997

Stock options to purchase 1,014,897 and 1,445,136 shares were outstanding for the second quarter and the first six months of 2006, respectively, and 819,500 and 686,181 for the second quarter and first six months of 2005, respectively, but were not included in the computation of diluted net income per share for the respective periods since the impact was anti-dilutive.

Note 3. Restructuring and Other Charges:

As described in Note 2 to the Consolidated Financial Statements in the Company's 2005 Annual Report, the Company has undertaken a significant reorganization, including management changes, consolidation of production facilities and related actions.

The Company undertook a plan to eliminate approximately 300 positions in manufacturing, selling, research and administration functions, principally in its European and North American operating regions. The majority of affected positions involve employee separation while the balance relates to open positions that will not be filled. As a result of these actions, the Company recognized pre-tax charges of \$23.3 million in 2005 and \$0.4 million in the first six months of 2006. A net gain of \$0.3 million was recognized in the second quarter of 2006 primarily as the result of a \$1.6 million gain recorded on disposition of the Dijon, France land and building, partially offset by \$1.3 million of charges incurred in connection with the restructuring plan. The Dijon assets were written down to their estimated net value in connection with the closure of that facility; the amount realized on disposition exceeded that estimated at the time the original charge was recorded.

Movements in the liabilities related to the restructuring charges, included in Restructuring and other charges or Other liabilities, as appropriate, were (in millions):

Employee- Related	Asset- Related and Other	Total

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Balance December 31, 2005	\$ 29.5	\$ 4.9	\$ 34.4
Additional charges	1.4	(1.0)	0.4
Cash and other costs	(14.0)	1.8	(12.2)
	-----	-----	-----
Balance June 30, 2006	\$ 16.9	\$ 5.7	\$ 22.6
	=====	=====	=====

Consistent with the original plan the balance of employee-related liabilities are expected to be utilized by 2008 as obligations are satisfied; the asset-related charges will be utilized in 2007 on final decommissioning and disposal of the affected equipment.

Note 4. Goodwill and Other Intangible Assets, Net

Goodwill by operating segment at June 30, 2006 and December 31, 2005 is as follows:

(DOLLARS IN THOUSANDS)	Amount
North America	\$ 218,575
Europe	258,607
India	29,209
Latin America	49,046
Asia Pacific	110,145

Total	\$ 665,582
	=====

Trademark and other intangible assets consist of the following amounts:

(DOLLARS IN THOUSANDS)	June 30, 2006	December 31, 2005
Gross carrying value	\$ 177,498	\$ 177,498
Accumulated amortization	77,850	70,429
	-----	-----
Total	\$ 99,648	\$ 107,069
	=====	=====

Amortization expense for the period ended June 30, 2006 was \$7.4 million; estimated annual amortization is \$14.8 million in 2006, \$13.5 million in 2007 and \$6.8 million in 2008 through 2011.

Note 5. Comprehensive Income:

Changes in the accumulated other comprehensive income component of shareholders' equity were as follows:

	Accumulated losses on derivatives	Minimum Pension
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2006 (Dollars in thousands)	Translation adjustments	qualifying as hedges, net of tax	Obligation, net of tax
Balance December 31, 2005	\$ (47,369)	\$ (2,606)	\$ (100,380)
Change	14,354	(17,747)	-
Balance June 30, 2006	\$ (33,015)	\$ (20,353)	\$ (100,380)

2005 (Dollars in thousands)	Translation adjustments	Accumulated losses on derivatives qualifying as hedges, net of tax	Minimum Pension Obligation, net of tax
Balance December 31, 2004	\$ 8,227	\$ (5,694)	\$ (110,705)
Change	(55,499)	1,369	-
Balance June 30, 2005	\$ (47,272)	\$ (4,325)	\$ (110,705)

Note 6. Borrowings:

Debt consists of the following:

(Dollars in thousands)	Rate	Maturities	June 30, 2006
Bank borrowings and overdrafts			\$ 308,936
Current portion of long-term debt	6.45%	2006	-
Current portion of deferred realized gains on interest rate swaps			-
Total current debt			308,936
Commercial Paper classified as long-term			281,521
Japanese Yen notes	2.45%	2008-11	132,623
Other		2011	42
Deferred realized gains on interest rate swaps			1,605
Total long-term debt			415,791
Total debt			\$ 724,727

The 6.45% Notes matured on May 15, 2006. On July 12, 2006, the Company issued an aggregate of \$375.0 million of Senior Unsecured Notes ("the Notes"). The Notes were issued in four series: (i) \$50.0 million in aggregate principal amount of 5.89% Series A Senior Notes due July 12, 2009, (ii) \$100.0 million in aggregate principal amount of 5.96% Series B Notes due July 12, 2011, (iii) \$100.0 million in aggregate principal amount of 6.05% Series C Notes due July 12, 2013 and (iv) \$125.0 million in aggregate principal amount of 6.14% Series D Notes due July 12, 2016. Commercial paper outstanding at June 30, 2006 is classified as

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long-term because proceeds from the Notes issued on July 12, 2006 were used to retire this borrowing.

Note 7. Equity Compensation Plans:

Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123(R) "Share-Based Payment" ("SFAS No. 123 (R)") using the modified prospective method, which requires measurement of compensation cost of all stock-based awards at fair value on the date of grant and recognition of compensation expense over the service periods for awards expected to vest. Under this transition method, compensation cost in 2006 includes the portion vesting in the period for (1) all share-based payments granted prior to, but not vested, as of January 1, 2006, based on the grant date fair value estimated in accordance with

the original provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), and (2) all share-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123(R). The Company will recognize the cost of all employee stock options on a straight-line attribution basis over their respective vesting periods, net of estimated forfeitures. Results for prior periods have not been restated.

The Company previously applied the recognition and measurement principles of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," ("APB 25") and provided the pro forma disclosures required by SFAS No. 123. No compensation expense for employee stock options was previously reflected in net earnings.

The Company changed its valuation model used for estimating the fair value of options granted after January 1, 2006, from a Black-Scholes option-pricing model to a Binomial lattice-pricing model. This change was made in order to provide a better estimate of fair value since the Binomial model is a more flexible method for valuing employee stock options than the Black-Scholes model. The flexibility of the simulated Binomial model stems from the ability to incorporate inputs that change over time, such as volatility and interest rates, and to allow for actual exercise behavior of option holders. The Company is using an average of implied and historical volatility while the expected term assumption was determined based on historical patterns.

The Company has various equity plans under which the Company's officers, senior management, directors and other key employees may be granted options to purchase the Company's common stock or other forms of equity-based awards. Prior to 2004, stock options were the primary form of equity compensation. Beginning in 2004, the Company granted Restricted Stock Unit's ("RSU's") as the principal element of its equity compensation plan for all eligible U.S. - based employees and a majority of eligible overseas employees. Vesting of the RSU's for the Company's officers and senior management has been performance and time based, and for the remainder of eligible employees, vesting is time based; the vesting period is primarily three years from date of grant, however vesting can be adjusted within certain parameters. For a small group of primarily overseas employees, the Company continues to grant stock options.

In 2006, the Board of Directors approved a Long Term Incentive Choice program (the "Program") for the Company's senior management under the Company's 2000 Stock Award and Incentive Plan ("2000 SAIP"). Under the Program, eligible employees can choose from among three equity alternatives and will be granted such equity awards under the 2000 SAIP up to certain dollar awards depending on the participant's grade level. A participant may choose among (1) Purchase Restricted Stock ("PRS"), (2) Stock Settled Appreciation Rights ("SSAR's") or (3) RSU's. The balance of employees who are not eligible under the Program receive RSU's or, as noted above, options.

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Purchase Restricted Stock

PRS provides for the participant to purchase restricted shares of the Company stock at 50% of the fair market value on the grant date of the award. The shares vest on the third anniversary of the grant date, are subject to employment and other specified conditions, and pay dividends if and when paid by the Company. The Company issued 183,183 shares of PRS in the second quarter 2006 for a purchase price of \$3.3 million.

Stock Options and SSAR's

Stock options generally become exercisable on the first anniversary of the grant date and have a maximum term of ten years. SSAR's become exercisable on the third anniversary of the grant date and have a maximum term of seven years. The Company awarded stock options and SSAR's of 212,000 and 141,374, respectively, in the second quarter 2006.

Compensation cost and the related tax benefit for unvested stock option awards issued prior to adoption of SFAS No. 123(R) totaled \$0.6 million and \$0.1 million for the second quarter 2006, respectively, and \$1.9 million and \$0.6 million for the six-month period ended June 30, 2006, respectively.

The following table illustrates the effect on net income and net income per share if the Company had applied the fair value recognition provisions of SFAS No. 123 to measure stock-based compensation expense for outstanding option awards for the quarter and six-month periods ended June 30, 2005. Net income, as reported, includes pre-tax compensation expense related to restricted stock and restricted stock units ("RSU's") of \$2.2 million and \$4.7 million in the second quarter and six-month period ended June 30, 2005. Using the Black-Scholes option valuation model, the estimated fair values of options granted during 2005 were \$10.57 per share.

(Dollars in thousands except per share amounts)	Three Months Ended June 30, 2005	Six Months June 30, 2005
Net income, as reported	\$56,713	
Deduct: Total stock-based employee compensation expense determined under fair value method for all stock option awards, net of related tax effects	1,913	
Pro-forma net income	\$54,800	
Net income per share:		
Basic - as reported	\$0.60	
Basic - pro-forma	\$0.58	
Diluted - as reported	\$0.60	
Diluted - pro-forma	\$0.58	

Principal assumptions used in applying the Black-Scholes model in 2005 and the binomial model in 2006 were:

	2005	2006
Risk-free interest rate	4.2%	5.0%

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Expected life, in years	5	5
Expected volatility	26.9%	21.3%
Expected dividend yield	1.7%	2.1%

The Company utilizes historical information to estimate expected life and forfeitures within the valuation model. The expected term of an option is based on historical employee exercise behavior, vesting terms and a contractual life of nine and one half years to ten years for options and seven years for SSAR's. The risk-free rate for periods within the expected life of the award is based on the U.S. Treasury yield curve in effect at the time of grant. Expected volatility is based on an average of implied and historical volatility of the price of our common shares over the calculated expected life. The Company anticipates paying cash dividends in the future and therefore uses an expected dividend yield in the valuation model using current cash dividends of \$.185 per share each quarter for options granted during 2006. The adoption of SFAS No. 123(R) did not change the way that the Company has accounted for stock options in prior periods.

Stock option and SSAR activity was as follows:

	Shares Subject to Options/SSAR's	Weighted Average Exercise Price	Average Remaining Contractual Term	A Intr (in
Balance at January 1, 2006	6,698,428	\$32.52		
Granted	-	-		
Exercised	187,535	\$29.80		
Cancelled	54,126	\$30.55		
Balance at March 31, 2006	6,456,767	\$32.61	5.7	\$
Granted	353,374	\$35.66		
Exercised	552,168	\$30.13		
Cancelled	160,784	\$46.09		
Balance at June 30, 2006	6,097,189	\$32.70	5.8	\$
Exercisable at March 31, 2006	6,144,512	\$32.34	5.6	\$
Exercisable at June 30, 2006	5,505,544	\$32.24	5.5	\$

The total intrinsic value of options exercised during the second quarter and six-month period ended June 30, 2006 was \$2.5 million and \$3.4 million, respectively.

The Company stock option and SSAR activity for non-vested awards was as follows:

	Shares	Weighted Average Exercise Price
Non-vested at January 1, 2006	1,074,140	\$33.05
Options/SSAR's granted	-	
Options/SSAR's vested	701,056	
Options/SSAR's cancelled	60,829	

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Non-vested at March 31, 2006	312,255	\$37.88
Options/SSAR's granted	353,374	
Options/SSAR's vested	50,990	
Options/SSAR's cancelled	1,668	

Non-vested at June 30, 2006	612,971	\$37.12
	=====	

As of June 30, 2006, there was \$4.8 million of total unrecognized compensation cost related to non-vested stock option and SSAR awards granted under the equity incentive plans relating to future periods. The cost is expected to be recognized over a weighted average period of 2.2 years.

Restricted Stock and Units

The Company may grant restricted shares and RSU's to eligible employees, giving them in most instances all of the rights of stockholders, except that they may not sell, assign, pledge or otherwise encumber such shares. Such shares and RSU's are subject to forfeiture if certain employment conditions are not met. RSU's generally vest 100% at the end of three years; however, RSU's granted to all officers and senior management have a performance restriction which if not attained terminates the RSU's prior to vesting. The fair value of the RSU's is equal to the market price of the Company's stock at date of grant and is amortized to expense ratably over the vesting period. The Company recorded compensation expense related to restricted stock and RSU's of \$4.0 million and \$5.5 million for the three and six month periods ended June 30, 2006, respectively.

Restricted stock and RSU activity was as follows:

	Shares	Weighted- Average Grant Date Fair Value Per Share
	-----	-----
Balance at January 1, 2006	909,385	\$38.84
Granted	-	
Vested	45,281	
Forfeited	98,398	

Balance at March 31, 2006	765,706	\$38.49
Granted	535,276	
Vested	-	
Forfeited	13,157	

Balance at June 30, 2006	1,287,825	\$37.12
	=====	

The total value of RSU's which vested during the first quarter was \$1.6 million. The adoption of SFAS No. 123(R) resulted in a cumulative effect gain of \$0.5 million which reflects the net cumulative impact of estimating future forfeitures in the determination of periodic expense for unvested RSU awards, rather than recording forfeitures only when they occur. The cumulative effect was recorded in operating expenses and not as a cumulative effect of a change in accounting principle because the amount was not material.

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Note 8. Segment Information:

The Company manages its operations by major geographical region. Flavors and fragrances have similar economic and operational characteristics including research and development, the nature of the creative and production processes, the type of customers, and the methods by which products are distributed. Accounting policies used for segment reporting are identical to those described in Note 1 of the Notes to the Consolidated Financial Statements included in the Company's 2005 Annual Report.

The Company evaluates the performance of its geographic regions based on segment profit which is income before taxes on income, excluding interest expense, other income and expense and the effects of restructuring and other charges and accounting changes. The Company is divided into five geographic regions for management purposes: North America, Europe, India, Latin America and Asia Pacific. The Global Expenses caption represents corporate and headquarters-related expenses including legal, finance, human resource and other administrative expenses not allocable to individual regions. Transfers between geographic regions are accounted for at prices that approximate arm's-length market prices. The Company's reportable segment information follows:

	Three Months Ended June 30					
(Dollars in thousands)	North America	Europe	India	Latin America	Asia Pacific	GL Exp
Sales to unaffiliated customers	\$164,018	\$199,173	\$ 16,288	\$ 66,283	\$ 84,743	\$
Transfers between areas	16,449	46,170	28	153	12,014	\$
Total sales	\$180,467	\$245,343	\$ 16,316	\$ 66,436	\$ 96,757	\$
Segment profit	\$ 16,995	\$ 59,935	\$ 4,117	\$ 8,976	\$ 15,761	\$ (
Restructuring and other charges	(721)	1,176	22	(3)	(170)	\$ (
Operating profit	\$ 16,274	\$ 61,111	\$ 4,139	\$ 8,973	\$ 15,591	\$ (
Interest expense						
Other income (expense), net						
Income before taxes on income						

	Three Months Ended June 30					
(Dollars in thousands)	North America	Europe	India	Latin America	Asia Pacific	GL Exp
Sales to unaffiliated customers	\$157,075	199,144	\$ 15,779	\$ 62,477	\$ 81,103	\$
Transfers between areas	19,058	51,879	3	120	11,305	\$
Total sales	\$176,133	251,023	\$ 15,782	\$ 62,597	\$ 92,408	\$
Segment profit	\$ 15,927	\$ 57,285	\$ 3,938	\$ 6,474	\$ 14,926	\$ (
Restructuring and other charges	-	-	-	-	-	\$ (
Operating profit	\$ 15,927	\$ 57,285	\$ 3,938	\$ 6,474	\$ 14,926	\$ (

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Interest expense
 Other income (expense), net
 Income before taxes on income

(Dollars in thousands)	Six Months Ended June 30, 200					
	North America	Europe	India	Latin America	Asia Pacific	GL Exp
Sales to unaffiliated customers	\$324,722	\$389,890	\$ 34,168	\$ 129,929	\$163,228	\$
Transfers between areas	31,627	91,319	298	252	23,036	
Total sales	\$356,349	\$481,209	\$ 34,466	\$ 130,181	\$186,264	\$
Segment profit	\$ 31,653	\$118,813	\$ 8,646	\$ 16,610	\$ 27,539	\$ (
Restructuring and other charges	(721)	1,170	(363)	(3)	(440)	
Operating profit	\$ 30,932	\$119,983	\$ 8,283	\$ 16,607	\$ 27,099	\$ (
Interest expense						
Other income (expense), net						
Income before taxes on income						

(Dollars in thousands)	Six Months Ended June 30, 200					
	North America	Europe	India	Latin America	Asia Pacific	GL Exp
Sales to unaffiliated customers	\$312,170	\$410,940	\$ 31,954	\$120,440	\$163,126	\$
Transfers between areas	40,361	98,762	4	438	21,238	
Total sales	\$352,531	\$509,702	\$ 31,958	\$120,878	\$184,364	\$
Segment profit	\$ 30,554	\$112,659	\$ 8,016	\$ 12,038	\$ 29,193	\$ (
Restructuring and other charges	-	-	-	-	-	
Operating profit	\$ 30,554	\$112,659	\$ 8,016	\$ 12,038	\$ 29,193	\$ (
Interest expense						
Other income (expense), net						
Income before taxes on income						

Note 9. Retirement Benefits:

As described in Note 14 of the Notes to the Consolidated Financial Statements included in the Company's 2005 Annual Report, the Company and most of its subsidiaries have pension and/or other retirement benefit plans covering substantially all employees. For the second quarter and six months ended June

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30, 2006 and 2005, pension expense for the U.S. and non - U.S. plans included the following components:

U.S. Plans	Three Months Ended June 30,	
(Dollars in thousands)	2006	2005
Service cost for benefits earned	\$ 2,636	\$ 2,390
Interest cost on projected benefit obligation	5,465	5,200
Expected return on plan assets	(5,493)	(5,243)
Net amortization and deferrals	2,015	1,191
Defined benefit plans	4,623	3,538
Defined contribution and other retirement plans	731	714
Total pension expense	\$ 5,354	\$ 4,252

Non - U.S. Plans	Three Months Ended June 30,	
(Dollars in thousands)	2006	2005
Service cost for benefits earned	\$ 3,189	\$ 2,663
Interest cost on projected benefit obligation	7,007	7,431
Expected return on plan assets	(9,459)	(8,419)
Net amortization and deferrals	2,103	2,190
Defined benefit plans	2,840	3,865
Defined contribution and other retirement plans	812	827
Total pension expense	\$ 3,652	\$ 4,692

The Company expects to contribute \$5.0 million to its qualified U.S. pension plans in the second half of 2006. No contributions were made to these plans in the first six months of 2006. In the quarter and six months ended June 30, 2006, \$1.4 million and \$2.1 million of benefit payments were made, respectively, with respect to the non-qualified plan. The Company expects to contribute \$22.1 million to its non-U.S. pension plans in 2006. In the quarter and six months ended June 30, 2006, \$1.7 million and \$5.9 million of contributions were made, respectively, to these plans.

For the quarter and six month periods ended June 30, 2006 and 2005, expense recognized for postretirement benefits other than pensions included the following components:

(Dollars in thousands)	Three Months Ended June 30,		Six Months En
(Dollars in thousands)	2006	2005	2006
Service cost for benefits earned	\$ 856	\$ 622	\$ 1,712
Interest on benefit obligation	1,575	1,226	3,150
Net amortization and deferrals	191	(107)	382

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Total postretirement benefit expense	\$ 2,622	\$ 1,741	\$ 5,244
	=====	=====	=====

The Company expects to contribute \$3.9 million to its postretirement benefit plans in 2006. In the quarter and six months ended June 30, 2006, \$1.2 million and \$2.2 million of contributions were made, respectively.

Note 10. Commitments and Contingencies:

The Company is party to a number of lawsuits and claims related primarily to flavoring supplied by the Company to manufacturers of butter flavor popcorn. At each balance sheet date, or more frequently as conditions warrant, the Company reviews the status of each pending claim, as well as its insurance coverage for such claims with due consideration given to potentially applicable deductibles,

retentions and reservation of rights under its insurance policies, and the advice of its outside legal counsel and a third party expert in modeling insurance deductible amounts with respect to all these matters. While the ultimate outcome of any litigation cannot be predicted, management believes that adequate provision has been made with respect to all known claims. There can be no assurance that future events will not require the Company to increase the amount it has accrued for any matter or accrue for a matter that has not been previously accrued. Based on information presently available and in light of the merits of its defenses and the availability of insurance, the Company does not expect the outcome of the above cases, singly or in the aggregate, to have a material adverse effect on the Company's financial condition, results of operation or liquidity.

The Company recorded its expected liability with respect to these claims in Other liabilities and expected recoveries from its insurance carrier group in Other Assets. The Company believes that realization of the insurance receivable is probable due to the terms of the insurance policies, the financial strength of the insurance carrier group and the payment experience to date of the insurance carrier group as it relates to these claims.

Note 11. Reclassifications:

Certain reclassifications have been made to the prior year's financial statements to conform to 2006 classifications.

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

Financial Condition

Overview

The Company is a leading creator and manufacturer of flavor and fragrance compounds used to impart or improve the flavor or fragrance in a wide variety of consumer products.

Fragrance compounds are used in perfumes, cosmetics, toiletries, hair care products, deodorants, soaps, detergents and softeners as well as air care products. Flavor products are sold to the food and beverage industries for use in consumer products such as prepared foods, beverages, dairy, food and confectionery products. The Company is also a leading manufacturer of synthetic ingredients used in making fragrances.

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Changing social habits resulting from such factors as increases in personal income and dual-earner households, leisure time, health concerns, urbanization and population growth stimulate demand for consumer products utilizing flavors and fragrances. These developments expand the market for products with finer fragrance quality, as well as the market for colognes and toiletries. Such developments also stimulate demand for convenience foods, soft drinks and low-fat food products that must conform to expected tastes. These developments necessitate the creation and development of flavors and fragrances and ingredients that are compatible with newly introduced materials and methods of application used in consumer products.

Flavors and fragrances are generally:

- created for the exclusive use of a specific customer;
- sold in solid or liquid form, in amounts ranging from a few kilograms to many tons depending on the nature of the end product in which they are used;
- a small percentage of the volume and cost of the end product sold to the consumer; and
- a major factor in consumer selection and acceptance of the product.

Flavors and fragrances have similar economic and operational characteristics, including research and development, the nature of the creative and production processes, the manner in which products are distributed and the type of customer; many of the Company's customers purchase both flavors and fragrances.

The flavor and fragrance industry is impacted by macroeconomic factors in all product categories and geographic regions. In addition, pricing pressure placed on the Company's customers by large and powerful retailers and distributors is inevitably passed along to the Company, and its competitors. Leadership in innovation and creativity mitigates the impact of pricing pressure. Success and growth in the industry is dependent upon creativity and innovation in meeting the many and varied needs of the customers' products in a cost-efficient and effective manner, and with a consistently high level of timely service and delivery.

The Company's strategic focus is:

- To improve customer service, in terms of both on-time deliveries and responsiveness to new product development initiatives, and to improve the win rate for new business with the Company's customers.
- To critically evaluate the profitability and growth potential of the Company's product portfolio, and to focus on those categories and customers considered to be the best opportunities for long-term profitable growth.
- To align resources of the Company with those of its major international key customers using the global reach of the Company to provide and enhance strategic partnerships.
- To focus research and development initiatives on those areas considered to be most likely, in the long-term, to yield the greatest value to the Company's customers and shareholders.

The Company has made strides to implement a number of these initiatives. On time delivery and continuous improvement in operations are supported by the global implementation of the enterprise requirements planning software package ("SAP"), and related initiatives, implementation of which are substantially completed at June 30, 2006. Product and category growth and strategic analysis of these objectives is a continual focus for management and a number of new ingredients are employed in flavor and fragrance compounds.

Operations

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Second Quarter 2006

Second quarter 2006 sales totaled \$531 million, increasing 3% over the prior year quarter; fragrance and flavor sales increased 3% and 2%, respectively. Reported sales for the 2006 period were affected by the strength of the U.S. dollar; had exchange rates remained constant, sales would have been one percentage point higher.

Fragrance sales were led by fine fragrance, which increased 9%; much of the growth resulted from new product introductions. Sales of functional fragrances increased 1% while fragrance ingredient sales declined 3%.

The flavor sales performance benefited from new wins as well as from ease of comparison with the prior year quarter, when flavor sales were affected by a vendor-supplied raw material contamination issue, the impact of which approximated \$5 million in the 2005 quarter.

Sales performance by region and product category in comparison to the prior year quarter follows:

		Second Quarter 2006 vs. 2005 % Change in Sales by Region of Destination				
		Fine	Func'l.	Ingr.	Total Frag.	Fla
North America	Reported	18%	1%	13%	10%	
Europe	Reported	3%	3%	-13%	-1%	
	Local Currency	5%	5%	-11%	1%	
Latin America	Reported	17%	-4%	-2%	1%	
Asia Pacific	Reported	2%	10%	-4%	5%	
	Local Currency	2%	10%	-1%	6%	
India	Reported	8%	-8%	18%	-1%	
	Local Currency	8%	-8%	20%	-	
Total	Reported	9%	1%	-3%	3%	
	Local Currency	10%	2%	-2%	4%	

- North America fine fragrance and flavor growth was driven mainly by new product introductions of approximately \$10 million while increases in ingredients and functional fragrances were primarily volume related.
- European growth was strongest in Eastern Europe, Africa and the Middle East, collectively increasing 15% over the 2005 quarter; a 2% decline in Western Europe offset this growth. Fine and functional fragrance growth was mainly the result of new product introductions approximating \$12 million while the decline in ingredients and flavor sales was mainly volume related.
- Latin America fine fragrance sales growth resulted from new product introductions of \$2 million while declines in functional fragrance and ingredients were primarily volume related. Flavor sales were strong throughout the region mainly as a result of new product introductions approximating \$2 million.
- Asia Pacific fine and functional fragrance sales growth resulted mainly from new product introductions of approximately \$2.5 million, while volume

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declines negatively impacted ingredient sales. Flavor sales growth was mainly the result of new product introductions in excess of \$2 million.

- India fragrance sales performance in all product categories resulted primarily from volume fluctuations while flavor sales increased due to the combined benefit of new product introductions and volume growth.

The percentage relationship of cost of goods sold and other operating expenses to sales for the second quarter 2006 and 2005 are detailed below.

	Second Quarter	
	2006	2005
Costs of Goods Sold	57.1%	58.0%
Research and Development Expenses	8.6%	8.6%
Selling and Administrative Expenses	16.5%	16.1%

- Gross profit, as a percentage of sales, improved nearly 1% compared to the prior year quarter. The improvement resulted from a combination of the local currency sales performance leading to improved manufacturing expense absorption and favorable product mix. The second quarter 2005 margin was unfavorably impacted by costs attributable to the raw material contamination matter.
- Research and Development ("R&D") expenses totaled 8.6% of sales, consistent with the prior year quarter.
- Selling, General and Administrative ("SG&A") expenses, as a percentage of sales, increased to 16.5% from 16.1%, mainly as a result of higher incentive plan accruals and an additional \$2 million in equity compensation expense recorded in the 2006 second quarter.
- Interest expense increased 4% from the prior year quarter mainly due to slightly higher average rates on borrowing compared to the prior year quarter and higher debt levels prior to the maturity of \$500 million of 5 year notes on May 15, 2006.
- The effective tax rate was 28.0% compared to 30.8% in the prior year quarter; variations in the effective rate are mainly attributable to fluctuations in earnings in the countries in which the Company operates.

Net income for the 2006 second quarter increased 8% compared with the prior year quarter, primarily as a result of the above factors.

First Six Months 2006

For the six-month period ended June 30, 2006, sales totaled \$1,042 million, essentially flat with the 2005 period. Reported sales for the 2006 period were affected by the strength of the U.S. dollar; had exchange rates remained constant, sales would have been three percentage points higher.

Fragrance sales were led by fine fragrance, which increased 6%; much of the growth resulted from new product introductions. Sales of functional fragrances declined 1% and fragrance ingredient sales declined 4%.

The flavor sales performance benefited from new wins as well as from ease of comparison with the prior year period, when flavor sales were affected by a vendor-supplied raw material contamination issue, the impact of which approximated \$5 million in the 2005 second quarter.

Sales performance by region and product category in comparison to the prior year period follows:

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Six Months 2006 vs. 2005
% Change in Sales by Region of Destination

		Fine	Func'l.	Ingr.	Total Frag.	F
North America	Reported	20%	-3%	13%	8%	
Europe	Reported	-2%	-2%	-16%	-6%	
	Local Currency	4%	4%	-12%	-1%	
Latin America	Reported	13%	1%	4%	4%	
Asia Pacific	Reported	2%	-1%	-5%	-1%	
	Local Currency	2%	-	-1%	-	
India	Reported	14%	4%	16%	8%	
	Local Currency	15%	5%	20%	10%	
Total	Reported	6%	-1%	-4%	-	
	Local Currency	9%	1%	-1%	3%	

- North America fine fragrance and flavor growth resulted mainly from new product introductions of nearly \$15 million while the decline in functional fragrances was volume related. Ingredients sales growth was due to a combination of volume and price.
- European growth was strongest in Eastern Europe, Africa and the Middle East, which was offset by an overall sales decline in Western Europe. Fine and functional fragrance growth resulted from new product introductions of approximately \$24 million while the decline in ingredients was volume related, as was the decline in flavor sales.
- Latin America fine fragrance sales growth resulted from new product introductions of approximately \$3 million while increases in functional fragrance and ingredients were primarily volume related. Flavor sales were strong throughout the region, mainly benefiting from new product introductions of approximately \$4 million.
- Asia Pacific fine fragrance sales growth resulted mainly from new product introductions totaling nearly \$3 million, while volume declines unfavorably impacted functional fragrance and ingredients. Flavor sales growth was mainly the result of new product introductions greater than \$3 million.
- India fragrance sales performance in all product categories resulted primarily from volume growth while flavor sales increased due to the combined benefit of new product introductions and volume growth.

The percentage relationship of cost of goods sold and other operating expenses to sales for the first six-month period ended June 30, 2006 and 2005 are detailed below.

	First Six Months	
	2006	2005
Costs of Goods Sold	57.4%	58.5%

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Research and Development Expenses	8.8%	8.6%
Selling and Administrative Expenses	16.6%	16.1%

- Gross profit, as a percentage of sales, improved greater than 1% compared to the prior year period. The improvement resulted mainly from the local currency sales performance, improved manufacturing expense absorption and favorable product mix. The 2005 six-month period margin was unfavorably impacted by costs attributable to the raw material contamination matter.
- R&D expenses totaled 8.8% of sales, slightly higher than the prior year period.
- SG&A expenses, as a percentage of sales, increased to 16.6% from 16.1%, mainly as a result of higher incentive plan accruals and \$3 million in additional equity compensation expense than the 2005 first six months partially offset by the Company's ongoing cost control initiatives.
- Interest expense was essentially unchanged from the prior year period.

- The effective tax rate was 28.3% compared to 31.0% in the prior year period; variations in the effective rate are mainly attributable to fluctuations in earnings in the countries in which the Company operates and realizing benefits of tax planning strategies put in place. The Company expects the effective tax rate to approximate 28.5% for 2006.

Net income for the first six months of 2006 increased 5% compared with the prior year period, primarily as a result of the improved sales performance, cost control initiatives and the above factors.

Restructuring and Other Charges

As described in Note 2 to the Consolidated Financial Statements in the Company's 2005 Annual Report, the Company has undertaken a significant reorganization, including management changes, consolidation of production facilities and related actions.

As a result of these actions, the Company recognized pre-tax charges of \$23.3 million in 2005 and \$0.4 million in the first six months of 2006. A net gain of \$0.3 million was recognized in the second quarter 2006 primarily as the result of a \$1.6 million gain recorded on the disposition of the Dijon, France land and building, the carrying value of which was reduced to its estimated net realizable value in connection with the closure of the facility in 2005; the amount realized on disposition exceeded the original estimate. The Dijon gain was offset by \$1.3 million in restructuring expense incurred in the 2006 second quarter. The remaining charges are expected to be recognized over the balance of 2006. Annual savings from these actions are expected to approximate \$16.0 million to \$18.0 million.

Movements in the liabilities related to the restructuring charges, included in Restructuring and other charges or Other liabilities as appropriate, were (in millions):

	Employee- Related	Asset- Related and Other	Total
	-----	-----	-----
Balance December 31, 2005	\$ 29.5	\$ 4.9	\$ 34.4
Additional charges	1.4	(1.0)	0.4
Cash and other costs	(14.0)	1.8	(12.2)
	-----	-----	-----
Balance June 30, 2006	\$ 16.9	\$ 5.7	\$ 22.6
	=====	=====	=====

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Consistent with the original plan, the balance of the employee-related liabilities are expected to be utilized by 2008 as obligations are satisfied; the asset-related charges will be utilized in 2007 on final decommissioning and disposal of the affected equipment.

Equity Compensation Plans

Effective January 1, 2006, the Company adopted the provisions of SFAS No. 123(R) "Share-Based Payment" ("SFAS No. 123 (R)") using the modified prospective method, which requires measurement of compensation cost of all stock-based awards at fair value on the date of grant and recognition of compensation expense over the service periods for awards expected to vest. Under this transition method, compensation cost in 2006 includes the portion vesting in the period for (1) all share-based payments granted prior to, but not vested, as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of FASB Statement No. 123, "Accounting for Stock-Based Compensation" ("SFAS No. 123"), and (2) all share-based payments granted subsequent to January 1, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS No. 123(R). The Company will recognize the cost of all employee stock options on a straight-line attribution basis over their respective vesting periods, net of estimated forfeitures. Results for prior periods have not been restated. Other equity based awards will be measured based on fair value as of the grant date, expensed over the vesting period and adjusted for forfeitures.

The Company previously applied the recognition and measurement principles of Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees," ("APB 25") and provided the pro forma disclosures required by SFAS No. 123. No compensation expense for employee stock options was previously reflected in net earnings.

The Company changed its valuation model used for estimating the fair value of options granted after January 1, 2006, from a Black-Scholes option-pricing model to a Binomial lattice-pricing model. This change was made in order to provide a

better estimate of fair value since the Binomial model is a more flexible method for valuing employee stock options than the Black-Scholes model. The flexibility of the simulated Binomial model stems from the ability to incorporate inputs that change over time, such as volatility and interest rates, and to allow for actual exercise behavior of option holders. The Company is using an average of implied and historical volatility while the expected term assumption was determined based on historical patterns.

The Company has various equity plans under which the Company's officers, senior management, directors and other key employees may be granted options to purchase the Company's common stock or other forms of equity-based awards. Prior to 2004, stock options were the primary form of equity compensation. Beginning in 2004, the Company granted Restricted Stock Units ("RSU's") as an element of its incentive compensation plan for all eligible U.S. - based employees and a majority of eligible overseas employees. Vesting of the RSU's for the Company's officers and senior management has been performance and time based, and for the remainder of eligible employees, vesting is time based; the vesting period is primarily three years from date of grant, however vesting can be adjusted within certain parameters. For a small group of primarily overseas employees, the Company continues to issue stock options.

In 2006, the Board of Directors approved a Long-Term Incentive Choice program (the "Program") for the Company's senior management under the Company's 2000 Stock Award and Incentive Plan ("2000 SAIP"). Under the Program, eligible

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employees can choose from among three alternative equity awards and will be granted such equity awards under the 2000 SAIP up to certain dollar awards depending on the participant's grade level. The participant may choose among (1) Purchase Restricted Stock ("PRS"), (2) Stock Settled Appreciation Rights ("SSAR's") or (3) RSU's. The balance of employees who are not eligible under the Program receive RSU's or, as noted above, options.

Developing the assumptions used in the binomial model requires significant judgment on the part of the Company and, generally, may involve analyzing all available historical data, considering whether historical data is relevant to predicting future behavior, making appropriate adjustments to historical data for future expectations, supplementing or replacing Company-specific historical data with data from other supportable sources and appropriately weighting each of the inputs. These assumptions are evaluated at each grant date. If factors change and the Company employs different assumptions for estimating share-based compensation expense in future periods or if the Company decides to use a different valuation model, the future periods may differ significantly from what the Company has recorded in the current period and could materially affect operating income, net income and net income per share. In addition, existing valuation models, including the Black-Scholes and binomial lattice-pricing model, may not provide reliable measures of the fair values of the Company's share-based compensation. Consequently, there is a significant risk that the Company's estimates of the fair values of share-based compensation awards on the grant dates may not reflect the actual values realized upon the vesting, exercise, expiration, early termination or forfeiture of those share-based payments in the future. There currently is no market-based mechanism or other practical application to verify the reliability and accuracy of the estimates stemming from these valuation models.

The future impact of the cost of share-based compensation on our results of operations, including net income and earnings per diluted share, will depend on, among other factors, the level of our equity awards as well as the market price of our shares at the time of award as well as various other assumptions used in valuing such awards.

See Note 7 of the Notes to the unaudited Consolidated Financial Statements for additional discussion of the impact of the adoption of, and the method of determining fair values under, SFAS No. 123(R).

Financial Condition

Cash, cash equivalents and short-term investments totaled \$30.2 million at June 30, 2006. Working capital at June 30, 2006 was \$291.1 million compared to \$(11.4) million at December 31, 2005. The change in working capital relates to the long-term refinancing of debt previously classified as current. Gross additions to property, plant and equipment during the first six months were \$19.8 million. The Company expects additions to property, plant and equipment to approximate \$60.0 to \$65.0 million for the full year 2006.

At June 30, 2006, the Company had \$724.7 million of debt outstanding. Debt, excluding deferred interest swap gains, includes \$281.5 million of commercial paper classified as long-term due to the Company's refinance intent, \$308.9 million in bank borrowings and overdrafts and \$134.2 million in long-term Japanese Yen denominated debt. On July 12, 2006, the Company issued an aggregate of \$375.0 million of Senior Unsecured Notes. The Notes were issued in four series: (i) \$50.0 million in aggregate principal amount of 5.89% Series A Senior Notes due July 12, 2009, (ii) \$100.0 million in aggregate principal amount of 5.96% Series B Notes due July 12, 2011, (iii) \$100.0 million in aggregate principal amount of 6.05% Series C Notes due July 12, 2013 and (iv) \$125.0 million in aggregate principal amount of 6.14% Series D Notes due July 12, 2016.

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Proceeds of the Notes were used to repay the commercial paper and for other general corporate purposes.

In April 2006, the Company paid a quarterly cash dividend of \$.185 per share to shareholders unchanged from the prior quarter dividend payment.

Under the share repurchase program of \$200.0 million authorized in May 2005, the Company repurchased approximately 0.4 million shares in the second quarter of 2006 at a cost of \$15.8 million. For 2006, the Company has repurchased 2.7 million shares at a cost of \$91.3 million. Repurchases will be made from time to time on the open market or through private transactions as market and business conditions warrant. Repurchased shares will be available for use in connection with the Company's employee compensation plans and for other general corporate purposes. At June 30, 2006, the Company had approximately \$86 million remaining under this repurchase plan.

The Company anticipates that its financing requirements will be funded from internal sources and credit facilities currently in place. As disclosed in the 2005 Annual Report, the Company and certain of its subsidiaries entered into a revolving credit agreement with certain banks which replaced existing credit facilities to meet short and long term financing requirements. Cash flows from operations and availability under its existing credit facilities are expected to be sufficient to fund the Company's anticipated normal capital spending, dividends and other expected requirements for at least the next twelve to eighteen months.

Non-GAAP Financial Measures

To supplement the Company's financial results presented in accordance with U.S. Generally Accepted Accounting Principles ("GAAP"), the Company uses certain non-GAAP financial measures. These non-GAAP financial measures should not be considered in isolation, or as a substitute for, or superior to, financial measures calculated in accordance with GAAP. These non-GAAP financial measures as disclosed by the Company may also be calculated differently from similar measures disclosed by other companies. To ease the use and understanding of our supplemental non-GAAP financial measures, the Company includes the most directly comparable GAAP financial measure.

The Company discloses, and management internally monitors, the sales performance of international operations on a basis that eliminates the positive or negative effects that result from translating foreign currency sales into U.S. dollars. Management uses this measure because it believes that it enhances the assessment of the sales performance of its international operations and the comparability between reporting periods.

Cautionary Statement Under The Private Securities Litigation Reform Act of 1995

Statements in this Quarterly Report, which are not historical facts or information, are "forward-looking statements" within the meaning of The Private Securities Litigation Reform Act of 1995. Such forward-looking statements are based on management's reasonable current assumptions and expectations. Such forward-looking statements which may be identified by such words as "expect," "believe," "anticipate," "outlook," "guidance," "may," and similar forward-looking terminology, involve significant risks, uncertainties and other factors, which may cause the actual results of the Company to be materially different from any future results expressed or implied by such forward-looking statements, and there can be no assurance that actual results will not differ materially from management's expectations. Such factors include, among others, the following: general economic and business conditions in the Company's

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markets, including economic, population health and political uncertainties; weather, geopolitical, civil hostilities and region specific uncertainties; interest rates; the price, quality and availability of raw materials; the Company's ability to implement its business strategy, including the achievement of anticipated cost savings, profitability, growth and market share targets; the impact of currency fluctuation or devaluation in the Company's principal foreign markets and the success of the Company's hedging and risk management strategies; the impact of possible pension funding obligations and increased pension expense on the Company's cash flow and results of operations; and the effect of legal and regulatory proceedings, as well as restrictions imposed on the Company, its operations or its representatives by foreign governments; and the fact that the outcome of litigation is highly uncertain and unpredictable and there can be no assurance that the triers of fact or law, at either the trial level or at any appellate level, will accept the factual assertions, factual defenses or legal positions of the Company or its factual or expert witnesses in any such litigation or other proceedings. The Company intends its forward-looking statements to speak only as of the time of such statements and does not plan to update or revise them as more information becomes available or to reflect changes in expectations, assumptions or results.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

There are no material changes in market risk from the information provided in the Company's 2005 Annual Report on Form 10-K.

Item 4. Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer, with the assistance of other members of the Company's management, have evaluated the effectiveness of the Company's disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on such evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures are effective as of the end of the reporting period covered by this report.

The Company's Chief Executive Officer and Chief Financial Officer have also concluded that there have not been any changes in the Company's internal control over financial reporting during the quarter ended June 30, 2006 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is subject to various claims and legal actions in the ordinary course of its business.

In September 2001, the Company was named as a defendant in a purported class action brought against it in the Circuit Court of Jasper County, Missouri, on behalf of employees of a plant owned and operated by Gilster-Mary Lee Corp. in Jasper, Missouri ("Benavides case"). The plaintiffs alleged that they sustained respiratory injuries in the workplace due to the use by Gilster-Mary Lee of a BBA and/or IFF flavor. For purposes of reporting these actions, BBA and/or IFF are referred to as the "Company".

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In January 2004, the Court ruled that class action status was not warranted. As a result of this decision, each of the 47 plaintiff cases was to be tried separately. Subsequently, 8 cases were tried to a verdict, 4 verdicts resulted for the plaintiffs and 4 verdicts resulted for the Company, all of which were appealed by the losing party. Subsequently all plaintiff cases related to the Benavides case have been settled or are in the process of settlement.

Thirteen other actions based on similar claims of alleged respiratory illness due to workplace exposure to flavor ingredients are currently pending against the Company and other flavor suppliers and related companies.

Trial has been scheduled in the action brought against the Company and another flavor supplier by 23 former and current workers at a Marion, Ohio factory. This case was filed in March 2003 and is pending in the Court of Common Pleas of Hamilton County, Ohio. The Plaintiffs in this case have been divided into 7 trial groups. The first trial group consists of 2 workers and 1 spouse, and their case will be tried on August 29, 2006. No other trial dates have been set (Arthur case). In May 2004, the Company and another flavor supplier were named defendants in a lawsuit by 4 former workers at a Ridgeway, Illinois factory in an action brought in the Circuit Court for the Second Judicial Circuit, Gallatin County, Illinois (Barker case) and another concerning 8 other workers at this same plant was filed in July 2004 and is pending in this same Court against the Company and another flavor supplier (Batteese case). In an action filed in June 2004, the Company, three other flavor suppliers, a flavor trade association and a consulting agency are defendants in a lawsuit by 1 worker at a Sioux City, Iowa facility which is pending in U.S. District Court for the Northern District of Iowa. Plaintiff voluntarily dismissed his claim against Bush Boake Allen, Inc. Trial is set for December 4, 2006 (Remmes case). Another case concerning 1 other worker at this same plant was filed in January 2006 and is pending in this same court against the same parties. The trial ready date is November 5, 2007 (Kuiper case). In June 2004, the Company and 3 other flavor suppliers were named defendants in a lawsuit by 1 plaintiff brought in the Court of Common Pleas, Hamilton County, Ohio. Trial is set for January 16, 2007 (Mitchell case). In June 2004, the Company and 2 other flavor suppliers were named defendants in a lawsuit by 1 former worker at a Northlake, Illinois facility in an action brought in the Circuit Court of Cook County, Illinois (Lopez case). In August 2004, the Company and another flavor supplier were named defendants in a lawsuit by 15 former workers at a Marion, Ohio factory in an action brought in the Court of Common Pleas, Marion County, Ohio. The Plaintiffs will be divided into 9 trial groups, the trials will be held consecutively from May through October, 2007 (Williams case). In March 2005, the Company and 10 other companies were named defendants in a lawsuit by 1 former employee of Bell Flavors and Fragrances, Inc. in an action brought in the Circuit Court of Cook County, Illinois. On June 29, 2006, Plaintiffs voluntarily dismissed their claims against one of the defendants, EMCO Chemical Distributors. There is no trial date pending (Robinson case). In July 2005, the Company and 9 other flavor and chemical suppliers were named defendants in a lawsuit by 1 former worker of Brach's Confections, Inc. in an action brought in the Circuit Court of Cook County, Illinois. There is no trial date pending (Campbell case). In August 2005, the Company and 8 other companies, including a flavor trade association and consulting agency, were named defendants in a lawsuit by 3 former employees of the Gilster-Mary Lee facility in McBride, Missouri in the Missouri Circuit Court, 22nd Judicial Circuit. Trial is set for May 7, 2007 (Fults case). In September 2005, the Company and 9 other companies were named defendants in a lawsuit by 2 former employees of the Gilster-Mary Lee facility in McBride, Missouri in the Circuit Court of St. Louis County. Trial is set for September 24, 2007 (Bowling case). In November 2005, the Company, a flavor trade association, and a consulting agency were named defendants in a lawsuit by 1 former employee of the Snappy Popcorn Company in Breda, Iowa brought in U.S. District Court for the Northern District of Iowa, Western Division. The trial

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ready date is June 30, 2007 (Weimer case). All these cases remain in the pretrial stage.

The Company believes that all IFF and BBA flavors at issue in these matters meet the requirements of the U.S. Food and Drug Administration and are safe for handling and use by workers in food manufacturing plants when used according to specified safety procedures. These procedures are detailed in instructions that

IFF and BBA provided to all their customers for the safe handling and use of their flavors. It is the responsibility of IFF's customers to ensure that these instructions, which include the use of appropriate engineering controls, such as adequate ventilation, prior handling procedures and respiratory protection for workers, are followed in the workplace.

At each balance sheet date, or more frequently as conditions warrant, the Company reviews the status of each pending claim, as well as its insurance coverage for such claims with due consideration given to potentially applicable deductibles, retentions and reservation of rights under its insurance policies, and the advice of its outside legal counsel and a third party expert in modeling insurance deductible amounts with respect to all these matters. While the ultimate outcome of any litigation cannot be predicted, management believes that adequate provision has been made with respect to all known claims. Based on information presently available and in light of the merits of its defenses and the availability of insurance, the Company does not expect the outcome of the above cases, singly or in the aggregate, to have a material adverse effect on the Company's financial condition, results of operation or liquidity. There can be no assurance that future events will not require the Company to increase the amount it has accrued for any matter or accrue for a matter that has not been previously accrued. See Note 10 of the Notes to the Consolidated Financial Statements.

Over the past 20 years, various federal and state authorities and private parties have claimed that the Company is a potentially responsible party as a generator of waste materials for alleged pollution at a number of waste sites operated by third parties located principally in New Jersey and seek to recover costs incurred and to be incurred to clean up the sites.

The waste site claims and suits usually involve million dollar amounts, and most of them are asserted against many potentially responsible parties. Remedial activities typically consist of several phases carried out over a period of years. Most site remedies begin with investigation and feasibility studies, followed by physical removal, destruction, treatment or containment of contaminated soil and debris, and sometimes by groundwater monitoring and treatment. To date, the Company's financial responsibility for some sites has been settled through agreements granting the Company, in exchange for one or more cash payments made or to be made, either complete release of liability or, for certain sites, release from further liability for early and/or later remediation phases, subject to certain "re-opener" clauses for later-discovered conditions. Settlements in respect of some sites involve, in part, payment by the Company and other parties of a percentage of the site's future remediation costs over a period of years.

The Company believes that the amounts it has paid and anticipates paying in the future for clean-up costs and damages at all sites are not and will not be material to the Company's financial condition, results of operations or liquidity, because of the involvement of other large potentially responsible parties at most sites, because payment will be made over an extended time period and because, pursuant to an agreement reached in July 1994 with three of the Company's liability insurers, defense costs and indemnity amounts payable by the Company in respect of the sites will be shared by the insurers up to an agreed amount.

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Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

(c) Issuer Purchases of Equity Securities

	Total Number of Shares Purchased(1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Program(2)
April 1 - 30, 2006	-	-	-
May 1 - 31, 2006	320,000	\$35.61	320,000
June 1 - 30, 2006	122,800	\$35.48	122,800

(1) An aggregate of 442,800 shares of common stock were repurchased during the second quarter of 2006 under a repurchase program announced in May 2005. Under the program, the Board of Directors approved the repurchase by the Company of up to \$200.0 million of its common stock.

Item 4. Submission of Matters to a Vote of Security Holders

The following matters were submitted to a vote of security holders during the Company's annual meeting of shareholders held on May 9, 2006:

	Votes Cast For	Authority Withheld	
1.) Election of Directors			
Margaret Hayes Adame	74,509,355	1,956,610	
Gunter Blobel	75,848,325	617,640	
J. Michael Cook	75,473,676	992,289	
Peter A. Georgescu	75,499,673	966,292	
Alexandra A. Herzan	75,852,019	613,946	
Henry W. Howell, Jr.	75,384,120	1,081,845	
Arthur C. Martinez	74,175,119	2,290,846	
Burton M. Tansky	75,417,093	1,048,872	
2.)	For	Against	Abstentions
Ratification of PricewaterhouseCoopers LLP as	74,977,260	1,068,406	420,299

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independent registered public
accounting firm

Item 6. Exhibits

- 3(ii) By-Laws of the Company, as amended effective as of July 1, 2006 (incorporated by reference to Exhibit 99.1 to the Company's Form 8-K filed with the SEC on June 30, 2006).
- 10.1 Retirement Agreement dated as of April 3, 2006 between Richard A. Goldstein, former Chairman of the Board of Directors and Chief Executive Officer, and the Company (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on April 3, 2006).
- 10.2 Letter Agreement dated June 28, 2006 between the Company and Robert M. Amen, Chairman of the Board of Directors and Chief Executive Officer (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on June 29, 2006).
- 10.3 Restricted Stock Units Agreement dated July 25, 2006 between the Company and Arthur C. Martinez (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the SEC on July 26, 2006).
- 4.1 Note Purchase Agreement, dated as of July 12, 2006, by and among the Company and the various purchasers named therein (incorporated by reference to Exhibit 4.7 to the Company's Form 8-K filed with the SEC on July 13, 2006).
- 4.2 Form of Series A, Series B, Series C and Series D Senior Notes (incorporated by reference to Exhibit 4.8 to the Company's Form 8-K filed with the SEC on July 13, 2006).
- 31.1 Certification of Robert M. Amen pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 31.2 Certification of Douglas J. Wetmore pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
- 32 Certification of Robert M. Amen and Douglas J. Wetmore pursuant to 18 U.S.C. Section 1350 as adopted pursuant to the Sarbanes-Oxley Act of 2002.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

INTERNATIONAL FLAVORS & FRAGRANCES INC.

Dated: August 7, 2006

By: /s/ DOUGLAS J. WETMORE

Douglas J. Wetmore, Senior Vice President
and Chief Financial Officer

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Dated: August 7, 2006

By: /s/ DENNIS M. MEANY

Dennis M. Meany, Senior Vice President,
General Counsel and Secretary

EXHIBIT INDEX

Number -----	Description -----
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Exhibit 31.1

CERTIFICATION

I, Robert M. Amen, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of International Flavors & Fragrances Inc.;

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2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasm" style="padding:0in .7pt 0in 0in;width:9.58%;">

Net Interest Income

16,167

15,841

8,198

7,997

Provision for Credit Losses

339

707

36

592

Net Interest Income After Provision For Credit Losses

15,828

15,134

8,162

7,405

Noninterest Income

Service charges on deposits

713

667

364

343

Gain on sale of loans

571

242

334

66

Gain on sale of investment securities

7

156

156

Other income

903

620

498

280

Total noninterest income

2,194

1,685

1,196

845

Noninterest Expense

Salaries and employee benefits

6,806

5,949

3,454

2,975

Premises and equipment expenses

2,463

1,688

1,255

819

Advertising

222

264

131

145

Outside data processing

445

436

183

208

Other expenses

2,344

2,048

1,208

1,015

Total noninterest expense

12,280

10,385

6,231

5,162

Income Before Income Tax Expense

5,742

6,434

3,127

3,088

Income Tax Expense

2,082

2,461

1,149

1,098

Net Income

\$

3,660

\$

3,973

\$

1,978

\$

1,990

Earnings Per Share (1)

Basic

\$

0.38

\$

0.42

\$

0.21

\$

0.21

Diluted

\$

0.37

\$

0.40

\$

0.20

\$

0.20

Dividends Declared Per Share (1)

\$

0.12

\$

0.11

\$

0.06

\$

0.05

See notes to consolidated financial statements.

(1) Earnings per share for June 30, 2006 have been adjusted to reflect the 1.3 for 1 stock split in the form of a 30% stock dividend paid on July 5, 2006.

3

EAGLE BANCORP, INC.

Consolidated Statements of Cash Flows

For the Six Month Periods Ended June 30, 2007 and 2006 (unaudited)
(dollars in thousands)

	2007	2006
Cash Flows From Operating Activities:		
Net income	\$ 3,660	\$ 3,973
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Provision for credit losses	339	707
Depreciation and amortization	672	394
Gains on sale of loans	(571)	(242)
Origination of loans held for sale	(29,072)	(23,868)
Proceeds from sale of loans held for sale	28,946	22,508
Increase in cash surrender value of BOLI	(220)	(197)
Gain on sale of investment securities	(7)	(156)
Stock based compensation expense	130	204
Excess tax benefit from exercise of non-qualified stock options	(11)	(191)
Decrease (Increase) in other assets	262	(2,494)
Decrease in other liabilities	(19)	(519)
Net cash provided by operating activities	4,109	119
Cash Flows From Investing Activities:		
Decrease (Increase) in interest bearing deposits with other banks and short term investments	472	(1,576)
Purchases of available for sale investment securities	(591)	(19,975)
Proceeds from maturities of available for sale securities	2,841	9,115
Proceeds from sale/call of available for sale securities	15,799	510
Net increase in loans	(33,884)	(24,195)
Bank premises and equipment acquired	(876)	(1,283)
Net cash used in investing activities	(16,239)	(37,404)
Cash Flows From Financing Activities:		
Increase in deposits	21,977	54,840
Increase in customer repurchase agreements and federal funds purchased	2,525	2,321
Increase in other short-term borrowings	12,000	25,000
Issuance of common stock	829	570
Excess tax benefit from exercise of non-qualified stock options	11	191
Payment of dividends and payment in lieu of fractional shares	(1,144)	(1,013)
Net cash provided by financing activities	36,198	81,909
Net Increase In Cash	24,068	44,624
Cash And Due From Banks At Beginning of Period	28,977	22,765
Cash And Due From Banks At End of Period	\$ 53,045	\$ 67,389
Supplemental Cash Flows Information:		
Interest paid	\$ 11,640	\$ 6,974
Income taxes paid	\$ 2,712	\$ 2,000
Non-cash Investing Activities		
Transfers from loans to other real estate owned	\$	\$ 257

See notes to consolidated financial statements.

EAGLE BANCORP, INC.

Consolidated Statements of Changes in Stockholders' Equity
For the Six Month Periods Ended June 30, 2007 and 2006 (unaudited)
(dollars in thousands)

	Common Stock	Additional Paid in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Stockholders Equity
Balance, January 1, 2007	\$ 95	\$ 50,278	\$ 22,796	\$ (253)	\$ 72,916
Comprehensive Income					
Net Income			3,660		3,660
Other comprehensive income:					
Unrealized gain on securities available for sale (net of taxes)				(389)	(389)
Less: reclassification adjustment for gains net of taxes of \$3 included in net income				(4)	(4)
Total Comprehensive Income				(393)	3,267
Cash Dividend (\$.12 per share)			(1,144)		(1,144)
Stock based compensation		130			130
Exercise of options for 71,804 shares of common stock	1	616			617
Shares issued under dividend reinvestment plan - 13,295 shares		212			212
Tax benefit adjustment on non-qualified options exercise		11			11
Balance, June 30, 2007	\$ 96	\$ 51,247	\$ 25,312	\$ (646)	\$ 76,009
Balance, January 1, 2006	\$ 72	\$ 48,594	\$ 16,918	\$ (620)	\$ 64,964
Comprehensive Income					
Net Income			3,973		3,973
Other comprehensive income:					
Unrealized loss on securities available for sale (net of taxes)				(318)	(318)
Less: reclassification adjustment for gains net of taxes of \$62 included in net income				(94)	(94)
Total Comprehensive Income				(412)	3,561
Cash Dividend (\$.11 per share)			(1,013)		(1,013)
Stock based compensation		204			204
Exercise of options for 63,703 shares of common stock		570			570
Tax benefit on non-qualified options exercise		191			191
Balance, June 30, 2006	\$ 72	\$ 49,559	\$ 19,878	\$ (1,032)	\$ 68,477

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

For the Three and Six Months Ended June 30, 2007 and 2006 (unaudited)

1. BASIS OF PRESENTATION

The consolidated financial statements of Eagle Bancorp, Inc. (the Company) included herein are unaudited; however, they reflect all adjustments, consisting only of normal recurring accruals, that in the opinion of Management, are necessary to present fairly the results for the periods presented. The amounts as of and for the year ended December 31, 2006 were derived from audited consolidated financial statements. Certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission. There have been no significant changes to the Company's Accounting Policies as disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2006. The Company believes that the disclosures are adequate to make the information presented not misleading. The results of operations for the three and six months ended June 30, 2007 are not necessarily indicative of the results of operations to be expected for the remainder of the year, or for any other period. Certain reclassifications have been made to amounts previously reported to conform to the classification made in 2007.

2. NATURE OF OPERATIONS

The Company, through EagleBank, its bank subsidiary (the Bank), conducts a full service community banking business, primarily in Montgomery County, Maryland and Washington, D.C. The primary financial services include real estate, commercial and consumer lending, as well as traditional deposit and repurchase agreement products. The Bank is also active in the origination and sale of residential mortgage loans and the origination of small business loans. The guaranteed portion of small business loans is typically sold through the Small Business Administration, in a transaction apart from the loan's origination. The Bank offers its products and services through nine banking offices and various electronic capabilities. In July 2006, the Company formed Eagle Commercial Ventures, LLC as a direct subsidiary to provide subordinate financing for the acquisition, development and construction of real estate projects, whose primary financing would be done by the Bank. Prior to the formation of ECV, the Company directly engaged in occasional subordinate financing transactions, which involve higher levels of risk with commensurate returns.

3. CASH FLOWS

For purposes of reporting cash flows, cash and cash equivalents include cash and due from banks, and federal funds sold (items with an original maturity of three months or less).

4. INVESTMENT SECURITIES

Amortized cost and estimated fair value of securities available for sale are summarized as follows:

(in thousands)

June 30, 2007	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U. S. Government agency securities	\$ 42,697	\$	\$ 528	\$ 42,169
Mortgage backed securities	25,122		642	24,480
Federal Reserve and Federal Home Loan Bank stock	4,420			4,420
Other equity investments	1,278	102		1,380
	\$ 73,517	\$ 102	\$ 1,170	\$ 72,449

December 31, 2006	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
U. S. Government agency securities	\$ 58,803	\$ 161	\$ 380	\$ 58,584
Mortgage backed securities	27,650	69	386	27,333
Federal Reserve and Federal Home Loan Bank stock	3,829			3,829
Other equity investments	1,278	116		1,394
	\$ 91,560	\$ 346	\$ 766	\$ 91,140

Gross unrealized losses and fair value by length of time that the individual available securities have been in a continuous unrealized loss position as of June 30, 2007 are as follows:

June 30, 2007	Estimated Fair Value	Less than 12 months	More than 12 months	Gross Unrealized Losses
U. S. Government agency securities	\$ 40,164	\$ 175	\$ 353	\$ 528
Mortgage backed securities	24,479	239	403	642
	\$ 64,643	\$ 414	\$ 756	\$ 1,170

December 31, 2006	Estimated Fair Value	Less than 12 months	More than 12 months	Gross Unrealized Losses
U. S. Government agency securities	\$ 32,919	\$ 45	\$ 335	\$ 380
Mortgage backed securities	17,788	27	359	386
	\$ 50,707	\$ 72	\$ 694	\$ 766

The unrealized losses that exist are the result of changes in market interest rates since original purchases. All of the bonds are rated AAA. The weighted average life of debt securities, which comprise 92% of total investment securities, is relatively short at 2.6 years. These factors, coupled with the Company's ability and intent to hold these investments for a period of time sufficient to allow for any anticipated recovery in fair value substantiates that the unrealized losses are temporary in nature.

5. INCOME TAXES

The Company employs the liability method of accounting for income taxes as required by Statement of Financial Accounting Standards No. 109 (SFAS), Accounting for Income Taxes. Under the liability method, deferred-tax assets and liabilities are determined based on differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities (i.e., temporary differences) and are measured at the enacted rates that will be in effect when these differences reverse.

6. EARNINGS PER SHARE

Earnings per common share are computed by dividing net income by the weighted average number of common shares outstanding during the period. Diluted net income per common share is computed by dividing net income by the weighted average number of common shares outstanding during the period, including any potential dilutive common shares outstanding, such as stock options. As of June 30, 2007 there were 198,961 shares excluded from the diluted net income per share computation because their inclusion would be anti-dilutive.

Earnings per share for the three and six months ended June 30, 2006 have been adjusted for a 30% stock dividend paid in the form of a 1.3 to 1 stock split on July 5, 2006.

7. SHARE-BASED COMPENSATION

The Company maintains the 1998 Stock Option Plan (1998 Plan) and the 2006 Stock Plan (2006 Plan). No additional options may be granted under the 1998 Plan. The 1998 Plan provided for the periodic granting of incentive and non-qualifying options to selected key employees and members of the Board. Option awards were made with an exercise price equal to the market price of the Company's shares at the date of grant. The option grants generally vested over a period of one to two years under the 1998 Plan.

The Company adopted the 2006 Plan upon approval by shareholders at the 2006 Annual Meeting held on May 25, 2006. The Plan provides for the issuance of awards of incentive options, nonqualifying options, restricted stock and stock appreciation rights with respect to up to 650,000 shares (as adjusted for the 1.3 to 1 stock split paid on July 5, 2006). The purpose of the 2006 Plan is to advance the interests of the Company by providing directors and selected employees of the Bank, the Company, and their affiliates with the opportunity to acquire shares of common stock, through awards of options, restricted stock and stock appreciation rights.

The Company also maintains the 2004 Employee Stock Purchase Plan (the ESPP). Under the ESPP, a total of 253,500 shares (as adjusted for the 1.3 to 1 stock split paid on July 5, 2006) of common stock, were reserved for issuance to eligible employees at a price equal to at least 85% of the fair market value of the shares of common stock on the date of grant. Grants each year expire no later than the last business day of January in the calendar year following the year in which the grant is made. No grants have been made under this plan in 2007.

The Company believes that awards under all plans better align the interests of its employees with those of its shareholders.

In January 2007, the Company awarded options to purchase 68,550 shares under the 2006 Plan which have a five-year term and vest over a three year period.

In January 2007, the Company awarded 20,390 stock appreciation rights to five senior officers under the 2006 Plan to be settled in the Company's common stock following a three-year service vesting period. The Company also granted performance based restricted stock, which vests at the end of a three-year period, subject to the achievement of specified goals. Restricted share awards are being recognized as compensation expense over a three-year performance period based on the market value of the shares at the date of grant. This compensation expense will be evaluated quarterly as to share awards based on an assumption of achievement of target goals.

The fair value of each option grant and other equity based award is estimated on the date of grant using the Black-Scholes option pricing model with the assumptions as shown in the table below used for grants during the six months ended June 30, 2007 and the twelve months ended December 31, 2006 and 2005.

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Below is a summary of changes in shares under option (split adjusted) for the six months ended June 30, 2007. The information excludes restricted stock awards.

	Stock Options	Wgt. Avg. Exercise Price	Wgt. Avg. Remaining Contractual Life	Wgt. Avg. Grant Date Fair Value	Aggregate Intrinsic Value
As of 1/1/2007					
Outstanding	899,797	\$ 8.67		\$ 5.25	
Vested	848,365	8.16		5.23	
Nonvested	51,432	17.17		5.58	
Period activity					
Issued	88,940	\$ 17.00		\$ 3.21	
Exercised	71,804	8.59		3.31	
Forfeited	14,630	7.66		2.44	
Expired	30,192	15.05		3.03	
As of 6/30/2007					
Outstanding	872,111	\$ 9.33	4.28	\$ 5.32	\$ 6,508,962
Vested	743,939	7.90	4.14	5.54	6,508,962
Nonvested	128,172	17.58	5.08	4.05	

Outstanding:

Range of Exercise Prices	Stock Options Outstanding	Wgt. Avg. Exercise Price	Wgt. Avg. Remaining Contractual Life
\$3.25 - \$8.75	428,472	\$ 4.31	2.62
\$8.76 - \$13.26	244,380	11.30	6.97
\$13.27 - \$17.77	90,038	16.99	4.12
\$17.78 - \$19.46	109,221	18.28	4.89
	872,111	9.33	4.28

Exercisable:

Range of Exercise Prices	Stock Options Exercisable	Wgt. Avg. Exercise Price
\$3.25 - \$8.75	428,472	\$ 4.31
\$8.76 - \$13.26	244,380	11.30
\$13.27 - \$17.77	1,273	16.38
\$17.78 - \$19.46	69,814	17.92
	743,939	7.90

Assumptions:

	Six Months Ended June 30, 2007	Year Ended 2006	Year Ended 2005
Expected Volatility	18.5% - 20.2	% 21.4% - 24.1	% 22.9% - 23.5
Weighted-Average Volatility	19.85	% 22.62	% 22.94
Expected Dividends	1.4	% 1.3	% 1.6
Expected Term (In years)	3.1 - 3.5	0.5 - 3.4	1.0 - 10.0
Risk-Free Rate	4.78	% 4.60	% 4.27
Weighted Average Fair Value (Grant date)	\$ 3.21	\$ 4.40	\$ 3.80

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Total intrinsic value of options exercised:	\$	573,928
Total fair value of shares vested:	\$	54,386
Weighted-average period over which nonvested awards are expected to be recognized:	1.97	years

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As of December 31, 2006, there was \$446 thousand of total unrecognized compensation cost related to non-vested equity awards under the Company's various share based compensation plans. The \$446 thousand cost is being amortized over the remaining service (vesting) period. Through June 30, 2007, \$68 thousand has been recognized in compensation cost related to those grants. In total, the Company recognized \$82 thousand (\$0.01 per share) and \$130 thousand (\$0.01 per share) in share based compensation expense for the three and six months ended June 30, 2007 as compared to \$34 thousand (\$0.00 per share) and \$204 thousand (\$0.02 per share) for the same period in 2006.

8. NEW ACCOUNTING PRONOUNCEMENTS

In March 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 156, *Accounting for Servicing of Financial Assets*. This Statement amends SFAS No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities*, and requires that all separately recognized servicing assets and servicing liabilities be initially measured at fair value, if practicable, and permits the entities to elect either fair value measurement with changes in fair value reflected in earnings or the amortization and impairment requirements of SFAS No. 140 for subsequent measurement. The subsequent measurement of separately recognized servicing assets and servicing liabilities at fair value eliminates the necessity for entities that manage the risks inherent in servicing assets and servicing liabilities with derivatives to qualify for hedge accounting treatment and eliminates the characterization of declines in fair value as impairments or direct write-downs. This Statement is effective as of the beginning of an entity's first fiscal year that begins after September 15, 2006. The Company's servicing asset was for the computed value of servicing fees on the sale of the guaranteed portion of SBA loans. Assumptions related to loan term and amortization are made to arrive at the initial recorded value. This asset is subject to impairment testing annually. The Company does not elect to measure this asset at fair value and believes this new accounting standard will have no impact on its financial condition or results of operations.

In June 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 clarifies when tax benefits should be recorded in financial statements, requires certain disclosures of uncertain tax matters and indicates how any tax reserves should be classified in a balance sheet. FIN 48 is effective for the Company in the first quarter of fiscal 2007. The Company is evaluating the impact if any of FIN 48 on results of operations and financial condition. The Company does not have any uncertain tax positions and believes this new accounting standard adopted during the first quarter of 2007 will have no impact on its financial condition or results of operation.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS 157). This statement provides a single definition of fair value, a framework for measuring fair value, and expanded disclosures concerning fair value. Previously, different definitions of fair value were contained in various accounting pronouncements creating inconsistencies in measurement and disclosures. SFAS 157 applies under those previously issued pronouncements that prescribe fair value as the relevant measure of value, except SFAS 123R and related interpretations and pronouncements that require or permit measurement similar to fair value but are not intended to measure fair value. This pronouncement is effective for fiscal years beginning after November 15, 2007. The Company is evaluating the impact of this new standard, but currently believes that adoption will not have a material impact on its financial position, results of operations, or cash flows.

In September 2006, the SEC's Office of the Chief Accountant and Divisions of Corporation Finance and Investment Management released SAB No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB No. 108), that provides interpretive guidance on how the effects of the carryover or reversal of prior year misstatements should be considered in quantifying a current year misstatement. The SEC staff believes that registrants should quantify errors using both a balance sheet and an income statement approach and evaluate whether either approach results in quantifying a misstatement that, when all relevant quantitative and qualitative factors are considered, is material. This pronouncement is effective for fiscal years ending after November 15, 2006. The adoption of SAB No. 108 had no material impact on the Company's financial position, results of operations, or cash flows.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 allows entities the option to measure eligible financial instruments at fair value as of specified dates. Such election, which may be applied on an instrument by instrument basis, is

typically irrevocable once elected. Statement 159 is effective for fiscal years beginning after November 15, 2007, and early application is allowed under certain circumstances. The Company is evaluating the impact of this new standard, but currently believes that adoption will not have a material impact on its financial position, results of operations, or cash flows.

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

The following discussion provides information about the results of operations, and financial condition, liquidity, and capital resources of the Company and its subsidiaries as of the dates and periods indicated. This discussion and analysis should be read in conjunction with the unaudited Consolidated Financial Statements and Notes thereto, appearing elsewhere in this report and the Management Discussion and Analysis in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

This report contains forward looking statements within the meaning of the Securities Exchange Act of 1934, as amended, including statements of goals, intentions, and expectations as to future trends, plans, events or results of Company operations and policies and regarding general economic conditions. In some cases, forward looking statements can be identified by use of such words as may, will, anticipate, believes, expects, plans, estimates, potential, continue, should, and similar words or phrases. These statements are based upon current and anticipated economic conditions, nationally and in the Company's market, interest rates and interest rate policy, competitive factors and other conditions which, by their nature, are not susceptible to accurate forecast, and are subject to significant uncertainty. Because of these uncertainties and the assumptions on which this discussion and the forward looking statements are based, actual future operations and results in the future may differ materially from those indicated herein. Readers are cautioned against placing undue reliance on any such forward looking statements.

GENERAL

Eagle Bancorp, Inc. is a growth oriented, one-bank holding company headquartered in Bethesda, Maryland. We provide general commercial and consumer banking services through our wholly owned banking subsidiary EagleBank (the Bank), a Maryland chartered bank which is a member of the Federal Reserve System. We were organized in October 1997, to be the holding company for the Bank. The Bank was organized as an independent, community oriented, full service banking alternative to the super regional financial institutions, which dominate our primary market area. Our philosophy is to provide superior, personalized service to our customers. We focus on relationship banking, providing each customer with a number of services, becoming familiar with and addressing customer needs in a proactive, personalized fashion. The Bank currently has six offices serving Montgomery County and three offices in the District of Columbia.

The Company offers a broad range of commercial banking services to our business and professional clients as well as full service consumer banking services to individuals living and/or working primarily in our service area. We emphasize providing commercial banking services to sole proprietors, small and medium-sized businesses, partnerships, corporations, non-profit organizations and associations, and investors living and working in and near our primary service area. A full range of retail banking services are offered to accommodate the individual needs of both corporate customers as well as the community we serve. These services include the usual deposit functions of commercial banks, including business and personal checking accounts, NOW accounts and money market and savings accounts, business, construction, and commercial loans, equipment leasing, residential mortgages and consumer loans and cash management services. We have developed significant expertise and commitment as an SBA lender, have been designated a Preferred Lender by the Small Business Administration (SBA), and are a leading community bank SBA lender in the Washington D.C. district.

CRITICAL ACCOUNTING POLICIES

The Company's consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) and follow general practices within the banking industry. Application of these principles requires management to make estimates, assumptions, and judgments that affect the amounts reported in the financial statements and accompanying notes. These estimates, assumptions and judgments are based on information available as of the date of the consolidated financial statements; accordingly, as this information changes, the consolidated financial statements could reflect different estimates, assumptions, and judgments. Certain policies inherently have a greater reliance on the use of estimates, assumptions and judgments and as such have a greater possibility of producing results that could be materially different than originally reported. Estimates, assumptions, and judgments are necessary when assets and liabilities are required to be recorded at fair value, when a decline in the value of an asset not carried on the financial statements at fair value warrants an impairment write-down or valuation reserve to be established, or when an asset or liability needs to be recorded contingent upon a future event. Carrying assets and liabilities at fair value inherently results in more financial statement volatility. The fair values and the information used to record valuation adjustments for certain assets and liabilities are based either on quoted market prices or are provided by other third-party sources, when available.

The allowance for credit losses is an estimate of the losses that may be sustained in our loan portfolio. The allowance is based on two principles of accounting: (a) Statement on Financial Accounting Standards (SFAS) 5, Accounting for Contingencies , which requires that losses be accrued when they are probable of occurring and are estimable and (b) SFAS No. 114, Accounting by Creditors for Impairment of a Loan , which requires that losses be accrued when it is probable that the Company will not collect all principal and interest payments according to the contractual terms of the loan. The loss, if any, can be determined by the difference between the loan balance and the value of collateral, the present value of expected future cash flows, or values observable in the secondary markets.

Three components comprise our allowance for credit losses: a specific allowance, a formula allowance and a nonspecific or environmental factors allowance. Each component is determined based on estimates that can and do change when actual events occur.

The specific allowance allocates an allowance to identified loans. A loan for which reserves are individually allocated may show deficiencies in the borrower's overall financial condition, payment record, support available from financial guarantors and or the fair market value of collateral. When a loan is identified as impaired, a specific reserve is established based on the Company's assessment of the loss that may be associated with the individual loan.

The formula allowance is used to estimate the loss on internally risk rated loans, exclusive of those identified as requiring specific reserves. Loans identified in the risk rating evaluation as substandard, doubtful and loss, are segregated from non-classified loans. Classified loans are assigned allowance factors based on an impairment analysis. Allowance factors relate to the level of the internal risk rating with loans exhibiting higher risk ratings receiving a higher allowance factor.

The nonspecific or environmental factors allowance is an estimate of potential loss associated with the remaining loans (those not identified as either requiring specific reserves or having classified risk ratings). The loss estimates are based on more global factors, such as delinquency trends, loss history, trends in the volume and size of individual credits, effects of changes in lending policy, the experience and depth of management, national and local economic trends, any concentrations of credit risk, the quality of the loan review system and the effect of external factors such as competition and regulatory requirements. The environmental factors allowance captures losses whose impact on the portfolio may have occurred but have yet to be recognized in the other allowance factors.

Management has significant discretion in making the judgments inherent in the determination of the provision and allowance for credit losses, including, in connection with the valuation of collateral, a borrower's prospects of repayment, and in establishing allowance factors on the formula allowance and nonspecific or environmental allowance components of the allowance. The establishment of allowance factors is a continuing evaluation, based on management's ongoing assessment of the global factors discussed above and their impact on the portfolio. The allowance factors may change from period to period, resulting in an increase or decrease in the

amount of the provision or allowance, based upon the same volume and classification of loans. Changes in allowance factors have a direct impact on the amount of the provision, and a related, after tax effect on net income. Errors in management's perception and assessment of the global factors and their impact on the portfolio could result in the allowance not being adequate to cover losses in the portfolio, and may result in additional provisions or charge-offs. Alternatively, errors in management's perception and assessment of the global factors and their impact on the portfolio could result in the allowance being in excess of amounts necessary to cover losses in the portfolio, and may result in lower provisioning in the future. For additional information regarding the allowance for credit losses, refer to the discussion under the caption Allowance for Credit Losses below.

Beginning in January 2006, the Company adopted the provisions of SFAS No. 123R, which requires the expense recognition for the fair value of share based compensation awards, such as stock options, restricted stock, performance based shares and the like. This standard allows management to establish modeling assumptions as to expected stock price volatility, option terms, forfeiture rates and dividend rates which directly impact estimated fair value. The accounting standard also allows for the use of alternative option pricing models which may impact fair value as determined. The Company's practice is to utilize reasonable and supportable assumptions which are reviewed with the appropriate Board Committee.

RESULTS OF OPERATIONS

Summary

The Company reported net income of \$3.7 million for the six months ended June 30, 2007, as compared to net income of \$4.0 million for the six months ended June 30, 2006, a decline of 8%. Income per basic share was \$0.38 for the six month period ended June 30, 2007, as compared to \$0.42 for the same period in 2006. Income per diluted share was \$0.37 for the six months ended June 30, 2007, as compared to \$0.40 for the same period in 2006.

For the three months ended June 30, 2007, the Company reported net income of \$2.0 million as compared to \$2.0 million for the same period in 2006. Income per basic share was \$0.21 and \$0.20 per diluted share for the three months ended June 30, 2007 and 2006.

Earnings per share for the three and six months ended June 30, 2006, have been adjusted to reflect a 1.3 for 1 stock split in the form of a 30% stock dividend paid on July 5, 2006.

The Company had an annualized return on average assets of 0.95% and an annualized return on average equity of 9.98% for the first six months of 2007, as compared to returns on average assets and average equity of 1.17% and 11.91%, respectively, for the same six months of 2006.

For the three months ended June 30, 2007, the Company had an annualized return on average assets of 1.02% and an annualized return on average equity of 10.50%.

The decrease in net income for the six months ended June 30, 2007 can be attributed substantially to an increase in interest expense of 54% while interest income increased by 19% as compared to the same period in 2006. Net interest income showed an increase of 2% on growth in average earning assets of 13%. For the six months ended June 30, 2007, the Company has experienced a 48 basis point decline in its net interest margin from 4.91% in 2006 to 4.43% in 2007. This change was primarily due to a flatter yield curve and reliance on more expensive sources of funds which has increased interest expenses at a faster rate than increases in interest income.

For the three months ended June 30, 2007, net interest income showed an increase of 3% as compared to the same period in 2006 on growth in average earning assets of 11%. For the three months ended June 30, 2007 as compared to the same period in 2006, the Company experienced a decline in its net interest margin from 4.82% to 4.45% or 37 basis points. The decrease for the quarter ended June 30, 2007, is primarily due to the same reasons stated above for the decline in the margin for the six month period ended June 30, 2007.

For the six months ended June 30, 2007, average interest bearing liabilities funding average earning assets increased to 77% as compared to 72% for the first six months of 2006. Additionally, while the average rate on earning assets for the six month period ended June 30, 2007, as compared to 2006 has risen by 36 basis points from

7.27% to 7.63%, the cost of interest bearing liabilities has increased by 89 basis points from 3.29% to 4.18%, resulting in a decline in the net interest spread of 53 basis points from 3.98% for the six months ended June 30, 2006 to 3.45% for the six months ended June 30, 2007. The 48 basis point decline in the net interest margin has been less than the decline in the net interest spread as the Company continues to benefit from a significant amount of average noninterest bearing funding sources. For the six months ended June 30, 2007, average noninterest sources funding earning assets was \$172 million as compared to \$185 million for the same period in 2006. The combination of higher levels of market interest rates and a slight decline in noninterest funding sources has resulted in an increase in the value of noninterest sources funding earning assets from 93 basis points for the first six months in 2006 to 98 basis points for the six months ended June 30, 2007.

Due to competitive pressures, rates paid on deposits, which have been increasing to meet funding needs, may continue to have increases in future periods, which may not be offset by further increases in interest rates on earning assets. As a result of such potential margin compression, the Company's earnings could be adversely impacted.

Loans, which generally have higher yields than securities and other earning assets, increased from 86% of average earning assets in the first six months of 2006 to 87% of average earning assets for the same period of 2007. Investment securities for both the first six months of 2007 and 2006 amounted to 11% of average earning assets, while federal funds sold averaged 1% in the first six months of 2007 versus 3% of average earning assets for the same period of 2006. This decline was directly related to average loan growth over the past twelve month period exceeding the growth of average deposit and other funding sources.

The provision for credit losses was \$339 thousand for the first six months in 2007 as compared to \$707 thousand for the same period in 2006. This decrease was largely attributable to an adjustment down in two factors evaluated within the component of the allowance related to environmental factors. The two specific factors warranting adjustment related to a decrease in the factor assigned to loan growth, consistent with a reduced overall rate of growth in the loan portfolio in the current year as compared to prior years, and a decrease in the factor assigned to a rising interest rate environment, consistent with the Federal Reserve Bank's stabilization of the discount rate over the past year and consequent leveling of interest rates to borrowers.

In total, the ratio of net charge-offs to average loans was .13% for the first six months of 2007 as compared to .14% for the first six months of 2006. The continued management of a quality loan portfolio remains a key objective of the Company.

Total noninterest income was \$2.2 million for the first six months of 2007 as compared to \$1.7 million for the same period in 2006, a 30% increase. Excluding securities gains of \$7 thousand during the first six months of 2007 and \$156 thousand during the same period in 2006, noninterest income increased by 43% for the first six months of 2007 as compared to the same period in 2006. The increase was attributed primarily to higher amounts of gains on the sale of SBA (\$349 thousand versus \$169 thousand) and residential mortgage loans (\$222 thousand versus \$73 thousand), higher deposit activity fees (\$713 thousand versus \$667 thousand) and income from subordinate financing of real estate projects (\$227 thousand versus \$0). Activity in SBA sales to secondary markets can vary widely from period to period. Income from subordinated financing activities is also subject to wide variances, as it is based on the sales progress of a limited number of development projects. Total noninterest income for the second quarter of 2007 was \$1.2 million compared to \$845 thousand for the second quarter of 2006, an increase of 41%. Excluding securities gains of \$156 thousand during the second quarter of 2006, noninterest income increased by 73%. The increase was due to the same factors mentioned above which affected the increase for the six month period. The efficiency ratio for the second quarter of 2007 was 66.33% as compared to 58.38% for the same period in 2006.

Total noninterest expenses increased from \$10.4 million in the first six months of 2006 to \$12.3 million for the first six months of 2007, an increase of 18%. The primary reasons for this increase were increases in staff levels, and related personnel cost, occupancy cost (due to a new banking office and an expanded lending center facility), higher software licensing costs and fees associated with a reinstated FDIC deposit insurance assessment. The efficiency ratio for the first six months of 2007 was 66.88% as compared to 59.25% for the same period in 2006. For the three months ended June 30, 2007, total noninterest expenses were \$6.2 million, as compared to \$5.2 million for

the same period in 2006, an increase of 21%. This increase was due to the same factors mentioned above which affected the increase for the six month period.

For the six months ended June 30, 2007 as compared to 2006, the combination of a slight increase in net interest income from increased volumes, a lower provision for credit losses and higher levels of noninterest income offset by a lower net interest margin and higher levels of noninterest expenses, resulted in an 8% decline in net income during the six month period. For the three months ended June 30, 2007, the same factors resulted in a .6% decline in net income, as compared to the same period in 2006.

The ratio of average equity to average assets declined from 9.79% for the first six months of 2006 to 9.65% for the first six months of 2007. As discussed below, the capital ratios of the Bank and Company remain above well capitalized levels.

Net Interest Income and Net Interest Margin

Net interest income is the difference between interest income on earning assets and the cost of funds supporting those assets. Earning assets are composed primarily of loans and investment securities. The cost of funds represents interest expense on deposits, customer repurchase agreements and other borrowings. Noninterest bearing deposits and capital are other components representing funding sources, which factors have been significant in the second quarter of 2007 versus 2006 (refer to discussion above under Results of Operations). Changes in the volume and mix of assets and funding sources, along with the changes in yields earned and rates paid, determine changes in net interest income. Net interest income for the first six months of 2007 was \$16.2 million compared to \$15.8 million for the first six months of 2006, a 2% increase. For the three months ended June 30, 2007, net interest income was \$8.2 million as compared to \$8.0 million for the same period in 2006, a 3% increase.

The table below labeled "Average Balances, Interest Yields and Rates and Net Interest Margin" presents the average balances and rates of the various categories of the Company's assets and liabilities. Included in the table is a measurement of interest rate spread and margin. Interest spread is the difference (expressed as a percentage) between the interest rate earned on earning assets less the interest expense on interest bearing liabilities. While net interest spread provides a quick comparison of earnings rates versus cost of funds, management believes that margin provides a better measurement of performance. Margin includes the effect of noninterest bearing sources in its calculation and is net interest income expressed as a percentage of average earning assets.

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EAGLE BANCORP, INC.

Average Balances, Interest Yields and Rates, and Net Interest Margin
(dollars in thousands)

	Six Months Ended June 30, 2007				2006		
	Average Balance	Interest	Average Yield/Rate		Average Balance	Interest	Average Yield/Rate
ASSETS							
Interest earning assets:							
Interest bearing deposits with other banks and other short-term investments	\$ 4,570	\$ 131	5.78	%	\$ 2,394	\$ 73	6.15
Loans (1) / (2)	642,001	25,498	8.01	%	556,996	21,457	7.77
Investment securities available for sale	81,440	2,018	5.00	%	70,373	1,427	4.09
Federal funds sold	7,520	196	5.26	%	20,343	480	4.76
Total interest earning assets	735,531	27,843	7.63	%	650,106	23,437	7.27
Total noninterest earning assets	46,564				43,289		
Less: allowance for credit losses	7,407				6,111		
Total noninterest earning assets	39,157				37,178		
TOTAL ASSETS	\$ 774,688				\$ 687,284		
LIABILITIES AND STOCKHOLDERS EQUITY							
Interest bearing liabilities:							
Interest bearing transaction	\$ 53,575	\$ 126	0.47	%	\$ 50,211	\$ 86	0.35
Savings and money market	168,400	3,073	3.68	%	156,279	2,359	3.04
Time deposits	266,084	6,624	5.02	%	212,501	4,243	4.03
Customer repurchase agreements and federal funds purchased	42,841	970	4.57	%	31,193	481	3.11
Other short-term borrowings	7,757	212	5.51	%	14,709	427	5.85
Long-term borrowings	25,160	671	5.38	%			
Total interest bearing liabilities	563,817	11,676	4.18	%	464,893	7,596	3.29
Noninterest bearing liabilities:							
Noninterest bearing demand	132,415				148,697		
Other liabilities	3,732				6,438		
Total noninterest bearing liabilities	136,147				155,135		
Stockholders equity	74,724				67,256		
TOTAL LIABILITIES AND STOCKHOLDERS EQUITY	\$ 774,688				\$ 687,284		
Net interest income		\$ 16,167				\$ 15,841	
Net interest spread			3.45	%			3.98
Net interest margin			4.43	%			4.91

(1) Includes Loans held for Sale

(2) Loans placed on nonaccrual status are included in average balances. Net loan fees and late charges in interest income on loans totaled \$697 thousand and \$916 thousand for the six months ended June 30, 2007 and 2006, respectively.

Allowance for Credit Losses

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The provision for credit losses represents the amount of expense charged to current earnings to fund the allowance for credit losses. The amount of the allowance for credit losses is based on many factors which reflect management's assessment of the risk in the loan portfolio. Those factors include economic conditions and trends,

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the value and adequacy of collateral, volume and mix of the portfolio, performance of the portfolio, and internal loan processes of the Company and Bank.

Management has developed a comprehensive analytical process to monitor the adequacy of the allowance for credit losses. This process and guidelines were developed utilizing among other factors, the guidance from federal banking regulatory agencies. The results of this process, in combination with conclusions of the Bank's outside loan review consultant, support management's assessment as to the adequacy of the allowance at the balance sheet date. Please refer to the discussion under the caption "Critical Accounting Policies" for an overview of the methodology management employs on a quarterly basis to assess the adequacy of the allowance and the provisions charged to expense. Also, refer to the following table which reflects the comparative charge-offs and recoveries of prior loan charge-offs information.

During the first six months of 2007, a provision for credit losses was made in the amount of \$339 thousand and the allowance for credit losses decreased \$85 thousand, including the impact of \$424 thousand in net charge-offs during the period (of which \$350 thousand related to one large commercial loan relationship identified in the third quarter of 2006 and which the Company believes is fully reserved). The provision for credit losses of \$339 thousand in the first six months of 2007 compared to a provision for credit losses of \$707 thousand in the first six months of 2006. The lower level of the provision in 2007 is primarily attributable to an adjustment down (in the second quarter of 2007) in two factors evaluated within the component of the allowance related to environmental factors. The two specific factors warranting adjustment related to a decrease in the factor assigned to loan growth, consistent with a reduced overall rate of growth in the loan portfolio in the current year as compared to prior years, and a decrease in the factor assigned to a rising interest rate environment, consistent with the Federal Reserve Bank's stabilization of the discount rate over the past year and consequent leveling of interest rates to borrowers.

During the quarter ended June 30, 2007, a provision for credit losses was made in the amount of \$36 thousand and the allowance for credit losses increased \$25 thousand, including the impact of \$11 thousand in net charge-offs during the quarter ended. The provision for credit losses of \$36 thousand in the quarter ended June 30, 2007 compared to \$592 thousand in the same period of 2006. The lower level of the provision in 2007 is attributable to the lowering of the environmental factors within the allowance analysis stated above.

At June 30, 2007, the Company had \$1.5 million of loans classified as nonperforming, consisting of a single commercial loan relationship, as compared to \$2.4 million at June 30, 2006, \$2.0 million at December 31, 2006, and \$1.6 million at March 31, 2007. The Company had no restructured loans at June 30, 2007, March 31, 2007, December 31, 2006 or June 30, 2006. Significant variation in these amounts may occur from period to period because the amount of nonperforming loans depends largely on the condition of a small number of individual credits and borrowers relative to the total loan portfolio. The Company had no Other Real Estate Owned (OREO) at June 30, 2007 and December 31, 2006 and \$798 thousand at June 30, 2006. The balance of impaired loans was \$1.5 million which consisted entirely of the commercial loan relationship identified above, with specific reserves against those loans of \$500 thousand at June 30, 2007, compared to \$134 thousand of impaired loans at June 30, 2006 with specific reserves of \$60 thousand. The allowance for loan losses represented 1.11% of total loans at June 30, 2007 as compared to 1.14% at March 31, 2007; 1.18% at December 31, 2006, and 1.10% at June 30, 2006.

As part of its comprehensive loan review process, the Company's Board of Directors and the Bank Director's Loan Committee and or Board of Director's Credit Review Committees carefully evaluates loans which are past-due 30 days or more. The Committee(s) make a thorough assessment of the conditions and circumstances surrounding each delinquent loan. The Bank's loan policy requires that loans be placed on nonaccrual if they are ninety days past-due, unless they are well secured and in the process of collection.

The maintenance of a high quality loan portfolio, with an adequate allowance for possible loan losses, will continue to be a primary management objective for the Company.

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The following table sets forth activity in the allowance for credit losses for the periods indicated.

(dollars in thousands)	Six Months Ended		
	June 30, 2007	2006	
Balance at beginning of year	\$ 7,373	\$ 5,985	
Charge-offs:			
Commercial	421	369	
Real estate commercial			
Construction			
Home equity			
Other consumer	24	15	
Total charge-offs	445	384	
Recoveries:			
Commercial	8		
Real estate commercial			
Construction			
Home equity			
Other consumer	13	5	
Total recoveries	21	5	
Net charge-offs	(424)	(379)	
Additions charged to operations	339	707	
Balance at end of period	\$ 7,288	\$ 6,313	
Annualized ratio of net charge-offs during the period to average loans outstanding during the period	0.13	% 0.14	%

The following table reflects the allocation of the allowance for credit losses at the dates indicated. The allocation of the allowance to each category is not necessarily indicative of future losses or charge-offs and does not restrict the use of the allowance to absorb losses in any category.

(dollars in thousands)	As of June 30, 2007		As of December 31, 2006		
	Amount	% (1)	Amount	% (1)	
Commercial	\$ 3,273	21	% \$ 3,379	21	%
Real estate commercial	2,770	55	% 2,800	56	%
Real estate residential	22	0	% 40	0	%
Construction - commercial and residential	949	15	% 854	14	%
Home equity	184	8	% 176	8	%
Other consumer	90	1	% 124	1	%
Total loans	\$ 7,288	100	% \$ 7,373	100	%

(1) Represents the percent of loans in each category to total loans.

Nonperforming Assets

The Company's nonperforming assets, which are comprised of loans delinquent 90 days or more, non-accrual loans, restructured loans and other real estate owned, totaled \$1.5 million at June 30, 2007 compared to \$3.2 million at June 30, 2006. The percentage of nonperforming loans to total loans was 0.22% at June 30, 2007, compared to .25% at March 31, 2007; .32% at December 31, 2006 and .41% at June 30, 2006.

The following table shows the amounts of nonperforming assets at the dates indicated.

(dollars in thousands)	June 30, 2007	2006	December 31, 2006
Nonaccrual Loans			
Commercial	\$ 1,450	\$ 2,374	\$ 1,976
Consumer			
Real estate			
Accrual loans-past due 90 days			
Commercial			37
Consumer			
Real estate			
Restructured loans			
Real estate owned		798	
Total non-performing assets	\$ 1,450	\$ 3,172	\$ 2,013

The Company experienced a decrease in the level of nonaccrual loans at June 30, 2007 as compared to both March 31, 2007 and December 31, 2006. This resulted primarily from a partial charge-off in the amount of \$350 thousand associated with a problem commercial lending relationship originally identified and provisioned for in the third quarter of 2006 and from the resolution of another problem loan in the third quarter of 2006. The current non-accrual loans of \$1.5 million relates to the one commercial lending relationship mentioned above, and which the Company believes is fully reserved for any potential shortfall between collateral values and outstanding balance.

At June 30, 2007, there were an additional \$4.4 million of performing loans considered potential problem loans, defined as loans which are not included in the past-due, nonaccrual or restructured categories, but for which known information about possible credit problems causes management to be uncertain as to the ability of the borrowers to comply with the present loan repayment terms which may in the future result in disclosures in the past-due, nonaccrual or restructured loan categories. Approximately \$4 million of the potential problem loans consists of two loans to related borrowers. One of the guarantors on these related facilities filed for Chapter 11 bankruptcy protection in late July, 2007. The subject guarantor's guaranty is secured by an indemnity deed of trust on real estate owned by the guarantor. Although the bankruptcy filing may impede the Company's ability to realize upon the assets securing the guaranty, and could adversely impact future cash flow and the ongoing collection of payments as and when due, which could result in the loans being reported as nonperforming in the future, management believes the related loans remain well secured, although there can be no assurance.

Noninterest Income

Total noninterest income consists primarily of deposit account service charges, gains on the sale of SBA and residential mortgage loans, other noninterest loan fees, income from bank owned life insurance (BOLI), investment gains and losses, other service fees and income from subordinate financing for the acquisition, development and construction of real estate projects. For the six months ended June 30, 2007, noninterest income was \$2.2 million. This compared to \$1.7 million of noninterest income for the six months ended June 30, 2006, an increase of 30%. Excluding securities gains of \$7 thousand during the first six months of 2007 and \$156 thousand during the same period in 2006, noninterest income increased by 43%. The increase was attributed primarily to higher amounts of gains on the sale of SBA and residential mortgage loans, higher deposit activity fees and income from subordinate financing of real estate projects. Activity in SBA sales to secondary markets can vary widely from

period to period. Income from subordinated financing activities is also subject to wide variances, as it is based on the sales progress of a limited number of development projects.

Total noninterest income for the second quarter of 2007 was \$1.2 million compared to \$845 thousand for the second quarter of 2006, an increase of 41%. Excluding securities gains of \$156 thousand during the second quarter of 2006 and \$7 thousand for the second quarter of 2007, noninterest income increased by 73%. The increase was due to the same factors mentioned above which affected the increase for the six month period.

The Company is an active originator of SBA loans and its current practice is to sell the insured portion of those loans at a premium. Income from this source was \$349 thousand for the six months ended June 30, 2007 compared to \$169 thousand for the six months ended June 30, 2006. For the three months ended June 30, 2007, gains on the sale of SBA loans amounted to \$201 thousand as compared to \$31 thousand for the same period in 2006. Activity in SBA loan sales to secondary markets can vary widely from quarter to quarter. EagleBank has been recognized as the leading community bank SBA lender in its marketplace and continued emphasis is anticipated.

The Company originates residential mortgage loans on a pre-sold basis, servicing released. Sales of these mortgage loans yielded gains of \$222 thousand in the first six months of 2007 compared to \$73 thousand in the same period in 2006. For the three months ended June 30, 2007, gains on the sale of residential mortgage loans were \$133 thousand as compared to \$35 thousand for the same three months of 2006. The Company continues its efforts to expand residential mortgage lending and associated sale of these assets on a servicing released basis. Loans sold are subject to repurchase in circumstances where documentation is not accurate or the underlying loan becomes delinquent within a specified period following sale and loan funding. The Bank considers these potential recourse provisions to be minimal and to date have experienced no repurchases.

The Company also provides subordinate financing for the acquisition, development and construction of real estate projects. These subordinate financings which are held by its wholly owned subsidiary ECV, generally entail a higher risk profile (including lower priority and higher loan to value ratios) than other loans made by the Bank. A portion of the amount which the Company expects to receive for such loans will be payments based on the success, sale or completion of the underlying project, and as such the income from these loans may be volatile from period to period, based on the status of such projects. For the six and three months ended June 30, 2007 the Company recognized \$227 thousand as the settlement of units occurred, compared to \$0 for the same periods in 2006. The Company expects settlement of additional units in 2007 and 2008.

Noninterest income for the six months ended June 30, 2007 included \$713 thousand from deposit account service charges, \$85 thousand from SBA loan service fees and \$220 thousand from BOLI, versus \$667 thousand from deposit account service charges, \$104 thousand from SBA service fees and \$197 thousand from BOLI for the six months ended June 30, 2006. Income for the three months ended June 30, 2007 included \$364 thousand from deposit account service charges, \$28 thousand from SBA loan service fees and \$113 thousand from BOLI, versus \$343 thousand from deposit account service charges, \$42 thousand from SBA service fees and \$100 thousand from BOLI for the three months ended June 30, 2006. Other noninterest income which comprises primarily loan commitment fees on terminated transactions, and loan prepayment fees, amounted to \$372 thousand for the first six months of 2007, as compared to \$320 thousand in the first six months of 2006. Other noninterest income amounted to \$131 thousand for the three months ended June 30, 2007, as compared to \$139 thousand in the three months ended June 30, 2006. The increase in deposit service fees was primarily related to new relationships.

For the three and six months ended June 30, 2007, investment gains amounted to \$0 and \$7 thousand, respectively as compared to \$156 thousand for the three and six months ended June 30, 2006.

Noninterest Expense

Total noninterest expense was \$12.3 million for the six months ended June 30, 2007 compared to \$10.4 million for the six months ended June 30, 2006, an increase of 18%.

For the three months ended June 30, 2006, total noninterest expense was \$6.2 million versus \$5.2 million for the same period in 2006, a 21% increase.

Salaries and benefits were \$6.8 million for the first six months of 2007, as compared to \$5.9 million for 2006, a 14% increase. For the three months ended June 30, 2007, salaries and benefits amounted to \$3.4 million versus \$3.0 million for the same period in 2006, a 16% increase. This increase was due to staff additions and related personnel costs, merit increases and increased benefit costs, offset by a decline in incentive based compensation. At June 30, 2007, the Company's staff numbered 172, as compared to 168 at March 31, 2007 and 153 at June 30, 2006.

Premises and equipment expenses amounted to \$2.5 million for the six months ended June 30, 2007 versus \$1.7 million for the same period in 2006. This increase of 46% was due to a new banking office opened in mid May 2006 and an expanded lending center facility opened in the first quarter of 2007. Additionally, ongoing operating expense increases associated with the Company's facilities, all of which are leased and increased equipment costs contributed to the overall increase in expense. For the three months ended June 30, 2007, premises and equipment expenses amounted to \$1.3 million versus \$819 thousand for the same period in 2006. The reason for the increase in expense for the three month period is the same as mentioned above for the six months ended.

Advertising costs decreased from \$264 thousand in the six months ended June 30, 2006 to \$222 thousand in the same period in 2007, a decrease of 16%. For the three months ended June 30, 2007, advertising expenses amounted to \$131 thousand versus \$145 thousand for the same period in 2006, a decrease of 10%. This decline was due primarily to lower levels of product advertising.

Outside data processing costs were \$445 thousand for the first six months of 2007, as compared to \$436 thousand in 2006, an increase of 2%. For the three months ended June 30, 2007, outside data processing costs amounted to \$183 thousand versus \$209 thousand for the same period in 2006, a decrease of 12%. This decline in the three months ended June 30, 2007 as compared to 2006 was due to savings achieved from the renegotiation of the bank's primary data processing vendor agreement. The increase for the six month period ended June 30 was due to increases in numbers of accounts and services and to network management and wire system enhancements offset substantially by the contract renegotiation savings mentioned above.

Other expenses, increased from \$2.0 million in the first six months of 2006 to \$2.3 million for the six months ended June 30, 2007, or an increase of 14%. For the three months ended June 30, 2007, other expenses amounted to \$1.2 million versus \$1.0 million for the same period in 2006, an increase of 19%. The major components of costs in this category include professional fees, including audit and accounting, ATM expenses, telephone, courier, printing, business development, office supplies, charitable contributions, director fees, dues and FDIC insurance premiums. For the first six months of 2007, as compared to 2006, the significant increases in this category were primarily broker fees, internet and license agreements, loan related expenses and the reinstated requirement that the Bank pay deposit insurance premiums. For the three months ended June 30, 2007, as compared to 2006, the increased costs relate to broker fees, internet and license agreements, audit and accounting fees and the reinstated requirement that the Bank pay deposit insurance premiums.

Income Tax Expense

The Company's ratio of income tax expense to pre-tax income (termed effective tax rate) decreased to 36.3% for the six months ended June 30, 2007 as compared to 38.2% for the same period in 2006. This decrease was due primarily to higher amounts of U.S. government agency income in the six months of 2007 as compared to 2006, which is non-taxable for state tax purposes, and to lower amounts of share based compensation in 2007 as compared to 2006 which is partially non-deductible for financial accounting purposes. For the second quarter of 2007 as compared to 2006, the effective tax rate was 36.7% as compared to 35.6%.

FINANCIAL CONDITION

Summary

At June 30, 2007, assets were \$813.0 million, loans were \$659.2 million, deposits were \$650.5 million, customer repurchase agreements and other borrowings were \$82.6 million and stockholders' equity was \$76.0 million. As compared to December 31, 2006, assets grew by \$39.6 million (5.1%), loans by \$33.5 million (5.4%), deposits by \$22.0 million (3.5%), customer repurchase agreements and other borrowings increased by \$14.5 million (21.3%) and stockholders' equity grew by \$3.1 million (4.2%).

The Company paid cash dividends of \$0.06 and \$0.05 per share in the first quarter of 2007 and 2006, respectively, as adjusted for the 1.3 to 1 stock split paid in July 2006.

Loans

Loans, net of amortized deferred fees and costs, at June 30, 2007, December 31, 2006 and June 30, 2006 by major category are summarized below:

(dollars in thousands)	As of June 30, 2007		As of December 31, 2006		As of June 30, 2006		
	Amount	%	Amount	%	Amount	%	
Commercial	\$ 137,587	21	% \$ 132,981	21	% \$ 119,678	21	%
Real estate mortgage commercial	363,345	55	% 349,044	56	% 304,234	54	%
Real estate mortgage residential	1,386	0	% 1,523	0	% 2,120	0	%
Construction - commercial and residential	100,678	15	% 86,524	14	% 88,742	15	%
Home equity	52,558	8	% 50,572	8	% 54,152	9	%
Other consumer	3,679	1	% 5,129	1	% 4,102	1	%
Total loans	659,233	100	% \$ 625,773	100	% 573,028	100	%
Less: Allowance for Credit Losses	(7,288)		(7,373)		(6,313)		
Net Loans and Leases	\$ 651,945		\$ 618,400		\$ 566,715		

Deposits and Other Borrowings

The principal sources of funds for the Bank are core deposits, consisting of demand deposits, NOW accounts, money market accounts, savings accounts and certificates of deposits from the local market areas surrounding the Bank's offices. The deposit base includes transaction accounts, time and savings accounts and accounts which customers use for cash management and which provide the Bank with a source of fee income and cross-marketing opportunities, as well as an attractive source of lower cost funds. Time and savings accounts, including money market deposit accounts, also provide a relatively stable and low-cost source of funding.

For the six months ending June 30, 2007, noninterest bearing deposits increased \$5.3 million as compared to December 31, 2006, while interest bearing deposits increased by \$16.6 million during the same period, primarily due to growth in savings and certificates of deposits accounts.

Approximately 42% of the Bank's deposits at June 30, 2007 are made up of time deposits, which are generally the most expensive form of deposit because of their fixed rate and term. Certificates of deposit in denominations of \$100 thousand or more can be more volatile and more expensive than certificates of less than \$100 thousand. However, because the Bank focuses on relationship banking, its historical experience has been that large certificates of deposit have not been more volatile or significantly more expensive than smaller denomination certificates. It has been the practice of the Bank to pay posted rates on its certificates of deposit whether under or over \$100 thousand, although some exceptions have been made for large deposit transactions. When appropriate in order to fund strong loan demand, the Bank accepts certificates of deposits, generally in denominations of less than

\$100 thousand from bank and credit union subscribers to a wholesale deposit rate line and to brokered deposits obtained from qualified investment firms. These deposits amounted to approximately \$36 million or 5% of total deposits at June 30, 2007, as compared to approximately \$7 million of deposits or 1% of total deposits at June 30, 2006 and approximately \$18 million or 3% of total; deposits at December 31, 2006. The Bank has found rates on these deposits to be generally competitive with rates in our market given the speed and minimal noninterest cost at which these deposits can be acquired.

At June 30, 2007, the Company had approximately \$145 million in noninterest bearing demand deposits, representing 22% of total deposits. This compared to approximately \$140 million of these deposits at December 31, 2006. These deposits are primarily business checking accounts on which the payment of interest is prohibited by regulations of the Federal Reserve. Proposed legislation has been introduced in each of the last several sessions of Congress which would permit banks to pay interest on checking and demand deposit accounts established by businesses. If legislation effectively permitting the payment of interest on business demand deposits is enacted, of which there can be no assurance, it is likely that we may be required to pay interest on some portion of our noninterest bearing deposits in order to compete with other banks. Payment of interest on these deposits could have a significant negative impact on our net interest income and net interest margin, net income, and the return on assets and equity.

As an enhancement to the basic noninterest bearing demand deposit account, the Company offers a sweep account, or customer repurchase agreement, allowing qualifying businesses to earn interest on short term excess funds which are not suited for either a CD investment or a money market account. The balances in these accounts were \$41 million at June 30, 2007 compared to \$38 million at December 31, 2006. Customer repurchase agreements are not deposits and are not insured but are collateralized by U.S. government agency securities. These accounts are particularly suitable to businesses with significant fluctuation in the levels of cash flows. Attorney and title company escrow accounts are an example of accounts which can benefit from this product, as are customers who may require collateral for deposits in excess of \$100 thousand but do not qualify for other pledging arrangements. This program requires the Company to maintain a sufficient investment securities level to accommodate the fluctuations in balances which may occur in these accounts.

At June 30, 2007, the Company had no outstanding balances under its lines of credit provided by a correspondent bank. The Bank had \$42 million of FHLB borrowings outstanding at June 30, 2007 and \$30 million outstanding at December 31, 2006. These advances are secured by a blanket lien on qualifying loans in the Bank's commercial mortgage and home equity loan portfolios.

Liquidity Management

Liquidity is a measure of the Bank's ability to meet loan demand and to satisfy depositor withdrawal requirements in an orderly manner. The Bank's primary sources of liquidity consist of cash and cash balances due from correspondent banks, loan repayments, federal funds sold and other short-term investments, maturities and sales of investment securities and income from operations. The Bank's entire investment securities portfolio is in an available-for-sale status which allows it flexibility to generate cash from sales as needed to meet ongoing loan demand. These sources of liquidity are primary and are supplemented by the ability of the Company and Bank to borrow funds, which are termed secondary sources. The Company maintains secondary sources of liquidity, which includes a \$15 million line of credit with a correspondent bank, secured by the stock of the Bank, against which there were no amounts outstanding at June 30, 2007. Additionally, the Bank can purchase up to \$66.5 million in federal funds on an unsecured basis and \$5.5 million on a secured basis from its correspondents, against which there were no borrowings outstanding at June 30, 2007. At June 30, 2007, the Bank was also eligible to take advances from the FHLB up to \$103 million based on collateral at the FHLB, of which it had \$42 million of advances outstanding at June 30, 2007. Also, the Bank may enter into repurchase agreements as well as obtaining additional borrowing capabilities from the FHLB provided adequate collateral exists to secure these lending relationships.

The loss of deposits, through disintermediation, is one of the greater risks to liquidity. Disintermediation occurs most commonly when rates rise and depositors withdraw deposits seeking higher rates in alternative savings and investment sources than banks may offer. The Bank was founded under a philosophy of relationship banking and, therefore, believes that it has less of an exposure to disintermediation and resultant liquidity concerns than do

many banks. There is, however, a risk that some deposits would be lost if rates were to increase and the Bank elected not to remain competitive with its deposit rates. Under those conditions, the Bank believes that it is well positioned to use other sources of funds such as FHLB borrowings, customer repurchase agreements and Bank lines of credit to offset a decline in deposits in the short run. Over the long-term, an adjustment in assets and change in business emphasis could compensate for a potential loss of deposits. The Bank also maintains a marketable investment portfolio to provide flexibility in the event of significant liquidity needs. The Bank Board's Asset Liability Committee has adopted policy guidelines which emphasize the importance of core deposits and their continued growth.

At June 30, 2007, under the Bank's liquidity formula, it had \$262 million of primary and secondary liquidity sources, which was deemed adequate to meet current and projected funding needs.

Commitments and Contractual Obligations

The following is a schedule of significant funding commitments at June 30, 2007:

	(in thousands)
Unused lines of credit (consumer)	\$ 53,011
Other commitments to extend credit	145,224
Standby letters of credit	10,177
Total	\$ 208,412

Asset/Liability Management and Quantitative and Qualitative Disclosure about Market Risk

A fundamental risk in banking is exposure to market risk, or interest rate risk, since a bank's net income is largely dependent on net interest income. The Bank's Asset Liability Committee (ALCO) of the Board of Directors formulates and monitors the management of interest rate risk through policies and guidelines established by it and the full Board of Directors. In its consideration of risk limits, the ALCO considers the impact on earnings and capital, the level and direction of interest rates, liquidity, local economic conditions, outside threats and other factors. Banking is generally a business of managing the maturity and re-pricing mismatch inherent in its asset and liability cash flows and to provide net interest income growth consistent with the Company's profit objectives.

The Company, through its ALCO, monitors the interest rate environment in which it operates and adjusts the rates and maturities of its assets and liabilities to remain competitive and to achieve its overall financial objectives subject to established risk limits. In the current interest rate environment, the Company has been extending the duration of its loan portfolio and acquiring more variable and short-term liabilities, so as to mitigate the risk to earnings and capital should interest rates decline from current levels. There can be no assurance that the Company will be able to successfully achieve its optimal asset liability mix, as a result of competitive pressures, customer preferences and the inability to perfectly forecast future interest rates.

One of the tools used by the Company to manage its interest rate risk is a static GAP analysis presented below. The Company also uses an earnings simulation model (simulation analysis) on a quarterly basis to monitor its interest rate sensitivity and risk and to model its balance sheet cash flows and its income statement effects in different interest rate scenarios. The model utilizes current balance sheet data and attributes and is adjusted for assumptions as to investment maturities (calls), loan prepayments, interest rates, the level of noninterest income and noninterest expense. The data is then subjected to a "shock test", which assumes a simultaneous change in interest rate up 100 and 200 basis points or down 100 and 200 basis points, along the entire yield curve, but not below zero. The results are analyzed as to the impact on net interest income, and net income over the next twelve and twenty four month periods and to the market value of equity impact. The Company's analysis at June 30, 2007 shows a positive effect on income when interest rates are shocked down 100 and 200 basis points, due to the significant level of variable rate and repricable liabilities. A negative impact occurs if rates were to increase based on the Company's liability sensitive position. Interest rate increases would increase income on earning assets less than the cost associated with interest bearing liabilities potentially resulting in net interest margin contraction.

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The following table reflects the result of a shock simulation on the June 30, 2007 balances.

Change in interest rates (basis points)	Percentage change in net interest income	Percentage change in net income	Percentage change in Market Value of Portfolio Equity	
+200	-3.9	% -9.8	% -5.5	%
+100	-1.9	% -4.8	% -3.5	%
0				
-100	+1.3	% +3.4	% +1.9	%
-200	+1.3	% +3.4	% +0.3	%

Certain shortcomings are inherent in the method of analysis presented in the foregoing table. For example, although certain assets and liabilities may have similar maturities or repricing periods, they may react in different degrees to changes in market interest rates. Also, the interest rates on certain types of assets and liabilities may fluctuate in advance of changes in market interest rates, while interest rates on other types may lag behind changes in market rates. Additionally, certain assets, such as adjustable-rate mortgage loans, have features that limit changes in interest rates on a short-term basis and over the life of the loan. Further, in the event of a change in interest rates, prepayment and early withdrawal levels could deviate significantly from those assumed in calculating the tables. Finally, the ability of many borrowers to service their debt may decrease in the event of a significant interest rate increase.

Gap Position

Banks and other financial institutions earnings are significantly dependent upon net interest income, which is the difference between interest earned on earning assets and interest expense on interest bearing liabilities.

In falling interest rate environments, net interest income is maximized with longer term, higher yielding assets being funded by lower yielding short-term funds, or what is referred to as a negative mismatch or GAP. Conversely, in a rising interest rate environment, net interest income is maximized with shorter term, higher yielding assets being funded by longer-term liabilities or what is referred to as a positive mismatch or GAP.

Based on the current economic environment, management has been extending (over the past 12 months) the duration of assets (both investments and loans) and emphasizing the acquisition of variable rate and shorter fixed rate liabilities. This strategy has mitigated the Company's exposure to lower interest rates as measured at June 30, 2007 as compared to the position at June 30, 2006. While management believes that this overall position creates a reasonable balance in managing its interest rate risk and maximizing its net interest margin within plan objectives, there can be no assurance as to actual results.

The GAP position, which is a measure of the difference in maturity and re-pricing volume between assets and liabilities, is a means of monitoring the sensitivity of a financial institution to changes in interest rates. The chart below provides an indication of the sensitivity of the Company to changes in interest rates. A negative GAP indicates the degree to which the volume of repriceable liabilities exceeds repriceable assets in given time periods. At June 30, 2007, the Company had a slight positive cumulative GAP position of approximately 2% of total assets out to three months and a negative cumulative GAP position of 14% out to 12 months, as compared to a three month positive GAP of 9% and a negative cumulative GAP out to 12 months of 10% at June 30, 2006 and a three month negative GAP of 1% and a negative cumulative GAP out to 12 months of 17% at December 31, 2006. The change in the GAP position at June 30, 2007 as compared to June 30, 2006 relates primarily to a change in the mix of deposits toward more time deposits with maturities within 12 months. The current position is within guideline limits established by ALCO.

If interest rates decline, the Company's net interest income and margin are expected to be relatively stable because of the present slight negative mismatch position out to 90 days combined with a more competitive business environment for both deposits and loans. Because competitive market behavior does not necessarily track the trend of interest rates but at times moves ahead of financial market influences, the change in the cost of liabilities may be different than anticipated by the GAP model. If this were to occur, the benefits of a declining interest rate environment may not be in accordance with management's expectations. If interest rates move significantly up or down, the Company's interest rate sensitivity position at June 30, 2007 as compared to June 30, 2006 shows very

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similar risk exposure, within established policy limits established by ALCO. Management has carefully considered its strategy to maximize interest income by reviewing interest rate levels, economic indicators and call features within its investment portfolio. These factors have been discussed with the ALCO and management believes that current strategies are appropriate to current economic and interest rate trends.

GAP Analysis

June 30, 2007

(dollars in thousand)

Repriceable in:	0-3 mos	4-12 mos	13-36 mos	37-60 mos	over 60 mos	Total Rate Sensitive	Non-sensitive	Total
RATE SENSITIVE ASSETS:								
Investments and bank deposits	\$ 6,070	\$ 9,975	\$ 26,845	\$ 24,177	\$ 5,382	\$ 72,449		
Loans (1)	290,470	68,069	148,687	141,012	13,849	662,087		
Fed funds and other short-term investments	32,529					32,529		
Other earning assets		11,748				11,748		
Total	\$ 329,069	\$ 89,792	\$ 175,532	\$ 165,189	\$ 19,231	\$ 778,813	\$ 34,203	\$ 813,016
RATE SENSITIVE LIABILITIES:								
Noninterest bearing demand	\$ 6,555	\$ 19,666	\$ 35,448	\$ 30,107	\$ 53,487	\$ 145,263		
Interest bearing transaction	15,870		10,580	10,580	15,865	52,895		
Savings and money market	177,496		626	417	1,876	180,415		
Time deposits	73,275	193,677	4,967			271,919		
Customer repurchase agreements	40,589					40,589		
Other borrowings		7,000	35,000			42,000		
Total	\$ 313,785	\$ 220,343	\$ 86,621	\$ 41,104	\$ 71,228	\$ 733,081	\$ 3,926	\$ 737,007
GAP	\$ 15,284	\$ (130,551)	\$ 88,911	\$ 124,085	\$ (51,997)	\$ 45,732		
Cumulative GAP	\$ 15,284	\$ (115,267)	\$ (26,356)	\$ 97,729	\$ 45,732			
Cumulative gap as percent of total assets	1.88	%(14.18)%(3.24)%12.02	%5.62	%		

(1) Includes loans held for sale

Although NOW and MMA accounts are subject to immediate repricing, the Bank's GAP model has incorporated a repricing schedule to account for a lag in rate changes based on our experience, as measured by the amount of those deposit rate changes relative to the amount of rate change in assets.

Capital Resources and Adequacy

The assessment of capital adequacy depends on a number of factors such as asset quality, liquidity, earnings performance, changing competitive conditions and economic forces, and the overall level of growth. The adequacy of the Company's current and future capital needs is monitored by management on an ongoing basis. Management seeks to maintain a capital structure that will assure an adequate level of capital to support anticipated asset growth and to absorb potential losses.

The capital position of both the Company and the Bank continues to exceed regulatory requirements to be considered well-capitalized. The primary indicators used by bank regulators in measuring the capital position are the tier 1 risk-based capital ratio, the total risk-based capital ratio, and the tier 1 leverage ratio. Tier 1 capital consists of common and qualifying preferred stockholders' equity less intangibles. Total risk-based capital consists of tier 1 capital, qualifying subordinated debt, and a portion of the allowance for credit losses. Risk-based capital ratios are calculated with reference to risk-weighted assets. The tier 1 leverage ratio measures the ratio of tier 1 capital to total average assets for

the most recent three month period.

The ability of the Company to continue to grow is dependent on its earnings and the ability to obtain additional funds for contribution to the Bank's capital, through additional borrowing, the sale of additional common stock, the sale of preferred stock, or through the issuance of additional qualifying equity equivalents, such as subordinated debt or trust preferred securities.

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The federal banking regulators have issued guidance for those institutions which are deemed to have concentrations in commercial real estate lending. Pursuant to the supervisory criteria contained in the guidance for identifying institutions with a potential commercial real estate concentration risk, institutions which have (1) total reported loans for construction, land development, and other land acquisitions which represent in total 100% or more of an institutions total risk-based capital; or (2) total commercial real estate loans representing 300% or more of the institutions total risk-based capital and the institution's commercial real estate loan portfolio has increased 50% or more during the prior 36 months are identified as having potential commercial real estate concentration risk. Institutions which are deemed to have concentrations in commercial real estate lending are expected to employ heightened levels of risk management with respect to their commercial real estate portfolios, and may be required to hold higher levels of capital. The Company, like many community banks, has a concentration in commercial real estate loans. Management has extensive experience in commercial real estate lending, and has implemented and continues to maintain heightened portfolio monitoring and reporting, and strong underwriting criteria with respect to its commercial real estate portfolio. The Company is well capitalized. Nevertheless, it is possible that we may be required to maintain higher levels of capital as a result of our commercial real estate concentration, which could require us to obtain additional capital, and may adversely affect shareholder returns.

Capital

The actual capital amounts and ratios for the Company and Bank as of June 30, 2007 and June 30, 2006 are presented in the table below:

(dollars in thousands)	Company Actual Amount	Ratio	Bank Actual Amount	Ratio	For Capital Adequacy Purposes Ratio	To Be Well Capitalized Under Prompt Corrective Action Provision Ratio *
As of June 30, 2007						
Total capital to risk-weighted assets	\$ 83,943	11.87%	\$ 75,791	10.84%	8.0	10.0
Tier 1 capital to risk-weighted assets	76,655	10.84%	68,539	9.80%	4.0	6.0
Tier 1 capital to average assets (leverage)	76,655	9.85%	68,539	8.89%	3.0	5.0
As of June 30, 2006						
Total capital to risk-weighted assets	\$ 75,822	12.06%	\$ 66,993	10.80%	8.0	10.0
Tier 1 to risk-weighted assets	69,509	11.05%	60,753	9.79%	4.0	6.0
Tier 1 capital to average assets (leverage)	69,509	9.87%	60,753	8.73%	3.0	5.0

* Applies to Bank only

Bank and holding company regulations, as well as Maryland law, impose certain restrictions on dividend payments by the Bank, as well as restricting extension of credit and transfers of assets between the Bank and the Company. At June 30, 2007, the Bank could pay dividends to the parent to the extent of its earnings so long as it maintained required capital ratios.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Please refer to Item 2 of this report, Management's Discussion and Analysis of Financial Condition and Results of Operations, under the caption Asset/Liability Management and Quantitative and Qualitative Disclosure about Market Risk.

Item 4. Controls and Procedures

The Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, evaluated as of the last day of the period covered by this report the effectiveness of the operation of the Company's disclosure controls and procedures, as defined in Rule 13a-14 under the Securities and Exchange Act of 1934. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective. There were no changes in

the Company's internal controls over financial reporting (as defined in Rule 13a-15 under the Securities Act of 1934) during the quarter ended June 30, 2007 that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1 - Legal Proceedings

From time to time the Company may become involved in legal proceedings. At the present time there are no proceedings which the Company believes will have an adverse impact on the financial condition or earnings of the Company.

Item 1A - Risk Factors

There have been no material changes as of June 30, 2007 in the risk factors from those disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2006.

Item 2 - Unregistered Sales of Equity Securities and Use of Proceeds

(a) Sales of Unregistered Securities. None

(b) Use of Proceeds. Not Applicable

(c) Issuer Purchases of Securities. None

Item 3 - Defaults Upon Senior Securities None

Item 4 - Submission of Matters to a Vote of Security Holders None

On May 15, 2007, the annual meeting of shareholders of the Company was held for the purpose of (1) electing nine directors, constituting the full Board of Directors, to serve one year terms or until their successors are elected and (2) to transact other business that may come before the meeting, of which there was none.

The names of each director elected at the meeting, and the votes for and against cast for such persons are set forth below:

	Votes For	Votes Withheld	Broker Non-Votes
Leonard L. Abel	7,761,330	10,003	None
Leslie M. Alperstein	7,768,127	3,206	None
Dudley C. Dworken	7,767,282	4,051	None
Michael T. Flynn	7,763,747	7,586	None
Harvey M. Goodman	7,763,388	7,945	None
Philip N. Margolius	7,763,977	7,356	None
Ronald D. Paul	7,767,285	4,048	None
Donald R. Rogers	7,473,368	297,965	None
Leland M. Weinstein	7,767,857	3,476	None

Item 5 - Other Information None

(a) Required 8-K Disclosures None

(b) Changes in Procedures for Director Nominations None

Item 6 - Exhibits

Exhibit

No.	Description of Exhibit
3(a)	Certificate of Incorporation of the Company, as amended (1)
3(b)	Bylaws of the Company (2)
10.1	1998 Stock Option Plan (3)
10.2	Employment Agreement between Michael T. Flynn and the Company (4)
10.3	Employment Agreement between Thomas D. Murphy and the Bank (4)
10.4	Employment Agreement between Ronald D. Paul and the Company (5)
10.5	Director Fee Agreement between Leonard L. Abel and the Company (5)
10.6	Employment Agreement between Susan G. Riel and the Bank (4)
10.7	Employment Agreement between Martha F. Tonat and the Bank (4)
10.8	Employee Agreement for James H. Langmead (4)
10.9	Employee Stock Purchase Plan (6)
10.11	2006 Stock Plan (7)
11	Statement Regarding Computation of Per Share Income
21	Subsidiaries of the Registrant
31.1	Rule 13a-14(a) Certification of Ronald D. Paul
31.2	Rule 13a-14(a) Certification of James H. Langmead
31.3	Rule 13a-14(a) Certification of Susan G. Riel
31.4	Rule 13a-14(a) Certification of Michael T. Flynn
32.1	Section 1350 Certification of Ronald D. Paul
32.2	Section 1350 Certification of James H. Langmead
32.3	Section 1350 Certification of Susan G. Riel
32.4	Section 1350 Certification of Michael T. Flynn

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- (1) Incorporated by reference to the exhibit of the same number to the Company's Quarterly Report on Form 10-QSB for the period ended September 30, 2002.
- (2) Incorporated by reference to Exhibit 3(b) to the Company's Registration Statement on Form SB-2, dated December 12, 1997.
- (3) Incorporated by reference to Exhibit 10.1 to the Company's Annual Report on Form 10-KSB for the year ended December 31, 1998.
- (4) Incorporated by reference to the Company's Annual Report on Form 10-K for the year ended December 31, 2006.
- (5) Incorporated by reference to exhibits of the same number to the Company's Annual Report on Form 10-K for the year ended December 31, 2003.
- (6) Incorporated by reference to Exhibit 4 to the Company's Registration Statement on Form S-8 (No. 333-116352)
- (7) Incorporated by reference to Exhibit 4 to the Company's Registration Statement on Form S-8 (No. 333-135072)

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

EAGLE BANCORP, INC.

Date: August 8, 2007

By: /s/ Ronald D. Paul
Ronald D. Paul, President and Chief Executive Officer

Date: August 8, 2007

By: /s/ James H. Langmead
James H. Langmead, Senior Vice President and
Chief Financial Officer

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