

COOPER COMPANIES INC
Form 10-Q
June 08, 2007
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For Quarterly Period Ended April 30, 2007

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period from _____ to _____

Commission File Number 1-8597

The Cooper Companies, Inc.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

94-2657368
(I.R.S. Employer
Identification No.)

6140 Stoneridge Mall Road, Suite 590, Pleasanton, CA
(Address of principal executive offices)

94588
(Zip Code)

Registrant's telephone number, including area code (925) 460-3600

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Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant 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

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

Class	Outstanding at May 31, 2007
Common Stock, \$.10 par value	44,783,966 Shares

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Consolidated Statements of Operations

(In thousands, except for earnings per share)

(Unaudited)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2007	2006	2007	2006
Net sales	\$ 225,535	\$ 211,397	\$ 444,955	\$ 417,136
Cost of sales	99,079	80,034	188,587	156,612
Gross profit	126,456	131,363	256,368	260,524
Selling, general and administrative expense	100,934	88,600	198,457	173,046
Research and development expense	7,957	13,914	19,068	19,846
Restructuring costs	2,842	866	4,707	2,206
Amortization of intangibles	4,192	3,503	7,843	7,232
Operating income	10,531	24,480	26,293	58,194
Interest expense	10,918	7,787	20,710	20,300
Other income (expense), net	9	(1,100)	828	(2,178)
(Loss) income before income taxes	(378)	15,593	6,411	35,716
Provision for income taxes	149	1,892	1,590	4,061
Net (loss) income	(527)	13,701	4,821	31,655
Add interest charge applicable to convertible debt, net of tax		523		1,045
(Loss) income for calculating diluted earnings per share	\$ (527)	\$ 14,224	\$ 4,821	\$ 32,700
Earnings per share:				
Basic	\$ (0.01)	\$ 0.31	\$ 0.11	\$ 0.71
Diluted	\$ (0.01)	\$ 0.30	\$ 0.11	\$ 0.69
Number of shares used to compute earnings per share:				
Basic	44,645	44,520	44,606	44,508
Diluted	44,645	47,577	45,012	47,606

See accompanying notes.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Consolidated Balance Sheets

(In thousands)

(Unaudited)

	April 30, 2007	October 31, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 12,033	\$ 8,224
Trade accounts receivable, net of allowance for doubtful accounts of \$5,512 at April 30, 2007 and \$5,523 at October 31, 2006	156,772	146,584
Inventories, net	261,612	236,512
Deferred tax assets	18,703	19,659
Prepaid expense and other current assets	49,423	45,972
Total current assets	498,543	456,951
Property, plant and equipment, at cost	717,717	637,428
Less: accumulated depreciation and amortization	161,614	141,071
	556,103	496,357
Goodwill	1,260,489	1,217,084
Other intangibles, net	147,493	147,160
Deferred tax assets	23,412	21,479
Other assets	23,709	13,570
	\$2,509,749	\$ 2,352,601
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Short-term debt	\$ 48,417	\$ 23,516
Current portion of long-term debt		37,850
Accounts payable	52,434	66,080
Employee compensation and benefits	28,567	29,755
Accrued acquisition costs	24,530	36,901
Accrued income taxes	33,457	28,534
Other current liabilities	69,180	53,994
Total current liabilities	256,585	276,630
Long-term debt	817,446	681,286
Deferred tax liability	11,681	9,494
Accrued pension liability and other	6,297	6,682
Total liabilities	1,092,009	974,092
Commitments and Contingencies (see Note 13)		

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Stockholders' equity:

Preferred stock, 10 cents par value, shares authorized: 1,000; zero shares issued or outstanding		
Common stock, 10 cents par value, shares authorized: 70,000; issued 45,111 at April 30, 2007 and 44,966 at October 31, 2006	4,511	4,497
Additional paid-in capital	1,009,880	993,713
Accumulated other comprehensive income	57,759	38,711
Retained earnings	351,484	348,000
Treasury stock at cost: 384 shares at April 30, 2007 and 418 shares at October 31, 2006	(5,894)	(6,412)
Stockholders' equity	1,417,740	1,378,509
	\$ 2,509,749	\$ 2,352,601

See accompanying notes.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Consolidated Condensed Statements of Cash Flows

(In thousands)

(Unaudited)

	Six Months Ended April 30,	
	2007	2006
Cash flows from operating activities:		
Net income	\$ 4,821	\$ 31,655
Depreciation and amortization	32,939	29,273
Decrease in operating capital	(8,511)	(17,843)
Other non-cash items	19,185	33,279
Net cash provided by operating activities	48,434	76,364
Cash flows from investing activities:		
Purchases of property, plant and equipment	(90,090)	(83,479)
Acquisitions of businesses, net of cash acquired	(68,793)	(61,235)
Net cash used in investing activities	(158,883)	(144,714)
Cash flows from financing activities:		
Net proceeds (repayments) of short-term debt	22,721	11,772
Repayments of long-term debt	(839,964)	(622,700)
Proceeds from long-term debt	938,200	662,750
Debt acquisition costs	(11,226)	(625)
Dividends on common stock	(1,337)	(1,335)
Excess tax benefit from share-based compensation Arrangements	176	1,510
Proceeds from exercise of stock options	5,313	2,500
Net cash provided by financing activities	113,883	53,872
Effect of exchange rate changes on cash and cash equivalents	375	207
Net increase (decrease) in cash and cash equivalents	3,809	(14,271)
Cash and cash equivalents beginning of period	8,224	30,826
Cash and cash equivalents end of period	\$ 12,033	\$ 16,555

See accompanying notes.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Consolidated Statements of Comprehensive Income

(In thousands)

(Unaudited)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2007	2006	2007	2006
Net (loss) income	\$ (527)	\$ 13,701	\$ 4,821	\$ 31,655
Other comprehensive income:				
Foreign currency translation adjustment	10,675	9,472	19,875	12,353
Change in value of derivative instruments, net of tax	(3,347)	1,113	(827)	1,101
Minimum pension liability adjustment, net of tax				197
Other comprehensive income	7,328	10,585	19,048	13,651
Comprehensive income	\$ 6,801	\$ 24,286	\$ 23,869	\$ 45,306

See accompanying notes.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements

(Unaudited)

Note 1. General

The Cooper Companies, Inc. (Cooper or the Company) markets, develops and manufactures healthcare products through its two business units:

CooperVision (CVI) markets, develops and manufactures a broad range of contact lenses for the worldwide vision care market. Its leading products are disposable and planned replacement lenses.

CooperSurgical (CSI) markets, develops and manufactures medical devices, diagnostic products and surgical instruments and accessories used primarily by gynecologists and obstetricians.

During interim periods, we follow the accounting policies described in our Annual Report on Form 10-K for the fiscal year ended October 31, 2006. Please refer to this when reviewing this Quarterly Report on Form 10-Q. Certain prior period amounts have been reclassified to conform to the current period's presentation. Readers should not assume that the results reported here either indicate or guarantee future performance.

The unaudited consolidated condensed financial statements presented in this report contain all adjustments necessary to present fairly Cooper's consolidated financial position at April 30, 2007 and October 31, 2006, the consolidated results of its operations for the three and six months ended April 30, 2007 and 2006 and its cash flows for the six months ended April 30, 2007 and 2006. Most of these adjustments are normal and recurring. However, certain adjustments associated with recent acquisitions and the related financial arrangements are of a nonrecurring nature.

We use derivatives to reduce market risks associated with changes in foreign exchange and interest rates. We do not use derivatives for trading or speculative purposes. We believe that the counterparties with which we enter into forward exchange contracts and interest rate swap agreements are financially sound and that the credit risk of these contracts is negligible.

Estimates and Critical Accounting Policies

Management estimates and judgments are an integral part of financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP). We believe that the critical accounting policies described in this section address the more significant estimates required of management when preparing our consolidated financial statements in accordance with GAAP. We consider an accounting estimate critical if changes in the estimate may have a material impact on our financial condition or results of operations. We believe that the accounting estimates employed are appropriate and resulting balances are reasonable; however, actual results could differ from the original estimates, requiring adjustment to these balances in future periods.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

Revenue recognition We recognize revenue when it is realized or realizable and earned, based on terms of sale with the customer, where persuasive evidence of an agreement exists, delivery has occurred, the seller's price is fixed and determinable and collectibility is reasonably assured. For contact lenses as well as CSI medical devices, diagnostic products and surgical instruments and accessories, this primarily occurs upon product shipment, when risk of ownership transfers to our customers. We believe our revenue recognition policies are appropriate in all circumstances and that our policies are reflective of our customer arrangements. We record, based on historical statistics, estimated reductions to revenue for customer incentive programs offered including cash discounts, promotional and advertising allowances, volume discounts, contractual pricing allowances, rebates and specifically established customer product return programs. While estimates are involved, historically, most of these programs have not been major factors in our business since a high percentage of our revenue is from direct sales to doctors.

Allowance for doubtful accounts Our reported balance of accounts receivable, net of the allowance for doubtful accounts, represents our estimate of the amount that ultimately will be realized in cash. We review the adequacy of our allowance for doubtful accounts on an ongoing basis, using historical payment trends and the age of the receivables and knowledge of our individual customers. When our analyses indicate, we increase or decrease our allowance accordingly. However, if the financial condition of our customers were to deteriorate, additional allowances may be required. While estimates are involved, bad debts historically have not been a significant factor given the diversity of our customer base, well established historical payment patterns and the fact that patients require satisfaction of healthcare needs in both strong and weak economies.

Net realizable value of inventory In assessing the value of inventories, we must make estimates and judgments regarding aging of inventories and other relevant issues potentially affecting the saleable condition of products and estimated prices at which those products will sell. On an ongoing basis, we review the carrying value of our inventory, measuring number of months on hand and other indications of salability, and reduce the value of inventory if there are indications that the carrying value is greater than market. At the point of the loss recognition, a new, lower-cost basis for that inventory is established, and subsequent changes in facts and circumstances do not result in the restoration or increase in that newly established cost basis. While estimates are involved, historically, obsolescence has not been a significant factor due to long product dating and lengthy product life cycles. We target to keep, on average, about seven months of inventory on hand to maintain high customer service levels given the complexity of our specialty lens product portfolio.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

Valuation of goodwill We account for goodwill and evaluate our goodwill balances and test them for impairment in accordance with the provisions of Statement of Financial Accounting Standards No. 142, *Goodwill and Other Intangible Assets*, (SFAS 142). The SFAS 142 goodwill impairment test is a two-step process. Initially, we compare the book value of net assets to the fair value of each reporting unit that has goodwill assigned to it. If the fair value of a reporting unit is determined to be less than the book value, a second step is performed to compute the amount of the impairment. When available and as appropriate, we use comparative market multiples to corroborate fair value results. A reporting unit is the level of reporting at which goodwill is tested for impairment.

Our reporting units are the same as our business segments CVI and CSI reflecting the way that we manage our business. We test goodwill for impairment annually during the third fiscal quarter and when an event occurs or circumstances change such that it is reasonably possible that impairment may exist. We performed an impairment test in our third fiscal quarter 2006, and our analysis indicated that we had no impairment of goodwill. The valuation of each of our reporting units was determined using a combination of discounted cash flows, an income valuation approach and the guideline company method, a market valuation approach.

Business combinations We routinely consummate business combinations. We allocate the purchase price of acquisitions based on our estimates and judgments of the fair value of net assets purchased, acquisition costs incurred and intangibles other than goodwill. On individually significant acquisitions, we utilize independent valuation experts to provide a basis in order to refine the purchase price allocation, if appropriate. Results of operations for acquired companies are included in our consolidated results of operations from the date of acquisition.

Income taxes The Company accounts for income taxes under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and for tax losses and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized.

As part of the process of preparing our consolidated financial statements, we must estimate our income tax expense for each of the jurisdictions in which we operate. This process requires significant management judgments and involves estimating our current tax exposures in each jurisdiction including the impact, if any, of additional taxes resulting from tax examinations as well as judging the recoverability of deferred tax assets. To the extent recovery of deferred tax assets is not likely based on our estimation of future taxable income in each jurisdiction, a valuation allowance is established. Tax exposures can

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

involve complex issues and may require an extended period to resolve. Frequent changes in tax laws in each jurisdiction complicate future estimates. To determine the quarterly tax rate, we are required to estimate full-year income and the related income tax expense in each jurisdiction. We update the estimated effective tax rate for the effect of significant unusual items as they are identified. Changes in the geographic mix or estimated level of annual pre-tax income can affect the overall effective tax rate, and such changes could be material.

Share-based compensation Effective November 1, 2005, we adopted Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R) as interpreted by SEC Staff Accounting Bulletin No. 107, using the modified prospective transition method. Periods prior to adoption have not been restated. See Note 10. Stock Plans in our Annual Report on Form 10-K for the fiscal year ended October 31, 2006, for a further description of the impact of the adoption of SFAS 123R and the Company's share-based compensation plans.

Under the fair value recognition provisions of SFAS 123R, share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense over the vesting period. Determining the fair value of share-based awards at the grant date requires judgment, including estimating Cooper's stock price volatility, employee stock option exercise behaviors and employee option forfeiture rates.

The expected life of the share-based awards is based on the observed and expected time to post-vesting forfeiture and/or exercise. Groups of employees that have similar historical exercise behavior are considered separately for valuation purposes. The expected volatility is based on implied volatility from publicly-traded options, historical volatility on the Company's stock at the date of grant, historical implied volatility of the Company's publicly-traded options and other factors. The risk-free interest rate is based on the continuous rates provided by the U.S. Treasury with a term equal to the expected life of the award. The dividend yield is based on the projected annual dividend payment per share, divided by the stock price at the date of grant.

As share-based compensation expense recognized in the Consolidated Statement of Operations is based on awards ultimately expected to vest, the amount of expense has been reduced for estimated forfeitures. SFAS 123R requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. Forfeitures are estimated based on historical experience.

If factors change and the Company employs different assumptions in the application of SFAS 123R, the compensation expense that it records in future periods may differ significantly from what it has recorded in the current period.

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Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

New Accounting Pronouncements

In September 2006, the SEC staff issued Staff Accounting Bulletin (SAB) No. 108, *Considering the Effects of Prior Year Misstatements when Quantifying Misstatements in Current Year Financial Statements* (SAB 108). In SAB 108, the SEC staff established an approach that requires quantification of financial statement misstatements based on the effects of the misstatements on each of the Company's financial statements and the related financial statement disclosures. SAB 108 permits public companies to initially apply its provisions either by (i) restating prior financial statements or (ii) recording the cumulative effect as adjustments to the carrying values of assets and liabilities with an offsetting adjustment recorded to the opening balance of retained earnings. The Company is required to adopt SAB 108 by the end of fiscal 2007. The Company has not completed its analysis but does not expect adoption to have a significant impact on the Company's results of operations or financial condition.

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 157, *Fair Value Measurements* (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles and expands disclosures about fair value measurements. This statement is effective for financial statements issued for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact SFAS 157 will have on its consolidated financial statements.

In September 2006, the FASB issued SFAS No. 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106 and 132(R)* (SFAS 158). SFAS 158 requires an employer to recognize the overfunded or underfunded status of a defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in that funded status in the year in which the changes occur through comprehensive income. SFAS 158 also requires an employer to measure the funded status of a plan as of the date of its year-end statement of financial position, with limited exceptions. This statement is effective for financial statements as of the end of fiscal years ending after December 15, 2006. The Company is currently evaluating the impact SFAS 158 will have on its consolidated financial statements.

In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48). FIN 48 applies to all tax positions related to income taxes subject to Statement SFAS No. 109, *Accounting for Income Taxes* (SFAS 109). Under FIN 48, a company would recognize the benefit from a tax position only if it is more-likely-than-not that the position would be sustained upon audit based solely on the technical merits of the tax position. FIN 48 clarifies how a company would measure the income tax benefits from the tax positions that are recognized, provides guidance as to the timing of the derecognition of previously recognized tax benefits and describes the methods for classifying and disclosing the liabilities within the financial statements for any unrecognized tax benefits. FIN 48 also addresses when a company should record interest and penalties related to tax positions and how the interest and penalties may be classified within the income statement and presented in the balance sheet. FIN 48 is effective for fiscal years beginning after December 15, 2006. For the Company, FIN 48 will be

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

effective for our 2008 fiscal year. Differences between the amounts recognized prior to and after the adoption of FIN 48 would be accounted for as a cumulative effect adjustment to the beginning balance of retained earnings. The Company is currently evaluating FIN 48 and its possible impacts on the Company's financial statements. Upon adoption, there is a possibility that the cumulative effect would result in a charge or benefit to the beginning balance of retained earnings, increases or decreases in future effective tax rates, and/or increases in future effective tax rate volatility.

In February 2007, FASB Issued SFAS No. 159, *Establishing the Fair Value Option for Financial Assets and Liabilities* (SFAS 159). The Financial Accounting Standards Board has issued SFAS 159 to permit all entities to choose to elect, at specified election dates, to measure eligible financial instruments at fair value. An entity shall report unrealized gains and losses on items for which the fair value option has been elected in earnings at each subsequent reporting date, and recognize upfront costs and fees related to those items in earnings as incurred and not deferred. SFAS 159 applies to fiscal years beginning after November 15, 2007, or our 2009 fiscal year, with early adoption permitted for an entity that has also elected to apply the provisions of SFAS 157, *Fair Value Measurements*. An entity is prohibited from retrospectively applying SFAS 159, unless it chooses early adoption. SFAS 159 also applies to eligible items existing at November 15, 2007 (or early adoption date). The Company has not completed its analysis but does not expect the adoption of SFAS 159 to have a material effect on the Company's financial condition.

Note 2. Acquisitions

Acquisition of Wallach Surgical Devices, Inc. (Wallach): On February 22, 2007, CSI acquired all of the outstanding shares of Wallach. Wallach's products consist of various diagnostic and therapeutic medical instruments primarily for in-office use in women's healthcare and other specialty instruments relating to dermatology, ophthalmology, anesthesiology, dentistry and veterinary medicine. We are in the process of obtaining a third-party valuation of the business using income approach valuation methodology. Research and development assets, if any, with no alternative future use will be written off to research and development in our consolidated statement of operations once determined.

We paid \$20.0 million in cash for Wallach and have initially ascribed \$16.7 million to goodwill, \$0.5 million to working capital (including acquisition costs of \$2.1 million), \$4.7 million to other intangible assets, \$0.3 million to property, plant and equipment and \$2.6 million to deferred tax liability. The allocation of the purchase price is subject to refinement as we are currently obtaining a third-party valuation of the business, using income approach valuation methodology. Subsequent adjustments could be material. Research and development assets, if any, with no alternative future use will be written off to research and development in our consolidated statement of operations once determined.

Lone Star Medical Products, Inc. (Lone Star): On November 2, 2006, Cooper acquired all of the outstanding shares of Lone Star, a manufacturer of medical devices that improve the management of the surgical site, most notably the *Lone Star Retractor System*, which places a retraction ring around the surgical incision providing greater exposure of the surgical field.

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Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

We estimate that the total restructuring costs under this integration plan, exclusive of accrued acquisition related costs, will be approximately \$45 - \$50 million, of which approximately \$25 - \$30 million is cash related, and will be reported as cost of sales or restructuring costs in our Consolidated Statements of Operations. The following table summarizes the restructuring costs incurred under this integration plan through April 30, 2007.

	Plant Shutdown	Severance	Asset Impairments (In millions)	Other	Total
Restructuring costs incurred:					
Through October 31, 2006	\$ 2.6	\$ 4.4	\$ 3.4	\$ 9.4	\$ 19.8
For the six-month period ended April 30, 2007	1.4	2.6	6.2	3.0	13.2
	\$ 4.0	\$ 7.0	\$ 9.6	\$ 12.4	\$ 33.0

Restructuring costs reported in our Consolidated Statements of Operations also include costs related to less significant restructuring activities within our consolidated organization.

Note 4. Inventories, Net

	April 30, 2007	October 31, 2006
	(In thousands)	
Raw materials	\$ 35,648	\$ 31,368
Work-in-process	16,617	19,774
Finished goods	209,347	185,370
	\$261,612	\$ 236,512

Inventories are stated at the lower of average cost or market. Cost is computed using standard cost that approximates actual cost, on a first-in, first-out basis.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

Note 5. Intangible Assets**Goodwill**

	CVI	CSI (In thousands)	Total
Balance as of November 1, 2005	\$ 1,047,538	\$ 121,511	\$ 1,169,049
Net (reductions) additions during the year ended October 31, 2006	(2,339)	48,204	45,865
Other adjustments*	2,170		2,170
Balance as of October 31, 2006	\$ 1,047,369	\$ 169,715	\$ 1,217,084
Net (reductions) additions during the six-month period ended April 30, 2007	(1,188)	41,617	40,429
Other adjustments*	2,976		2,976
Balance as of April 30, 2007	\$ 1,049,157	\$ 211,332	\$ 1,260,489

* Primarily translation differences in goodwill denominated in foreign currency.

Other Intangible Assets

	As of April 30, 2007		As of October 31, 2006	
	Gross Carrying Amount	Accumulated Amortization & Translation	Gross Carrying Amount	Accumulated Amortization & Translation
	(In thousands)			
Trademarks	\$ 2,907	\$ 350	\$ 1,807	\$ 231
Technology	89,482	23,793	88,950	19,739
Shelf space and market share	79,986	12,148	73,486	9,007
License and distribution rights and other	17,142	5,733	17,070	5,176
	189,517	\$ 42,024	181,313	\$ 34,153
Less accumulated amortization and translation	42,024		34,153	
Other intangible assets, net	\$ 147,493		\$ 147,160	

We estimate that amortization expense will be about \$15.4 million per year in the five-year period ending October 31, 2011.

During the first fiscal quarter of 2007, payments of \$4.2 million related to a license agreement to distribute gynecological medical devices were written-off as acquired in-process research and development, as the products are pending Food and Drug Administration approval.

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

Note 6. Debt

	April 30, 2007	October 31, 2006
	(In thousands)	
Short-term:		
Overdraft and other credit facilities	\$ 48,417	\$ 23,516
Current portion of long-term debt		37,850
	\$ 48,417	\$ 61,366
Long-term:		
Convertible senior debentures, net of discount of 2,324 and 2,396	\$ 112,676	\$ 112,604
Revolver	354,400	605,300
Senior Notes	350,000	
Other	370	1,232
	817,446	719,136
Less current portion		37,850
	\$ 817,446	\$ 681,286

Credit Facility: On January 31, 2007, Cooper refinanced its existing \$750 million syndicated bank credit facility, which consisted of a \$250 million term loan and a \$500 million revolving credit facility, with a new \$650 million syndicated Senior Unsecured Revolving Line of Credit (Revolver) and \$350 million aggregate principal amount of 7.125% of Senior Notes, described below. The refinancing extended the maturity and provided additional borrowing flexibility along with lower overall pricing relative to the prior agreement. In addition, the Company has the ability from time to time to increase the size of the Revolver by up to an additional \$250 million. KeyBank led the Revolver refinancing, which resulted in a number of the banks retaining or increasing their participation in the agreement. The Revolver matures on January 31, 2012.

Interest rates for the Revolver are based on the London Interbank Offered Rate (LIBOR) plus additional basis points determined by certain ratios of debt to pro forma earnings before interest, taxes, depreciation and amortization (EBITDA), as defined in the credit agreement. These range from 75 to 150 basis points. As of April 30, 2007, the additional basis points were 125.

The Revolver:

Requires that the ratio of Consolidated Pro Forma EBITDA to Consolidated Interest Expense (as defined, Interest Coverage Ratio) be at least 3.0 to 1.0 at all times.

Requires that the ratio of Consolidated Funded Indebtedness to Consolidated Pro Forma EBITDA (as defined, Total Leverage Ratio) be no higher than 4.00 to 1.00 from January 31, 2007 through October 31, 2009, and 3.75 to 1.00 thereafter.

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At April 30, 2007, the Company's Interest Coverage Ratio was 6.33 to 1.00 and the Total Leverage Ratio was 3.63 to 1.00.

The Company wrote off about \$0.9 million of debt issuance costs in interest expense as a result of extinguishing the term loan. The remaining \$1.7 million of existing debt issuance costs and the \$10.4 million of costs incurred to refinance the Revolver and Notes are carried in other assets and amortized to interest expense over the life of the credit facility.

At April 30, 2007, we had \$295.4 million available under the Revolver:

(In millions)	
Amount of Revolver	\$ 650.0
Outstanding loans	(354.6)*
Available	\$ 295.4

* Includes \$0.2 million in letters of credit

Senior Notes: On January 31, 2007, the Company issued \$350 million aggregate principal amount of 7.125% Senior Notes (the Notes) due February 15, 2015. The Notes were offered in a private placement to qualified institutional buyers pursuant to Rule 144A under the Securities Act of 1933. The Notes pay interest semi-annually on February 15 and August 15 of each year, beginning August 15, 2007. We may redeem some or all of the Notes at any time prior to February 15, 2011, at a price equal to 100% of the principal amount of the Notes redeemed plus accrued and unpaid interest to the redemption date and a make-whole premium. We may redeem some or all of the Notes at any time on or after February 15, 2011, at the redemption prices (expressed as percentages of principal amounts) set forth below, plus accrued and unpaid interest to the redemption date and additional interest (if we fail to comply with certain obligations under the registration rights agreement that we entered in connection with the Notes (Additional Interest)), if any, on the Notes redeemed to the applicable redemption date, if redeemed during the twelve-month period beginning on February 15 of the years indicated below:

Year	Percent
2011	103.56%
2012	101.78%
2013 and thereafter	100.00%

In addition, prior to February 15, 2010, we may redeem up to 35% of the Notes at a price equal to 107.13% of the principal amount of the Notes redeemed plus accrued and unpaid interest to the redemption date and Additional Interest, if any, on the Notes redeemed to the applicable redemption date, from the proceeds of certain equity offerings.

Net proceeds from the issuance totaled approximately \$342.6 million.

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Under the indenture governing the Notes, our ability to incur indebtedness and pay distributions is subject to restrictions and the satisfaction of various conditions. In addition, the indenture imposes restrictions on certain other customary matters, such as limitations on certain investments, transactions with affiliates, the incurrence of liens, sale and leaseback transactions, certain asset sales and mergers.

The Notes are our senior unsecured obligations and rank equally with all of our existing and future senior unsecured obligations and senior to our subordinated indebtedness. The Notes are effectively subordinated to our existing and future secured indebtedness to the extent of the assets securing that indebtedness. On the issue date, certain of our direct and indirect subsidiaries entered into unconditional guarantees of the Notes that are unsecured. These guarantees rank equally with all existing and future unsecured senior obligations of the guarantors and are effectively subordinated to existing and future secured debt of the guarantors to the extent of the assets securing that indebtedness. The Notes are structurally subordinated to indebtedness and other liabilities, including payables, of our non-guarantor subsidiaries.

Canadian Credit Facility: On April 30, 2007, the Company entered into a \$10 million Canadian dollar credit facility supported by a continuing and unconditional guaranty. Interest expense is calculated on outstanding balances based on an applicable base rate plus a fixed spread. At April 30, 2007, \$7.3 million of the facility was utilized. The weighted average interest rate on the outstanding balances at April 30, 2007, was 6.5%.

European Credit Facilities: On November 1, 2006, the Company entered into a \$45 million European credit facility supported by a continuing and unconditional guaranty, which replaced our previous European overdraft facility. The Company will pay all forms of indebtedness in the currency in which it is denominated for those certain subsidiaries. Interest expense is calculated on all outstanding balances based on an applicable base rate for each country plus a fixed spread common across all subsidiaries covered under the guaranty. At April 30, 2007, \$20.7 million of the facility was utilized. The weighted average interest rate on the outstanding balances was 4.77%.

In addition to the \$45 million European Credit Facilities, the Company has two non-guaranteed Italian overdraft facilities totaling approximately \$7 million. At April 30, 2007, these facilities were not utilized.

Asian Pacific Credit Facilities: On February 22, 2006, the Company entered into a \$15 million Yen-denominated credit facility in Japan supported by a continuing and unconditional guaranty. The Company will pay to the bank all forms of indebtedness in Yen upon demand by the bank. Interest expense is calculated on the outstanding balance based on the EuroYen rate plus a fixed spread. At April 30, 2007, \$14.0 million of the facility was utilized. The weighted average interest rate on the outstanding balances was 1.32%.

During the three months ended April 30, 2007, the Company entered into an additional \$13 million overdraft facility that included Japan and certain of our Asian Pacific subsidiaries.

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This overdraft facility is supported by a continuing and unconditional guaranty. The Company will pay all forms of indebtedness in the currency in which it is denominated for those certain subsidiaries. Interest expense is calculated on all outstanding balances based on an applicable base rate for each country plus a fixed spread common across all subsidiaries covered under the guaranty. At April 30, 2007, \$5.2 million of the facility was utilized. The interest rate on the outstanding balances was 1.32%.

Note 7. Derivative Instruments

We operate multiple foreign subsidiaries that manufacture and/or sell our products worldwide. As a result, our earnings, cash flows and financial position are exposed to foreign currency risk from foreign currency denominated receivables and payables, sales transactions, capital expenditures and net investment in certain foreign operations. Our policy is to minimize transaction, remeasurement and specified economic exposures with derivative instruments including forward contracts. The gains and losses on foreign exchange forward contracts are intended to at least partially offset the transaction gains and losses recognized in earnings. We do not enter into foreign exchange forward contracts for trading or speculative purposes. Under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities* (SFAS 133), all derivatives are recorded on the balance sheet at fair value. Changes in the fair value of derivatives that do not qualify, or are not effective as cash flow hedges, must be recognized currently in earnings.

Cash Flow Hedging

In November 2006, the Company entered into approximately \$400 million of foreign currency forward contracts with maturities of up to thirteen months to reduce foreign currency fluctuations related to forecasted foreign currency denominated purchases and sales of product. The derivatives are accounted for as cash flow hedges under SFAS 133 and are expected to be effective through their maturities.

Interest Rate Swaps

Effectiveness testing of the hedge relationship and measurement to quantify ineffectiveness is performed at the end of each fiscal quarter using the hypothetical derivative method. The interest rate swaps have been and are expected to remain highly effective for the life of the hedges. The fixed rates on the outstanding swaps are between 3.98% and 4.02%. As of April 30, 2007, the fair value of the outstanding swaps, approximately \$2.4 million, was recorded as an asset and the effective offset is recorded in other comprehensive income (OCI) in our Consolidated Balance Sheet.

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On January 31, 2007, Cooper refinanced its existing \$750 million syndicated bank credit facility, with a \$650 million syndicated Senior Unsecured Revolving Line of Credit (Revolver) and \$350 million aggregate principal amount of 7.125% Senior Notes. As part of this new debt structure, the Company terminated an interest rate swap with a notional value of \$125 million on January 30, 2007. This interest rate swap was set to mature on February 7, 2009, and the Company settled it and received \$1.1 million from the counterparty. As a result of the termination of the interest rate swap, the Company realized a gain of approximately \$1 million. The Company will amortize this gain from OCI to interest expense over the original life of the interest rate swap. During the six months ended April 30, 2007, approximately \$200,000 of effective gains were amortized from OCI to interest expense. Effective amounts are amortized to interest expense as the related hedged expense is incurred. As of April 30, 2007, we estimated that approximately \$0.5 million will be amortized during fiscal year 2007. During the six months ended April 30, 2007, approximately \$0.2 million of ineffective gains were reclassified from OCI to interest expense.

On May 3, 2007, Cooper terminated two \$125 million floating-to-fixed interest rate swaps that were set to mature on February 7, 2008. The Company received a total of \$3.2 million from the counterparties as a result of these swap terminations and used the proceeds to reduce our outstanding debt. The Company realized a gain of approximately \$2.4 million that will be amortized from OCI to interest expense over the original life of the interest rate swaps. Effective amounts are amortized to interest expense as the related hedged expense is incurred. As of April 30, 2007, we estimated that approximately \$1.7 million will be amortized during fiscal year 2007.

Concurrent with these interest rate swap terminations, the Company reset its fixed rate debt structure under the Revolver to extend maturities by entering into four new interest rate swaps on May 3, 2007. These new interest rate swaps, totaling \$250 million, serve to fix the floating rate debt under the Revolver for terms between 30 and 48 months with fixed rates between 4.94% to 4.96%.

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Note 8. Earnings Per Share (EPS)

	Three Months Ended April 30,		Six Months Ended April 30,	
	2007	2006	2007	2006
	(In thousands, except for per share amounts)			
Net (loss) income	\$ (527)	\$ 13,701	\$ 4,821	\$ 31,655
Add interest charge applicable to convertible debt, net of tax		523		1,045
(Loss) income for calculating diluted earnings per share	\$ (527)	\$ 14,224	\$ 4,821	\$ 32,700
Basic:				
Weighted average common shares	44,645	44,520	44,606	44,508
Basic (loss) earnings per common share	\$ (0.01)	\$ 0.31	\$ 0.11	\$ 0.71
Diluted:				
Weighted average common shares	44,645	44,520	44,606	44,508
Effect of dilutive stock options		467	406	508
Shares applicable to convertible debt		2,590		2,590
Diluted weighted average common shares	44,645	47,577	45,012	47,606
Diluted (loss) earnings per common share	\$ (0.01)	\$ 0.30	\$ 0.11	\$ 0.69

The following table sets forth stock options to purchase Cooper's common stock and common shares applicable to convertible debt that are not included in the diluted net loss per share calculation because to do so would be anti-dilutive for the periods presented:

	Three Months Ended		Six Months Ended	
	April 30,		April 30,	
	2007	2006	2007	2006
Stock options to purchase common stock	4,901,535	2,129,133	3,187,783	2,129,133
Exercise prices	\$ 15.35-\$80.51	\$ 55.33-\$80.51	\$ 52.40-\$80.51	\$ 55.33-\$80.51
Number of common shares applicable to convertible debt	2,590,090		2,590,090	

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Note 9. Share-Based Compensation Plans

The Company has two share-based compensation plans, which include stock options and restricted stock awards. The 2007 Long-Term Incentive Plan, as amended (2007 LTIP) and the 2006 Long-Term Incentive Plan for Non-Employee Directors (2006 Directors Plan) are the only plans with stock awards currently available for grant as of April 30, 2007. The 2007 LTIP has replaced the Second Amended and Restated 2001 Long-Term Incentive Plan (2001 LTIP), which expired in December 2006 by its terms. The 2006 Directors Plan has replaced the 1996 Long-Term Incentive Plan for Non-Employee Directors (1996 Directors Plan), which expired in November 2005 by its terms.

Share-Based Compensation

Compensation cost associated with share-based awards recognized in fiscal 2007 and fiscal 2006 includes: 1) amortization related to the remaining unvested portion of all stock option awards granted prior to November 1, 2005, based on the grant date fair value estimated in accordance with the original provisions of SFAS 123 and 2) amortization related to all stock option awards granted on or subsequent to November 1, 2005, based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. The compensation and related income tax benefit recognized in the Company's consolidated financial statements for stock options and restricted stock awards were as follows:

	Three Months Ended		Six Months Ended	
	April 30,		April 30,	
	2007	2006	2007	2006
	(In millions)			
Selling, general and administrative expenses	\$ 2.7	\$ 3.1	\$ 9.4	\$ 7.9
Cost of products sold	0.3	0.1	0.6	0.1
Research and development expense	0.2	0.1	0.4	0.2
Restructuring costs	0.8		0.8	
Capitalized in inventory	0.5	0.3	1.0	0.6
Total compensation expense	\$ 4.5	\$ 3.6	\$ 12.2	\$ 8.8
Related income tax benefit	\$ 1.0	\$ 0.7	\$ 3.1	\$ 2.1

Cash received from options exercised under all share-based payment arrangements for the three and six months ended April 30, 2007, was \$3.8 million and \$5.3 million, respectively. Cash received from options exercised under all share-based payment arrangements for the three and six months ended April 30, 2006, was \$0.4 million and \$2.5 million, respectively.

Details regarding the valuation and accounting for stock options follow.

The fair value of each share-based award granted after the adoption of SFAS 123R is estimated on the date of grant using the Black-Scholes option valuation model and fair value assumptions. The expected life of the awards is based on the observed and expected time to post-vesting forfeiture and/or exercise. Groups of employees that have similar historical

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exercise behavior are considered separately for valuation purposes. The expected volatility is based on implied volatility from publicly-traded options on the Company's stock at the date of grant, historical implied volatility of the Company's publicly-traded options, historical volatility and other factors. The risk-free interest rate is based on the continuous rates provided by the U.S. Treasury with a term equal to the expected life of the option. The dividend yield is based on the projected annual dividend payment per share, divided by the stock price at the date of grant.

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The fair value of each option award granted during the three and six months ended April 30, 2007 and 2006 was estimated on the date of grant using the Black-Scholes option valuation model and weighted-average assumptions in the following table.

	Three Months Ended		Six Months Ended	
	April 30,		April 30,	
	2007	2006	2007	2006
Expected life	2.71 to 2.8 years	4.42 to 5.16 yrs.	2.8 to 5.16 yrs.	3.56 to 5.16 yrs.
Expected volatility	29.3% to 30.4%	29.5% to 30.2%	30.0% to 30.4%	29.5% to 30.8%
Risk-free interest rate	4.5% to 4.73%	4.38% to 4.52%	4.47% to 4.73%	4.37% to 4.52%
Dividend yield	0.09% to 0.117%	0.09%	0.09%	0.09%

The status of the Company's stock option plans at April 30, 2007, is summarized below:

	Number of Shares	Weighted-Average Exercise Price Per Share	Weighted-Average Remaining Contractual Term (in Years)	Aggregate Intrinsic Value
Outstanding at October 31, 2006	4,988,468	\$ 52.73		
Granted	155,400	\$ 56.92		
Exercised	(171,333)	\$ 28.50		
Forfeited or expired	(71,000)	\$ 67.32		
Outstanding at April 30, 2007	4,901,535	\$ 53.50	6.40	\$
Vested and exercisable at April 30, 2007	1,993,694	\$ 40.95	5.77	\$ 16,263,265

The weighted-average fair value of each option granted during the three and six months ended April 30, 2007, estimated as of the grant date using the Black-Scholes option pricing model, for the 2007 LTIP was \$13.79. For the 2001 LTIP and for the Directors Plans, there were no options granted during the three months ended April 30, 2007. The weighted-average fair value of each option granted during the six months ended April 30, 2007, estimated as of the grant date using the Black-Scholes option pricing model, for the 2001 LTIP and Directors Plans was \$10.61 and \$20.36, respectively. The total intrinsic value of options exercised during the three months and six months ended April 30, 2007 was \$3 million and \$3.3 million, respectively. The expected requisite service periods for options granted in both the three and six months ended April 30, 2007, for employees was 33 months. Directors' options and restricted stock grants are expensed on the date of grant as the 2006 Directors Plan does not contain a substantive future requisite service period.

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Stock awards outstanding under the Company's current plans have been granted at prices which are either equal to or above the market value of the stock on the date of grant. Options granted under the 2007 LTIP and the 2001 LTIP generally vest over three and one-half to five years based on market and service conditions and expire no later than ten years after the grant date. Options granted under the 2006 Directors Plan and the 1996 Directors Plan generally vest in five years or upon achievement of a market condition and expire no later than ten years after the grant date. Effective November 1, 2005, the Company generally recognizes compensation expense ratably over the vesting period. As of April 30, 2007, there was \$34.3 million of total unrecognized compensation cost related to nonvested options, which is expected to be recognized over a remaining weighted-average vesting period of 3.02 years.

Note 10. Income Taxes

Cooper's effective tax rate (ETR) (provision for income taxes divided by pretax income) for the first half of fiscal 2007 was 24.81 percent. Accounting principles generally accepted in the United States of America (GAAP) require that the projected fiscal year ETR be included in the year-to-date results. The ETR used to record the provision for income taxes for the six-month period ended April 30, 2006, was 11.37 percent. The increase in the 2007 ETR reflects certain expenses associated with the Ocular integration plan impacting jurisdictions with lower tax rates.

Note 11. Employee Benefits

Cooper's Retirement Income Plan (Plan) covers substantially all full-time United States employees. Cooper's contributions are designed to fund normal cost on a current basis and to fund over 30 years the estimated prior service cost of benefit improvements (5 years for annual gains and losses). The unit credit actuarial cost method is used to determine the annual cost. Cooper pays the entire cost of the Plan and funds such costs as they accrue. Virtually all of the assets of the Plan are comprised of equity and fixed income funds.

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Cooper's results of operations for the three and six months ended April 30, 2007 and 2006 reflect the following pension costs.

	Three Months Ended		Six Months Ended	
	April 30,		April 30,	
	2007	2006	2007	2006
	(In thousands)			
Components of net periodic pension cost:				
Service cost	\$ 714	\$ 761	\$ 1,429	\$ 1,501
Interest cost	453	398	906	786
Expected returns on assets	(458)	(420)	(916)	(841)
Amortization of prior service cost	8	8	15	14
Amortization of transition obligation	7	6	13	14
Recognized net actuarial loss	42	109	85	225
Net periodic pension cost	\$ 766	\$ 862	\$ 1,532	\$ 1,699

No pension contributions were made during either period.

Note 12. Cash Dividends

We paid a semiannual dividend of approximately \$1.3 million or 3 cents per share on January 5, 2007, to stockholders of record on December 15, 2006.

On May 11, 2007, we announced that the Company declared a semiannual dividend of 3 cents per share payable on July 5, 2007, to stockholders of record on June 13, 2007.

Note 13. Contingencies**Legal Proceedings**

The Company is from time to time involved in various litigation and legal matters arising in the normal course of its business operations. By describing any particular matter, the Company does not intend to imply that it or its legal advisors have concluded or believe that the outcome of any of those particular matters is or is not likely to have a material adverse impact upon the Company's consolidated financial position, cash flows or results of operations.

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On February 15, 2006, Alvin L. Levine filed a putative securities class action lawsuit in the United States District Court for the Central District of California, Case No. SACV-06-169 CJC, against the Company, A. Thomas Bender, its Chairman of the Board, President and Chief Executive Officer and a director, Robert S. Weiss, its Executive Vice President, Chief Operating Officer and a director, and John D. Fruth, a director. Two similar putative class action lawsuits were also filed in the United States District Court for the Central District of California, Case Nos. SACV-06-306 CJC and SACV-06-331 CJC. On May 19, 2006, the Court consolidated all three actions under the heading In re Cooper Companies, Inc. Securities Litigation and selected a lead plaintiff and lead counsel pursuant to the provisions of the Private Securities Litigation Reform Act of 1995, 15 U.S.C. § 78u-4.

The lead plaintiff filed a consolidated complaint on July 31, 2006. The consolidated complaint was filed on behalf of all purchasers of the Company's securities between July 28, 2004, and December 12, 2005, including persons who received Company securities in exchange for their shares of Ocular in the January 2005 merger pursuant to which the Company acquired Ocular. In addition to the Company, Messrs. Bender, Weiss, and Fruth, the consolidated complaint names as defendants several of the Company's other current officers and directors and one former officer.

The consolidated complaint purports to allege violations of Sections 10(b) and 20(a) of the Securities and Exchange Act of 1934 by, among other things, contending that: (a) the Company improperly accounted for assets acquired in the Ocular merger by improperly allocating \$100 million of acquired customer relationships and manufacturing technology to goodwill (which is not amortized against earnings) instead of to intangible assets other than goodwill (which are amortized against earnings); (b) the Company's earnings guidance reflected the improper accounting for intangible assets and was inflated by (among other things) the amount of the understated amortization expense; (c) contrary to certain alleged statements, Ocular had flooded the trade channel with its older products as its Premier lenses were not being well received by customers; (d) the Company's aggressive revenue and growth targets for 2005 and beyond lacked any reasonable basis when made and did not reflect realistically achievable results primarily because of the absence of a two-week silicone hydrogel product; (e) the Company's internal controls were inadequate making it possible to misstate earnings by improperly accounting for the merger with Ocular and (f) sales force integration was not materializing and was fraught with dissension and acrimony.

On September 29, 2006, the Company and the individual defendants moved to dismiss the consolidated complaint. A hearing on the motion is currently scheduled for July 16, 2007. The Company intends to vigorously defend this matter.

On March 17, 2006, Eben Brice filed a purported shareholder derivative complaint in the United States District Court for the Central District of California, Case No. 8:06-CV-00300-CJC-RNB, against several current and former officers and directors of the Company. The Company is named as a nominal defendant. Following the filing of the first purported shareholder derivative lawsuit, three similar purported shareholder derivative suits were filed in the United States District Court for the Central District of California. All four actions have been consolidated under the heading In re Cooper Companies, Inc. Derivative Litigation, and the Court selected a lead plaintiff and lead counsel.

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On September 11, 2006, plaintiffs filed a consolidated amended complaint. The complaint purports to allege causes of action for breach of fiduciary duty, insider trading, breach of contract, and unjust enrichment, and largely repeats the allegations in the class action securities case, described above. The Company and the individual defendants have yet to respond to the consolidated amended complaint.

In addition to the derivative action pending in federal court, three similar purported shareholder actions were filed in the Superior Court for the State of California for the County of Alameda. These actions have been consolidated under the heading *In re Cooper Companies, Inc. Shareholder Derivative Litigation*, Case No. RG06260748. A consolidated amended complaint was filed on September 18, 2006.

On November 29, 2006, the Superior Court for the County of Alameda entered an order staying the action pending the resolution of the federal derivative action.

Both the state and federal derivative action are derivative in nature and do not seek damages from the Company.

On October 5, 2004, Bausch & Lomb Incorporated (Bausch & Lomb) filed a lawsuit against Ocular Sciences, Inc. in the U.S. District Court for the Western District of New York alleging that its *Biomedics* toric soft contact lens and its private label equivalents infringe Bausch & Lomb's U.S. Patent No. 6,113,236 relating to toric contact lenses having optimized thickness profiles. The complaint seeks an award of damages, including multiple damages, attorneys' fees and costs and an injunction preventing the alleged infringement. The parties have filed claim construction briefs for the court to consider for its Markman order, and fact discovery substantially concluded during the first quarter of fiscal 2006. Based on our review of the complaint and the patent, as well as other relevant information obtained in discovery, we believe this lawsuit is without merit and plan to continue to pursue a vigorous defense.

United States Tax Court Litigation: On September 29, 2004, the Internal Revenue Service (IRS) issued Notices of Deficiency (Notices) to Ocular Sciences, Inc. (Ocular) in connection with its audit of Ocular's income tax returns for the years 1999, 2000 and 2001. The Notices primarily pertain to transfer pricing issues and an alternative adjustment under the anti-deferral provisions of Subpart F of the Internal Revenue Code and asserts that \$44.8 million of additional taxes is owed for these years, plus unspecified interest and approximately \$12.7 million in related penalties.

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On December 29, 2004, Ocular filed a Petition for the United States Tax Court to redetermine the deficiencies asserted by the IRS. On April 24, 2007, the Company received notification from the United States Tax Court that final decisions have been entered in the case on April 18, 2007. As a result, the total deficiency was reduced to \$3.5 million, plus unspecified interest, with no penalties being assessed. The amount of the deficiency has largely been reserved in connection with the Ocular acquisition and will not have a material adverse effect on earnings. Because of the nature of the adjustments under the anti-deferral provisions of Subpart F, the decision has no precedential value on subsequent years of Ocular (2002-2005), which are currently under examination by the IRS.

The Company continues to be subject to the examination of Ocular's income tax returns by the IRS and other fiscal authorities, and we cannot assure that the outcomes from these examinations will not have a material adverse effect on the Company's operating results and financial condition. Moreover, the Company's future effective tax rates could be adversely affected by earnings being higher than anticipated in countries where it has higher statutory rates or lower than expected in countries where it has lower statutory rates, by changes in the valuation of deferred tax assets or liabilities or by changes in tax laws or interpretations thereof.

On April 10, 2006, CooperVision filed a lawsuit against CIBA Vision (CIBA) in the United States District Court for the Eastern District of Texas alleging that CIBA is infringing United States Patent Nos. 6,431,706, 6,923,538, 6,467,903, 6,857,740 and 6,971,746 by, among other things, making, using, selling and offering to sell its O2Optix line of contact lenses. On June 5, 2006, CIBA filed an answer denying infringement and asserting certain affirmative defenses. The Court has set a trial date of January 8, 2008.

On April 11, 2006, CooperVision filed a lawsuit against CIBA in the United States District Court for the District of Delaware seeking a judicial declaration that CooperVision's *Biofinity* line of silicone hydrogel contact lenses does not infringe any valid and enforceable claims of United States Patent Nos. 5,760,100, 5,776,999, 5,789,461, 5,849,811, 5,965,631 and 6,951,894. On July 5, 2006, CIBA answered the complaint by denying the allegation that CooperVision's *Biofinity* line of silicone hydrogel contact lenses does not infringe any valid and enforceable claims of the foregoing patents. The answer also asks the Court for permission to interpose a counterclaim for infringement in the future if, after examination of the lenses, CIBA believes they infringe the foregoing patents, which counterclaim would seek both damages and injunctive relief. The Court has set a trial date of October 6, 2008.

On November 21, 2006, CooperVision filed a lawsuit against CIBA in the United States District Court for the Eastern District of Texas alleging that CIBA is infringing United States Patent Nos. 7,134,753 and 7,133,174 by, among other things, making, using, selling and offering to sell its O2Optix toric line of contact lenses. On December 11, 2006, CIBA filed an answer denying infringement and asserting certain affirmative defenses. The Court has set a trial date of January 8, 2008.

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(Unaudited)

Note 14. Financial Information for Guarantor and Non-Guarantor Subsidiaries

On January 31, 2007, the Company issued \$350 million aggregate principal amount of 7.125% Senior Notes due 2015 (the Notes, see Note 6). The Notes are guaranteed by certain of our direct and indirect subsidiaries. The Notes are our general unsecured obligations; senior in right of payment to all of our existing and any future subordinated indebtedness; pari passu in right of payment with all of our existing and any future unsecured indebtedness that is not by its terms expressly subordinated to the Notes; effectively junior in right of payment to our existing and future secured indebtedness to the extent of the value of the collateral securing that indebtedness; unconditionally guaranteed by all of our existing and future domestic subsidiaries, other than any excluded domestic subsidiaries; and structurally subordinated to indebtedness of our subsidiaries that are not subsidiary guarantors.

Presented below are the Consolidating Condensed Statements of Operations for the three and six months ended April 30, 2007 and 2006, the Consolidating Condensed Balance Sheets as of April 30, 2007 and October 31, 2006 and the Consolidating Condensed Statements of Cash Flows for the six months ended April 30, 2007 and 2006 for The Cooper Companies, Inc. (Parent Company), the guarantor subsidiaries (Guarantor Subsidiaries) and the subsidiaries that are not guarantors (Non-Guarantor Subsidiaries):

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THE COOPER COMPANIES, INC. AND SUBSIDIARIES

Notes to Consolidated Condensed Financial Statements, Continued

(Unaudited)

Consolidating Condensed Statements of Operations

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
<u>Three Months Ended April 30, 2007</u>					
Net sales	\$	\$ 114,190	\$ 132,459	\$ (21,114)	\$ 225,535
Cost of sales		49,329	70,599	(20,849)	99,079
Gross profit		64,861	61,860	(265)	126,456
Operating expenses	7,324	51,962	56,964	(325)	115,925
Operating income (loss)	(7,324)	12,899	4,896	60	10,531
Interest expense	10,918				10,918
Other income (expense), net	14,850	(10,460)	(4,381)		9
(Loss) income before income taxes	(3,392)	2,439	515	60	(378)
Provision for (benefit from) income taxes	(2,278)	1,392	1,035		149
Net (loss) income	\$ (1,114)	\$ 1,047	\$ (520)	\$ 60	\$ (527)

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
<u>Six Months Ended April 30, 2007</u>					
Net sales	\$	\$ 221,838	\$ 253,673	\$ (30,556)	\$ 444,955
Cost of sales		98,731	119,929	(30,073)	188,587
Gross profit		123,107	133,744	(483)	256,368
Operating expenses	17,440	102,813	110,556	(734)	230,075
Operating income (loss)	(17,440)	20,294	23,188	251	26,293
Interest expense	20,710				20,710
Other income (expense), net	25,154	(15,882)	(8,444)		828
Income (loss) before income taxes	(12,996)	4,412	14,744	251	6,411
Provision for (benefit from) income taxes	(6,318)	2,702	5,206		1,590
Net income (loss)	\$ (6,678)	\$ 1,710	\$ 9,538	\$ 251	\$ 4,821

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Consolidating Condensed Statements of Operations

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
Three Months Ended April 30, 2006					
Net sales	\$	\$ 122,215	\$ 140,864	\$ (51,682)	\$ 211,397
Cost of sales		59,469	64,070	(43,505)	80,034
Gross profit		62,746	76,794	(8,177)	131,363
Operating expenses	7,180	53,999	46,414	(710)	106,883
Operating income (loss)	(7,180)	8,747	30,380	(7,467)	24,480
Interest expense	7,787				7,787
Other income (expense), net	14,611	(10,035)	(5,676)		(1,100)
Income (loss) before income taxes	(356)	(1,288)	24,704	(7,467)	15,593
Provision for (benefit from) income taxes	(1,013)	6,006	(3,101)		1,892
Net income (loss)	\$ 657	\$ (7,294)	\$ 27,805	\$ (7,467)	\$ 13,701

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
Six Months Ended April 30, 2006					
Net sales	\$	\$ 236,571	\$ 273,209	\$ (92,644)	\$ 417,136
Cost of sales		120,429	122,184	(86,001)	156,612
Gross profit		116,142	151,025	(6,643)	260,524
Operating expenses	15,770	96,910	91,202	(1,552)	202,330
Operating income (loss)	(15,770)	19,232	59,823	(5,091)	58,194
Interest expense	20,300				20,300
Other income (expense), net	18,933	(10,252)	(10,859)		(2,178)
Income (loss) before income taxes	(17,137)	8,980	48,964	(5,091)	35,716
Provision for (benefit from) income taxes	(14,406)	18,090	377		4,061
Net income (loss)	\$ (2,731)	\$ (9,110)	\$ 48,587	\$ (5,091)	\$ 31,655

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(Unaudited)

Consolidating Condensed Balance Sheets

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
April 30, 2007					
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 2,078	\$ 1,394	\$ 8,561	\$	\$ 12,033
Trade receivables, net		69,445	87,327		156,772
Inventories, net		93,749	227,379	(59,516)	261,612
Deferred tax asset	564	14,423	3,716		18,703
Other current assets	2,825	15,159	31,720	(281)	49,423
Total current assets	5,467	194,170	358,703	(59,797)	498,543
Property, plant and equipment, net	772	87,098	468,233		556,103
Goodwill	58	673,949	586,482		1,260,489
Other intangibles, net	407	86,924	60,162		147,493
Deferred tax asset	61,788	(40,509)	2,133		23,412
Other assets	1,488,957	1,944	7,869	(1,475,061)	23,709
	\$ 1,557,449	\$ 1,003,576	\$ 1,483,582	\$ (1,534,858)	\$ 2,509,749
LIABILITIES					
Current liabilities:					
Short-term debt	\$	\$ 286	\$ 48,131	\$	\$ 48,417
Other current liabilities	43,251	52,601	112,316		208,168
Total current liabilities	43,251	52,887	160,447		256,585
Long-term debt	817,076		370		817,446
Deferred tax liability		1	11,680		11,681
Intercompany and other liabilities	(332,980)	(134,608)	473,884	1	6,297
Total liabilities	527,347	(81,720)	646,381	1	1,092,009
Stockholders' equity	1,030,102	1,085,296	837,201	(1,534,859)	1,417,740
	\$ 1,557,449	\$ 1,003,576	\$ 1,483,582	\$ (1,534,858)	\$ 2,509,749

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Consolidating Condensed Balance Sheets

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
October 31, 2006					
ASSETS					
Current assets:					
Cash and cash equivalents	\$ 401	\$ (307)	\$ 8,130	\$	\$ 8,224
Trade receivables, net		66,149	80,435		146,584
Inventories, net		107,814	187,598	(58,900)	236,512
Deferred tax asset	(240)	16,063	3,836		19,659
Other current assets	2,438	14,549	29,827	(842)	45,972
Total current assets	2,599	204,268	309,826	(59,742)	456,951
Property, plant and equipment, net	417	80,278	415,662		496,357
Goodwill		632,952	584,132		1,217,084
Other intangibles, net	407	84,048	62,705		147,160
Deferred tax asset	19,781		1,698		21,479
Other assets	1,482,633	4,250	1,748	(1,475,061)	13,570
	\$ 1,505,837	\$ 1,005,796	\$ 1,375,771	\$ (1,534,803)	\$ 2,352,601
LIABILITIES AND STOCKHOLDERS' EQUITY					
Current liabilities:					
Short-term debt	\$ 37,500	\$ 714	\$ 23,152	\$	\$ 61,366
Other current liabilities	24,257	78,884	112,123		215,264
Total current liabilities	61,757	79,598	135,275		276,630
Long-term debt	680,404	500	382		681,286
Deferred tax liability	(37,962)	37,962	9,494		9,494
Intercompany and other liabilities	(238,113)	(180,777)	425,572		6,682
Total liabilities	466,086	(62,717)	570,723		974,092
Stockholders' equity	1,039,751	1,068,513	805,048	(1,534,803)	1,378,509
	\$ 1,505,837	\$ 1,005,796	\$ 1,375,771	\$ (1,534,803)	\$ 2,352,601

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Consolidating Condensed Statements of Cash Flows

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
<u>Six Months Ended April 30, 2007</u>					
Cash flows from operating activities:					
Net cash provided by operating activities	\$ 5,182	\$ 37,199	\$ 6,053	\$	\$ 48,434
Cash flows from investing activities:					
Purchase of property, plant and equipment	(80)	(12,110)	(77,900)		(90,090)
Acquisitions of businesses, net of cash acquired	(326)	(67,086)	(1,381)		(68,793)
Net cash used in investing activities	(406)	(79,196)	(79,281)		(158,883)
Cash flows from financing activities:					
Net proceeds (repayments) of short-term debt		(2,328)	25,049		22,721
Intercompany proceeds (repayments)	(95,125)	46,806	48,319		
Net proceeds (repayments) of long-term debt	99,100	(780)	(84)		98,236
Debt acquisition costs	(11,226)				(11,226)
Dividends on common stock	(1,337)				(1,337)
Excess tax benefit from share-based compensation arrangements	176				176
Proceeds from exercise of stock options	5,313				5,313
Net cash provided by (used in) financing activities	(3,099)	43,698	73,284		113,883
Effect of exchange rate changes on cash and cash equivalents			375		375
Net increase in cash and cash equivalents	1,677	1,701	431		3,809
Cash and cash equivalents at the beginning of the period	401	(307)	8,130		8,224
Cash and cash equivalents at the end of the period	\$ 2,078	\$ 1,394	\$ 8,561	\$	\$ 12,033

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Consolidating Condensed Statements of Cash Flows

	Parent Company	Guarantor Subsidiaries	Non-Guarantor Subsidiaries (In thousands)	Consolidating Entries	Consolidated Total
<u>Six Months Ended April 30, 2006</u>					
Cash flows from operating activities:					
Net cash provided by operating activities	\$ 25,372	\$ 4,731	\$ 45,676	\$ 585	\$ 76,364
Cash flows from investing activities:					
Purchase of property, plant and equipment	(231)	(19,551)	(63,697)		(83,479)
Acquisitions of businesses, net of cash acquired	(2,279)	(38,608)	(20,348)		(61,235)
Net cash used in investing activities	(2,510)	(58,159)	(84,045)		(144,714)
Cash flows from financing activities:					
Net proceeds (repayments) of short-term debt		1,513	10,259		11,772
Intercompany proceeds (repayments)	(78,064)	53,230	25,419	(585)	
Net proceeds (repayments) of long-term debt	40,250	(150)	(50)		40,050
Debt acquisition costs	(625)				(625)
Dividends on common stock	(1,335)				(1,335)
Excess tax benefit from share-based compensation arrangements	1,510				1,510
Proceeds from exercise of stock options	2,500				2,500
Net cash provided by (used in) financing activities	(35,764)	54,593	35,628	(585)	53,872
Effect of exchange rate changes on cash and cash equivalents			207		207
Net increase in cash and cash equivalents	(12,902)	1,165	(2,534)		(14,271)
Cash and cash equivalents at the beginning of the period	13,262	(813)	18,377		30,826
Cash and cash equivalents at the end of the period	\$ 360	\$ 352	\$ 15,843	\$	\$ 16,555

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Note 15. Business Segment Information

Cooper uses operating income, as presented in our financial reports, as the primary measure of segment profitability. We do not allocate costs from corporate functions to the segments' operating income. Items below operating income are not considered when measuring the profitability of a segment. We use the same accounting policies to generate segment results as we do for our consolidated results.

Identifiable assets are those used in continuing operations except cash and cash equivalents, which we include as corporate assets. Long-lived assets are property, plant and equipment.

Segment information:

	Three Months Ended April 30,		Six Months Ended April 30,	
	2007	2006	2007	2006
	(In thousands)			
Net sales to external customers:				
CVI	\$ 188,159	\$ 181,668	\$ 371,781	\$ 357,294
CSI	37,376	29,729	73,174	59,842
	\$ 225,535	\$ 211,397	\$ 444,955	\$ 417,136
Operating income (loss):				
CVI	\$ 11,501	\$ 33,779	\$ 35,535	\$ 70,806
CSI	6,354	(2,119)	5.9%	5.7%

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10. Fair Value of Financial Instruments

The Company adopted SFAS No. 157 effective January 1, 2008, and accordingly all assets and liabilities measured at fair value will utilize valuation methodologies in accordance with the statement. The Company has established and documented processes for determining fair values. Fair value is based upon quoted market prices, where available. If listed prices or quotes are not available, then fair value is based upon internally developed models that primarily use inputs that are market-based or independently-sourced market parameters, including interest rate yield curves.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The three levels of valuation hierarchy established by FAS 157 are defined as follows:

Level 1 - inputs to the valuation methodology are quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 - inputs to the valuation methodology include quoted prices for similar assets and liabilities in active markets, and inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 - inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The following describes the valuation methodologies used for the Company's financial instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy.

a. Investment Securities Available for Sale - Fair value is generally based on quoted prices provided by dealers who make markets in similar financial instruments. The dealers will incorporate common market pricing methods, including a spread measurement to the Treasury curve or Interest Rate Swap Curve as well as underlying characteristics of the particular security including coupon, periodic and life caps, collateral type, rate reset period and seasoning or age of the security. If the fair value of a security is not reasonably available from a dealer, management estimates the fair value based on characteristics of the security that the Company receives from the issuer and based on available market information. Management reviews all prices used in determining valuation to ensure they represent current market conditions. This review includes surveying similar market transactions, comparisons to interest pricing models as well as offerings of like securities by dealers. The Company's investment securities are valued based upon readily observable market parameters and are classified as Level 2 fair values.

b. Interest Rate Swaps and Caps - The fair value of interest rate swaps and caps are based on using market accepted financial models as well as dealer quotes. The model utilizes readily observable market parameters, including treasury rates, interest rate swap spreads and swaption volatility curves. The Company's interest rate caps and swaps are classified as Level 2 fair values.

The following table presents the Company's financial instruments carried at fair value, at the dates indicated below as of June 30, 2008, on the condensed consolidated balance sheet by SFAS No. 157 valuation hierarchy, as previously described (dollar amounts in thousands):

Fair Value at June 30, 2008

	Level 1	Level 2	Level 3	Total
Assets:				
Investment securities - available for sale	\$ —	\$ 499,404	\$ —	\$ 499,404
Mortgage loans held for sale (net)	—	—	6,200	6,200
Interest Rate Caps	—	355	—	355
Interest Rate Swaps	—	2,085	—	2,085
Total assets carried at fair value	\$ —	\$ 501,844	\$ 6,200	\$ 508,044

The following table provides a summary of changes in fair value of the Level 3 financial asset for the three and six months ended June 30, 2008 (dollar amounts in thousands):

	Three Months	
	Ended June 30, 2008	Six Months Ended June 30, 2008
Mortgage Loans Held for Sale (Net)		
Beginning Balance	\$ 6,209	\$ 8,077
Principal Paydown	(8)	(1,844)
Provision for loan losses	(1)	(399)
Charge-offs		366
Ending Balance	\$ 6,200	\$ 6,200

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Any changes to the valuation methodology are reviewed by management to ensure the changes are appropriate. As markets and products develop and the pricing for certain products becomes more transparent, the Company continues to refine its valuation methodologies. The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies, or assumptions, to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. The Company uses inputs that are current as of the measurement date, which may include periods of market dislocation, during which price transparency may be reduced. This condition could cause the Company's financial instruments to be reclassified from Level 2 to Level 3 in future periods.

11. Segment Reporting

Until March 31, 2007, the Company operated two reportable segments, the mortgage portfolio management segment and the mortgage lending segment. Upon the sale of substantially all the mortgage lending operating assets on March 31, 2007, the Company exited the mortgage lending business and accordingly will no longer report segment information.

12. Capital Stock and Earnings per Share

The Company had 400,000,000 shares of common stock, par value \$0.01 per share, authorized with 9,320,104 shares issued and outstanding as of June 30, 2008 and 1,817,927 shares issued and outstanding as of December 31, 2007. The Company had 200,000,000 shares of preferred stock, par value \$0.01 per share, authorized, including 2,000,000 shares of Series A Cumulative Convertible Redeemable Preferred Stock (" Series A Preferred Stock ") authorized. As of June 30, 2008 and December 31, 2007, the Company had issued and outstanding 1,000,000 and 0 shares, respectively, of Series A Preferred Stock. Of the common stock authorized, 103,111 shares (plus forfeited shares of 32,832 previously granted) were reserved for issuance as restricted stock awards to employees, officers and directors pursuant to the 2005 Stock Incentive Plan. As of June 30, 2008, 135,943 shares remain reserved for issuance under the 2005 Plan.

On February 21, 2008, the Company completed the issuance and sale of 7.5 million shares of its common stock in a private placement at a price of \$8.00 per share. This private offering of the Company's common stock generated net proceeds to the Company of \$56.6 million after payment of private placement fees and expenses. In connection with this private offering of our common stock, we entered into the Common Stock Registration Rights Agreement, pursuant to which we are required to file with the Securities and Exchange Commission, or SEC, a resale shelf registration statement registering for resale the 7.5 million shares sold in this private offering. The Company filed a resale shelf registration statement on Form S-3 on April 4, 2008 which became effective on April 18, 2008.

On April 21, 2008, the Company declared a \$0.12 per share cash dividend on its common stock. The dividend was payable on May 15, 2008 to common stockholders of record as of April 30, 2008. On June 26, 2008, the Company declared a \$0.16 per share cash dividend on its common stock. The dividend was payable on July 25, 2008 to common stockholders of record as of July 10, 2008.

On June 26, 2008 the Company declared a \$0.50 per share cash dividend, or an aggregate of \$0.5 million, payable on July 31, 2008 to holders of record of our Series A Preferred Stock as of June 30, 2008.

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The Board of Directors declared a one-for-two reverse stock split of the Company's common stock, effective on May 27, 2008, decreasing the number of shares outstanding to approximately 9.3 million.

The Board of Directors declared a one for five reverse stock split of the Company's common stock, effective on October 9, 2007, decreasing the number of common shares outstanding at the time to approximately 3.6 million.

All per share and share amounts provided in the quarterly report have been restated to give effect to both reverse stock splits.

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The Company calculates basic net income (loss) per share by dividing net income (loss) for the period by weighted-average shares of common stock outstanding for that period. Diluted net income (loss) per share takes into account the effect of dilutive instruments, such as convertible preferred stock, stock options and unvested restricted or performance stock, but uses the average share price for the period in determining the number of incremental shares that are to be added to the weighted-average number of shares outstanding.

The following table presents the computation of basic and diluted net income (loss) per share for the periods indicated (in thousands, except per share amounts):

	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
	2008	2007	2008	2007
Numerator:				
Net income (loss) – Basic	\$ 1,263	\$ (14,196)	\$ (19,995)	\$ (18,937)
Net income (loss) from continuing operations	434	(5,178)	(21,004)	(6,078)
Net income (loss) from discontinued operations (net of tax)	829	(9,018)	1,009	(12,859)
Effect of dilutive instruments:				
Convertible preferred debentures (1)	569	—	1,075	—
Net income (loss) – Dilutive	1,263	(14,196)	(19,995)	(18,937)
Net income (loss) from continuing operations	434	(5,178)	(21,004)	(6,078)
Net income (loss) from discontinued operations (net of tax)	\$ 829	\$ (9,018)	\$ 1,009	\$ (12,859)
Denominator:				
Weighted average basis shares outstanding	9,320	1,811	7,218	1,810
Effect of dilutive instruments:				
Convertible preferred debentures (1)	2,500	—	2,267	—
Weighted average dilutive shares outstanding	9,320	1,811	7,218	1,810
EPS:				
Basic EPS	\$ 0.14	\$ (7.84)	\$ (2.77)	\$ (10.46)
Basic EPS from continuing operations	0.05	(2.86)	(2.91)	(3.36)
Basic EPS from discontinued operations (net of tax)	0.09	(4.98)	0.14	(7.10)
Dilutive EPS	\$ 0.14	\$ (7.84)	\$ (2.77)	\$ (10.46)
Dilutive EPS from continuing operations	0.05	(2.86)	(2.91)	(3.36)
Dilutive EPS from discontinued operations (net of tax)	0.09	(4.98)	0.14	(7.10)

(1) – Amount excluded from dilutive calculation as it is anti-dilutive.

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13. Convertible Preferred Debentures

As of June 30, 2008, there were 1.0 million shares of our Series A Preferred Stock outstanding, with an aggregate redemption value of \$20.0 million and current dividend payment rate of 10% per year. The Series A Preferred Stock matures on December 31, 2010, at which time any outstanding shares must be redeemed by the Company at the \$20.00 per share liquidation preference. Pursuant to SFAS No. 150, *Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity*, because of this mandatory redemption feature, the Company classifies these securities as a liability on its balance sheet.

We issued these shares of Series A Preferred Stock, to JMP Group Inc. and certain of its affiliates for an aggregate purchase price of \$20.0 million. The Series A Preferred Stock entitles the holders to receive a cumulative dividend of 10% per year, subject to an increase to the extent any future quarterly common stock dividends exceed \$0.20 per share. The Series A Preferred Stock is convertible into shares of the Company's common stock based on a conversion price of \$8.00 per share of common stock, which represents a conversion rate of two and one-half (2 ½) shares of common stock for each share of Series A Preferred Stock.

14. Related Party Transactions

Concurrent and in connection with the issuance of our Series A Preferred Stock on January 18, 2008, we entered into an advisory agreement with JMPAM, which is an affiliate of JMP Group, Inc. and JMP Realty Trust, Inc. As of April 23, 2008, JMPAM and JMP Group, Inc. beneficially owned approximately 16.8% and 12.2% of our common stock. Under the agreement, JMPAM advises the Managed Subsidiaries. As previously disclosed, we have an approximately \$63.7 million net operating loss carry-forward that remains with us after the sale of our mortgage lending business. As an advisor to the Managed Subsidiaries, we expect that JMPAM will, at some point in the future, focus on the acquisition of alternative mortgage related investments on behalf of the Managed Subsidiaries. Some of those investments may allow us to utilize all or a portion of the net operating loss carry-forward to the extent available by law. The commencement of any activity by JMPAM must be approved by the Board of Directors and any subsequent investment on behalf of Managed Subsidiaries must adhere to investment guidelines adopted by our board of directors. JMPAM will earn a base advisory fee of 1.5% of the "equity capital" (as defined in the advisory agreement) of the Managed Subsidiaries and is also eligible to earn incentive compensation if the Managed Subsidiaries achieve certain performance thresholds. As of June 30, 2008, JMPAM was not managing any assets in the Managed Subsidiaries, but was earning a base advisory fee on the net proceeds to our Company from our private offerings in each of January 2008 and February 2008. For the three and six months ended June 30, 2008, we paid JMPAM \$0.2 million and \$0.3 million respectively, in advisory fees. As of the date of this report, we expect to pay approximately \$0.7 million in advisory fees to JMPAM during the 2008 fiscal year.

In addition, pursuant to the stock purchase agreement providing for the sale of the Series A Preferred Stock to JMP Group, Inc. and certain of its affiliates, James J. Fowler and Steven M. Abreu were appointed to our Board of Directors, with Mr. Fowler being appointed the non-executive chairman of our Board of Directors. In addition, concurrent with the completion of the issuance and sale of the Series A Preferred Stock and pursuant to the stock purchase agreement, four of our then-existing directors resigned from the Board.

James J. Fowler, the Non-Executive Chairman of our Board of Directors and also the non-compensated Chief Investment Officer of Hypotheca Capital, LLC and New York Mortgage Funding, LLC, is a managing director of JMPAM and the president of JMP Realty Trust, Inc., a private REIT that is externally managed by JMPAM and which

is one of the investors in our Series A Preferred Stock. JMPAM and JMP Realty Trust, Inc. are affiliates of JMP Group, Inc.

On February 21, 2008, we completed the issuance of 7.5 million shares of our common stock in a private placement to certain accredited investors, resulting in \$56.6 million in net proceeds to the Company. JMP Securities LLC, an affiliate of JMPAM, JMP Group, Inc. and JMP Realty Trust, Inc., served as the sole placement agent for the transaction and was paid a \$3.0 million placement fee from the gross proceeds.

NEW YORK MORTGAGE TRUST, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2008
(unaudited)

15. Income Taxes

All income tax benefits relate to HC and are included in the results of operations of the discontinued operation. Deferred taxes at June 30, 2008 include a deferred tax asset of \$0.1 million and a deferred tax liability of \$0.1 million which represents the tax effect of differences between tax basis and financial statement carrying amounts of assets and liabilities. The \$63.7 million net operating loss carry-forward expires at various intervals between 2024 and 2028. During the quarter ended September 30, 2007 management determined that the Company would likely not be able to utilize the deferred tax asset and accordingly recorded a 100% valuation allowance. The Company continued to reserve 100% of deferred tax benefit in the quarter ended June 30, 2008 as the facts continue to support the Company's inability to utilize the deferred tax asset.

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

CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains certain forward-looking statements. Forward-looking statements are those which are not historical in nature. They can often be identified by their inclusion of words such as “will,” “anticipate,” “estimate,” “should,” “expect,” “believe,” “intend” and similar expressions. Any projection of revenues, earnings, losses, capital expenditures, distributions, capital structure or other financial terms is a forward-looking statement. Certain statements regarding the following particularly are forward-looking in nature:

- our business strategy;
- future performance, developments, market forecasts or projected dividends;
- projected acquisitions or joint ventures; and
- projected capital expenditures.

It is important to note that the description of our business in general and our investment in mortgage loans and mortgage-backed securities holdings in particular, is a statement about our operations as of a specific point in time and is not meant to be construed as an investment policy. The types of assets we hold, the amount of leverage we use or the liabilities we incur and other characteristics of our assets and liabilities disclosed in this report as of a specified period of time are subject to reevaluation and change without notice.

Our forward-looking statements are based upon our management's beliefs, assumptions and expectations of our future operations and economic performance, taking into account the information currently available to us. Forward-looking statements involve risks and uncertainties, some of which are not currently known to us and many of which are beyond our control and that might cause our actual results, performance or financial condition to be materially different from the expectations of future results, performance or financial condition we express or imply in any forward-looking statements. Some of the important factors that could cause our actual results, performance or financial condition to differ materially from expectations are:

- our portfolio strategy and operating strategy may be changed or modified by our management without advance notice to you or stockholder approval and we may suffer losses as a result of such modifications or changes;
- market changes in the terms and availability of repurchase agreements used to finance our investment portfolio activities;
- reduced demand for our securities in the mortgage securitization and secondary markets;
- interest rate mismatches between our mortgage-backed securities and our borrowings used to fund such purchases;
- changes in interest rates and mortgage prepayment rates;
- effects of interest rate caps on our adjustable-rate mortgage-backed securities;
- the degree to which our hedging strategies may or may not protect us from interest rate volatility;

- potential impacts of our leveraging policies on our net income and cash available for distribution;
- our board's ability to change our operating policies and strategies without notice to you or stockholder approval;
- our ability to manage, minimize or eliminate liabilities stemming from the discontinued operations including, among other things, litigation, repurchase obligations on the sales of mortgage loans and property leases; and
- the other important factors identified, or incorporated by reference into this report, including, but not limited to those under the captions “Management's Discussion and Analysis of Financial Condition and Results of Operations” and “Quantitative and Qualitative Disclosures about Market Risk”, and those described in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2007, Part II, Item 1A of our Quarterly Report on Form 10-Q for the three months ended June 30, 2008 and the various other factors identified in any other documents filed by us with the Securities and Exchange Commission, or SEC.

We undertake no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. In light of these risks, uncertainties and assumptions, the events described by our forward-looking events might not occur. We qualify any and all of our forward-looking statements by these cautionary factors. In addition, you should carefully review the risk factors described in other documents we file from time to time with the Securities and Exchange Commission.

General

New York Mortgage Trust, Inc. together with its consolidated subsidiaries (“NYMT”, the “Company”, “we”, “our”, and “us”) a self-advised real estate investment trust, or REIT, in the business of investing in residential adjustable rate mortgage-backed securities issued by a United States government-sponsored enterprise (“GSE” or “Agency”), such as the Federal National Mortgage Association (“Fannie Mae”), or the Federal Home Loan Mortgage Corporation (“Freddie Mac”), prime credit quality residential adjustable-rate mortgage (“ARM”) loans, or prime ARM loans, and non-agency mortgage-backed securities. We refer to residential adjustable rate mortgage-backed securities throughout this Quarterly Report on Form 10-Q as “MBS” and MBS issued by a GSE as “ Agency MBS”. We seek attractive long-term investment returns by investing our equity capital and borrowed funds in such securities. Our principal business objective is to generate net income for distribution to our stockholders resulting from the spread between the interest and other income we earn on our interest-earning assets and the interest expense we pay on the borrowings that we use to finance these assets, which we refer to as our net interest income. We believe that the best approach to generating a positive net interest income is to manage our liabilities, principally in the form of short-term indebtedness (maturities of one year or less), in relation to the interest rate risks of our investments. To help achieve this result, we employ repurchase agreement financing, generally short-term, and over time will combine our financings with hedging techniques, primarily interest rate swaps. We may, subject to maintaining our REIT qualification, also employ other hedging techniques from time to time, including interest rate caps, floors and swap options to protect against adverse interest rate movements.

Since inception, our investment portfolio strategy has focused on the acquisition of high-credit quality ARM loans and securities. Moreover, since our exit from the mortgage lending business on March 31, 2007, we have exclusively focused our resources and efforts on investing, on a leveraged basis, in MBS and, since August 2007, we have employed a portfolio strategy that focuses on investments in Agency MBS. As of June 30, 2008, our investment portfolio was comprised of \$499.4 million in MBS, including \$273.0 million of Agency ARM MBS, \$199.3 million of Agency CMO floaters and \$27.1 million of non-Agency MBS, of which \$26.7 million are rated in the highest category by two rating agencies (either Moody's Investor Service, Inc. or Standard & Poor's, Inc.), and \$377.0 million of prime ARM loans held in securitization trusts. As of June 30, 2008, we had approximately \$897.3 million of total assets as compared to \$809.3 million at December 31, 2007.

Our Alternative Investment Strategy Under Our Advisory Agreement

Although we are in the business of investing in MBS and have most recently employed a portfolio strategy that focuses on investments in Agency MBS, we may engage in an alternative mortgage related investment strategy in the near future that would potentially allow us to utilize an approximately \$63.7 million net operating loss carry-forward that resulted from our exit from the mortgage lending business. We expect this alternative mortgage-related investment strategy, which will be managed by JMP Asset Management LLC (“JMPAM”) pursuant to an advisory agreement between JMPAM and our company, to primarily take the form of equity investments in unaffiliated third party entities, or Funds, that acquire or manage a portfolio of non-Agency MBS, some or all of which may be classified as non-investment grade securities. Under the advisory agreement with JMPAM, which was entered into concurrent with our issuance of 1.0 million shares of Series A Cumulative Convertible Redeemable Preferred Stock to JMP Group, Inc. and certain of its affiliates, JMPAM advises two of our wholly-owned subsidiaries, Hypotheca Capital, LLC, or HC (formerly known as The New York Mortgage Company, LLC), and New York Mortgage Funding, LLC, or NYMF, as well as any additional subsidiaries acquired or formed in the future to hold investments made on our behalf by JMPAM. We refer to these subsidiaries in our periodic reports filed with the SEC as the “Managed Subsidiaries.” As an advisor to the Managed Subsidiaries, we expect that JMPAM will focus on the acquisition of alternative mortgage related investments. Investments by us in Funds will generally expose us to greater credit risk and less interest rate risk than investments in Agency MBS. Although our investment strategy thus far in 2008 has focused on the acquisition of Agency MBS, JMPAM may commence investments under this alternative mortgage related investment strategy in the near future; *provided, however*, that the commencement of investments by JMPAM under this strategy must first be approved by our board of directors and any subsequent investment on behalf of Managed Subsidiaries must adhere to investment guidelines adopted by our board of directors. This strategy, if and when implemented, will vary from our core strategy and we can provide no assurance that we will be successful at implementing any alternative investment strategy.

Significant Events Second Quarter

Reverse Stock Split

On May 27, 2008, we completed a one-for-two reverse stock split of our common stock. The one-for-two reverse stock split (the “2008 Reverse Stock Split”) provided stockholders of record as of 12:01 a.m. on May 27, 2008, which we refer to as the effective time, with one share of our common stock for every two shares of common stock owned as of the effective time. The Articles Supplementary Establishing and Fixing the Rights and Preferences of the Series A Preferred Stock, or Articles Supplementary, provide that the conversion rate and effective conversion price for our Series A Preferred Stock be appropriately adjusted to reflect any reverse stock split. As a result, the conversion rate on our Series A Preferred Stock was automatically adjusted to two and one-half to one (2 ½ to 1) from the original five to one (5 to 1) conversion rate and the effective conversion price on our Series A Preferred Stock was adjusted to \$8.00 per share from the original \$4.00 per share.

Common Stock Approved for Listing on NASDAQ Capital Market

Our common stock was approved for listing on the NASDAQ Capital Market on June 4, 2008 and began trading on the NASDAQ Capital Market effective June 5, 2008 under the symbol “NYMT”. Prior to our listing on the NASDAQ Capital Market, our common stock was most recently quoted on the Over-the-Counter Bulletin Board, or OTCBB, under the stock symbol “NYMO”. Our Series A Preferred Stock is not currently listed on any securities exchange.

Pursuant to a registration rights agreement between our company and the investors in our February 2008 private placement of common stock, we are subject to a liquidated damages penalty upon certain events. Because our common stock was not listed on the NASDAQ Capital Market for the period April 19, 2008 through the date of our initial listing, we paid the investors in our February 2008 private placement approximately \$0.5 million in liquidated

damages on July 3, 2008. In addition, in May 2008, we paid these same investors approximately \$0.2 million in liquidated damages as a result of our failure to file a resale registration statement during the time period required pursuant to the registration rights agreement. Although we do not expect to incur additional liquidated damages under this agreement in the future, there can be no assurance that we will remain in compliance with the liquidated damage provisions in the future.

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Known Material Trends and Commentary

Declines in the prices of mortgage assets - Investors' appetite for U.S. mortgage assets continued to be weak in the first half of 2008. In addition, the market disruption of March 2008 and related de-leveraging in the mortgage asset industry involved the liquidation or sale of a significant amount of Agency securities. This selling, along with decreased demand for these assets among investors, caused mortgage asset prices to decline in the quarter ended March 31, 2008. Prices improved during the second quarter as FNMA and FHLMC increased buying of Agency securities for their portfolio. The increased buying by the agencies was a direct result of the removal of the consent order that restricted portfolio growth by the Office of Federal Housing Enterprise Oversight (OFHEO)

Tightening in the financing markets and reduced liquidity - As prices of mortgage assets decreased, many lenders that finance mortgage assets took measures to insure their liquidity needs would not be compromised, particularly in March 2008. In connection with the market disruption of March 2008, many financial institutions withdrew financing and liquidity that they typically offered clients as part of their daily business operations. The most common forms of liquidity provided to the mortgage market are in the form of repurchase agreements for MBS. This reduced availability of financing subsequently led to de-leveraging by many in the industry and, in some cases, forced liquidations, all of which exacerbated the problem. During the second quarter liquidity stabilized and there were no significant failures or disruptions.

Volatility in financing costs - The dislocations in the mortgage market led to increased volatility in the cost of financing. The relationships between certain short-term interest rates, normally very consistent, became less so in the second half of 2007 and has continued to widen during the first half of 2008. The Federal Funds rate, an interest rate used by banks for overnight loans to each other and determined by the Federal Reserve Board, is a benchmark used by others to determine similar short term rates. The London Inter Bank Offered Rate ("LIBOR"), a market determined rate for short term loans, is typically 10 basis points higher than the Federal Funds rate. LIBOR averaged 12 basis points above the Fed Funds target during the first quarter and 50 basis points during the second quarter. Because our repurchase agreements rates generally move with one month LIBOR, our costs have not decreased on a relative basis as would be expected given the 225 basis points reduction in the Fed Funds rate since the beginning of the year.

Hedging - We generally seek to reduce the volatility of our net income by entering into interest rate swap agreements. As of June 30, 2008, we are a party to interest rate swap agreements with an aggregate notional amount of \$158 million. The Company discontinued hedge accounting treatment for the interest rate swap positions during the fourth quarter of 2007 as part of our strategic portfolio realignment related to the Series A Preferred Stock offering. Accordingly, the unrealized loss was recorded as an unrealized loss in our Statement of Operations and no longer reflected as part of other comprehensive income in our Balance Sheet. During the quarter ended March 31, 2008 the Company terminated certain swaps resulting in a realized loss of \$4.8 million. The Company did not terminate any additional swaps during the second quarter of 2008.

Changes in the U.S. economy - Changes in the U.S. economy have also affected us. The U.S. economy continued to soften in the first half of 2008. Weak demand in the housing market and increased stress on borrowers, including in particular, residential mortgage borrowers, has had a ripple effect throughout the U.S. economy. As stated in testimony by the Chairman of the Federal Reserve to the U.S. Senate Committee on Banking, Housing and Urban Affairs on July 15, 2008, "sales of existing homes have been about unchanged this year, sales of new homes have continued to fall, and inventories of unsold new homes remain high." As a result, home prices have continued to fall, particularly in regions that experienced the largest price increases earlier this decade. This decline in home prices has contributed to increased home foreclosures during 2008. The Federal Reserve continued to reduce short term interest rates resulting in an overall reduction of 200 basis points during the first quarter of 2008 with another 25 basis points reduction on April 30, 2008. Recently, increased concern regarding inflation has arisen principally due to increases in global commodity prices. We believe the inflation concerns have kept longer term interest rates high relative to short term rates. This so called steep yield curve generally results in increased returns on equity for companies that employ

an Agency MBS strategy similar to ours. The possibility of rising inflation, however, increases the possibility of interest rates moving higher to slow inflationary stresses, which may result in flattening of the yield curve.

Presentation Format

In connection with the sale of substantially all of our wholesale and retail mortgage lending platform assets during the first quarter of 2007, we classified certain assets and liabilities related to our mortgage lending segment as a discontinued operation in accordance with the provisions of SFAS No. 144. As a result, we have reported revenues and expenses related to the segment as a discontinued operation and the related assets and liabilities as assets and liabilities related to a discontinued operation for all periods presented in the accompanying condensed consolidated financial statements. Our continuing operations are primarily comprised of what had been our portfolio management operations. In addition, certain assets such as the deferred tax asset, and certain liabilities, such as subordinated debt and liabilities related to leased facilities not assigned to Indymac, have become part of the ongoing operations of NYMT and accordingly, we have not classified as a discontinued operation in accordance with the provisions of SFAS No. 144.

The Board of Directors declared a one for five reverse stock split of our common stock, providing shareholders of record as of October 9, 2007, with one share of common stock for each five shares owned of record as of October 9, 2007 (the "2007 Reverse Stock Split"). Prior and current period share amounts and earnings per share disclosures have been restated to reflect the 2008 Reverse Stock Split and 2007 Reverse Stock Split.

Significance of Estimates and Critical Accounting Policies

A summary of our critical accounting policies is included in our Annual Report on Form 10-K for the year ended December 31, 2007 in "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations" and "Note 2 - Summary of Significant Accounting Policies" to the consolidated financial statements included therein. There have been no significant changes to those policies during 2008.

Overview of Performance

For the three and six months ended June 30, 2008, we reported a net income (loss) of \$1.3 million and \$(20.0) million as compared to a net loss of \$14.2 million and \$18.9 million, respectively for the same periods in 2007.

The main components of the change in income (loss) for the three and six months ended June 30, 2008 as compared to the same period for the prior year are detailed in the following table (dollar amounts in thousands):

Detailed Components of the change in income (loss)

	For the Three Months Ended June 30,			For the Six Months Ended June 30,		
	2008	2007	Difference	2008	2007	Difference
Net interest income on investment portfolio	\$ 3,964	\$ 1,006	\$ 2,958	\$ 6,703	\$ 1,635	\$ 5,068
Net interest income	2,499	112	2,387	3,773	(141)	3,914
Loan losses	(22)	(940)	918	(1,455)	(940)	(515)
Loss on securities and related hedges	(83)	(3,821)	3,738	(19,931)	(3,821)	(16,110)
Income (loss) on continuing operations	434	(5,178)	5,612	(21,004)	(6,078)	(14,926)
Income (loss) from discontinued operations - net of tax	829	(9,018)	9,847	1,009	(12,859)	(13,868)
Net income (loss)	\$ 1,263	\$ (14,196)	\$ 15,549	\$ (19,995)	\$ (18,937)	\$ (1,058)

Summary of Operations and Key Performance Measurements

For the three and six months ended June 30, 2008, our net income was dependent upon the net interest income (the interest income on portfolio assets net of the interest expense and hedging costs associated with the such assets) generated from our portfolio of MBS and mortgage loans held in securitization trusts, which was partially offset by losses on delinquent loans held in securitization trusts and certain other expenses. The net interest spread on our investment portfolio increased to 143 basis points for the quarter ended June 30, 2008, as compared with 85 basis points for the quarter ended March 31, 2008, and 46 basis points for the quarter ended December 31, 2007.

Because the assets in our MBS portfolio represent approximately 56% of our total assets as of June 30, 2008 and we fund these assets, which generally have maturities with longer terms than their funding source, with short-term borrowings under repurchase agreements, our ability to achieve our investment objectives depends on our ability to borrow money in sufficient amounts and on favorable terms and on our ability to renew or replace maturing borrowings on a continuous basis. Repurchase agreements provide us with short-term borrowings that are secured by the securities in our investment portfolio and bear interest rates that are closely linked to the LIBOR. During the quarter ended June 30, 2008, we continued to employ a balanced and diverse funding mix to finance our investment portfolio and assets. At June 30, 2008, our MBS portfolio was funded with approximately \$417.9 million of repurchase agreement borrowing, or approximately 48% of our total liabilities, and our loans held in securitization trusts were permanently financed with approximately \$11.8 million of our own equity investment in the securitization trusts and the issuance of approximately \$365.2 million of CDOs, or approximately 43% of our total liabilities. At June 30, 2008 our leverage ratio for our MBS investment portfolio, which we define as our outstanding indebtedness under repurchase agreements divided by total stockholders' equity, was 7 to 1. Given the continued uncertainty in the credit markets, we believe that maintaining a leverage ratio in the range of 7 to 10 times is appropriate at this time.

The key performance measures for our portfolio management activities are:

- net interest spread on the portfolio;
- losses on loans held in securitization trusts;
- change in book value;
- return on equity capital invested.

Financial Condition

As of June 30, 2008, we had approximately \$897.3 million of total assets, as compared to approximately \$809.3 million of total assets as of December 31, 2007. The increase in total assets results primarily from an increase in MBS of \$148.9 million and a decrease of \$53.7 million in mortgage loans held in securitization trust.

We received net proceeds of approximately \$19.6 million from our private offerings of Series A Preferred Stock and \$56.6 million from our common stock during the first quarter of 2008. We used substantially all of the net proceeds to purchase approximately \$714.1 million of Agency MBS during January and February 2008. As previously disclosed in our Quarterly Report on Form 10-Q for the three months ended March 31, 2008, we sold an aggregate of \$592.8 million of Agency MBS in our portfolio during March 2008 in an effort to reduce our leverage and improve our liquidity position in response to the market disruption of March 2008, and incurred a loss of \$15.9 million. In addition, the Company terminated a total of \$517.7 million of notional interest rate swaps in the quarter ended March 31, 2008, resulting in a realized loss of \$4.8 million.

Balance Sheet Analysis - Asset Quality

Investment Securities - Available for Sale - Our securities portfolio primarily consists of Agency securities or AAA-rated residential mortgage-backed securities. At June 30, 2008 and December 31, 2007, we had no investment securities in a single issuer or entity (other than a government sponsored agency of the U.S. Government) that had an aggregate book value in excess of 10% of our total assets. The following tables set forth the credit characteristics of our securities portfolio as of June 30, 2008 and December 31, 2007 (dollar amounts in thousands):

Credit Characteristics of Our Investment Securities

June 30, 2008	Sponsor or Rating	Par Value	Carrying Value	% of Portfolio	Coupon	Yield
Agency REMIC CMO floaters	FNMA/ FHLMC	\$ 208,214	\$ 199,349	40%	3.27%	3.93%
Agency Hybrid Arms	FNMA/ FHLMC	270,553	272,948	55%	5.16%	4.70%
Non-Agency floaters	AAA	28,530	24,552	5%	3.21%	6.00%
NYMT retained securities	AAA-BBB	2,169	2,158	0%	6.76%	5.67%
NYMT retained securities	Below BBB	2,750	397	0%	5.68%	11.69%
Total/Weighted average		\$ 512,216	\$ 499,404	100%	4.29%	4.50%

December 31, 2007	Sponsor or Rating	Par Value	Carrying Value	% of Portfolio	Coupon	Yield
Agency REMIC CMO floaters	FNMA/FHLMC	\$ 324,676	\$ 318,689	91%	5.98%	5.55%
Non-Agency floaters	AAA	29,764	28,401	8%	5.66%	5.50%
NYMT retained securities	AAA-BBB	2,169	2,165	1%	6.31%	6.28%
NYMT retained securities	Below BBB	2,756	1,229	0%	5.68%	12.99%
Total/Weighted average		\$ 359,365	\$ 350,484	100%	5.95%	5.61%

The following table sets forth the stated reset periods and weighted average yields of our investment securities at June 30, 2008 and December 31, 2007 (dollar amounts in thousands):

Reset/ Yield of our Investment Securities

June 30, 2008	Less than 6 Months		More than 6 Months To 24 Months		More than 24 Months To 60 Months		Total	
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield
Agency REMIC CMO floaters	\$ 199,349	3.93%	\$ —	—%	\$ —	—%	\$ 199,349	3.93%
Agency Hybrid Arms	—	—	—	—	272,948	4.70%	272,948	6.00%
Non-Agency floaters	24,552	6.00%	—	—	—	—	24,552	4.70%
NYMT retained securities	2,158	5.67%	—	—	397	11.69%	2,555	9.03%
Total/Weighted average	\$ 226,059	4.20%	\$ —	—%	\$ 273,345	4.77%	\$ 499,404	4.50%

December 31, 2007	Less than 6 Months		More than 6 Months To 24 Months		More than 24 Months To 60 Months		Total	
	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield	Carrying Value	Weighted Average Yield
Agency REMIC CMO Floating Rate	\$ 318,689	5.55%	\$ —	—%	\$ —	—%	\$ 318,689	5.55%
Non-Agency floaters	28,401	5.50%	—	—%	—	—%	28,401	5.50%
NYMT Retained Securities	2,165	6.28%	—	—%	1,229	12.99%	3,394	10.03%
Total/Weighted Average	\$ 349,255	5.55%	\$ —	—%	\$ 1,229	12.99%	\$ 350,484	5.61%

Mortgage Loans Held in Securitization Trusts - Included in our portfolio are ARM loans that we originated or purchased in bulk from third parties that met our investment criteria and portfolio requirements. These loans are classified as “mortgage loans held for investment” during a period of aggregation and until the portfolio reaches a size sufficient for us to securitize such loans. If the securitization qualifies as a financing for SFAS No. 140 purposes, the loans are then re-classified as “mortgage loans held in securitization trusts.”

New York Mortgage Trust 2006-1, qualified as a sale under SFAS No. 140, which resulted in the recording of residual assets and mortgage servicing rights. As of June 30, 2008 the residual assets totaled \$0.4 million and are included in investment securities available for sale.

The following table details mortgage loans held in securitization trusts at June 30, 2008 (dollar amounts in thousands):

	Par Value	Coupon	Carrying Value	Yield
June 30, 2008	\$ 377,336	5.68%	\$ 376,984	5.19%

At June 30, 2008 mortgage loans held in securitization trusts totaled approximately \$377.0 million, or 42% of our total assets. Of this mortgage loan investment portfolio, 100% are traditional ARMs or hybrid ARMs and 78% are ARM loans that are interest only. On our hybrid ARMs, interest rate reset periods are predominately five years or less and the interest-only/amortization period is typically 10 years, which mitigates the “payment shock” at the time of interest rate reset. No loans in our investment portfolio of mortgage loans are option-ARMs or ARMs with negative amortization.

The following table sets forth the composition of our portfolio of mortgage loans held in securitization trusts and retained interests in our REMIC securitization, NYMT 2006-1, as of June 30, 2008 (dollar amounts in thousands):

	# of Loans	Par Value	Carrying Value
Loan Characteristics:			
Mortgage loans held in securitization trusts	847	\$ 377,336	\$ 376,984
Retained interest in securitization (included in Investment securities available for sale)	359	191,556	2,555
Total Loans Held	1,206	\$ 568,892	\$ 379,539

	Average	High	Low
General Loan Characteristics:			
Original Loan Balance	\$ 494	\$ 3,500	\$ 48
Coupon Rate	5.76%	9.88%	3.88%
Gross Margin	2.34%	6.50%	1.13%
Lifetime Cap	11.21%	13.75%	9.13%
Original Term (Months)	360	360	360
Remaining Term (Months)	325	333	289
Average Months to Reset	20	30	1
Original Average FICO Score	737	820	593
Original Average LTV	69.9	95.0	10.9

The following table details loan summary information for loans held in securitization trust at June 30, 2008 (dollar amounts in thousands)

Property Type	Description	Loan Balance	Loan Count	Interest Rate %			Final Maturity		Periodic Payment Term (months)	Prior Delinquencies	Face Amount of Mortgage	Carrying Amount of Mortgage	Principal amount of loans subject to
				Max	Min	Avg	Min	Max					
Single	<= \$100	13	7.75	4.75	5.60	12/01/34	11/01/35	360	NA	\$ 1,870	\$ 917	\$ 69	
Family	\$ <=250	95	8.50	4.75	5.73	09/01/32	12/01/35	360	NA	18,125	17,035	246	
	<= \$500	149	7.63	4.25	5.66	09/01/32	01/01/36	360	NA	54,596	52,110	500	
	<= \$1,000	69	9.50	4.13	5.89	07/01/33	12/01/35	360	NA	50,461	48,385	3,652	
	> \$1,000	37	7.75	4.00	5.74	06/01/34	01/01/36	360	NA	65,127	64,488	1,999	
	Summary	363	9.50	4.00	5.73	09/01/32	01/01/36	360	NA	\$ 190,179	\$ 182,935	\$ 6,466	
2-4 FAMILY	<= \$100	1	6.63	6.63	6.63	02/01/35	02/01/35	360	NA	\$ 80	\$ 77	\$ -	
	<= \$250	6	6.75	4.38	5.75	12/01/34	07/01/35	360	NA	1,115	1,028	-	
	<= \$500	22	7.25	4.63	5.74	09/01/34	01/01/36	360	NA	8,110	7,924	-	
	<= \$1,000	4	7.25	5.38	6.31	10/01/35	10/01/35	360	NA	3,068	3,050	517	
	> \$1,000	1	5.63	5.63	5.63	12/01/34	08/01/35	360	NA	2,600	2,600	-	
	Summary	34	7.25	4.38	5.83	09/01/34	01/01/36	360	NA	\$ 14,973	\$ 14,679	\$ 517	
Condo	<= \$100	18	6.63	4.38	5.68	01/01/35	12/01/35	360	NA	\$ 2,368	\$ 1,294	\$ -	
	<= \$250	94	7.88	4.50	5.72	08/01/32	01/01/36	360	NA	18,313	17,118	229	
	<= \$500	102	8.13	4.00	5.60	09/01/32	12/01/35	360	NA	36,070	35,091	1,031	
	<= \$1,000	37	7.75	4.13	5.46	08/01/33	11/01/35	360	NA	27,137	25,379	-	
	> \$1,000	15	6.13	4.88	5.48	07/01/34	09/01/35	360	NA	24,568	22,091	-	
	Summary	266	8.13	4.00	5.62	08/01/32	01/01/36	360	NA	\$ 108,456	\$ 100,973	\$ 1,260	
CO-OP	<= \$100	5	7.25	4.75	6.00	09/01/34	06/01/35	360	NA	\$ 842	\$ 276	\$ -	
	<= \$250	25	7.13	4.00	5.51	10/01/34	12/01/35	360	NA	4,782	4,431	-	
	<= \$500	51	7.75	3.88	5.51	08/01/34	12/01/35	360	NA	20,640	19,205	-	
	<= \$1,000	30	6.75	4.75	5.35	11/01/34	11/01/35	360	NA	22,254	21,360	-	
	> \$1,000	6	6.00	4.75	5.25	11/01/34	12/01/35	360	NA	8,664	8,488	-	
	Summary	117	7.75	3.88	5.44	08/01/34	12/01/35	360	NA	\$ 57,182	\$ 53,760	\$ -	
PUD	<= \$100	2	5.63	5.25	5.44	07/01/35	07/01/35	360	NA	\$ 438	\$ 186	\$ -	
	<= \$250	28	7.75	4.38	5.70	01/01/35	12/01/35	360	NA	5,578	5,187	-	
	<= \$500	24	9.88	4.38	6.40	08/01/32	12/01/35	360	NA	8,850	8,301	-	
	<= \$1,000	9	7.50	4.75	5.72	09/01/33	12/01/35	360	NA	6,196	6,102	856	
	> \$1,000	4	6.22	5.63	5.96	04/01/34	12/01/35	360	NA	5,233	5,213	-	
	Summary	67	9.88	4.38	5.96	08/01/32	01/01/36	360	NA	\$ 26,295	\$ 24,989	\$ 856	
Summary	<= \$100	39	7.75	4.38	5.71	09/01/34	12/01/35	360	NA	\$ 5,598	\$ 2,750	\$ 69	
	<= \$250	248	8.50	4.00	5.70	08/01/32	01/01/36	360	NA	47,913	44,799	475	
	<= \$500	348	9.88	3.88	5.66	08/01/32	01/01/36	360	NA	128,266	122,631	1,531	
	<= \$1,000	149	9.50	4.13	5.68	07/01/33	12/01/35	360	NA	109,116	104,276	5,025	
	> \$1,000	63	7.75	4.00	5.64	04/01/34	01/01/36	360	NA	106,192	102,880	1,999	
	Grand Total	847	9.88	3.88	5.68	08/01/32	01/01/36	360	NA	\$ 397,085	\$ 377,336	\$ 9,099	

The following table details activity for loans held in securitization trust for the six months ended June 30, 2008.

	Principal	Premium	Loan Reserve	Net Carrying Value
Balance, January 1, 2008	\$ 429,629	\$ 2,733	\$ (1,647)	\$ 430,715
Additions	-	-	-	-
principal repayments	(52,293)	-	-	(52,293)
Reserve for loan loss	-	-	(1,455)	(1,455)
Charge offs	-	-	364	364
Amortization for premium	-	(347)	-	(347)
Balance, June 30, 2008	\$ 377,336	\$ 2,386	\$ (2,738)	\$ 376,984

Cash and cash equivalents - We had unrestricted cash and cash equivalents of \$4.9 million at June 30, 2008 versus \$5.5 million at December 31, 2007.

Restricted Cash - Restricted cash includes amounts held by counterparties as collateral for hedging instruments, amounts held as collateral for three letters of credit related to the Company's lease of office space, including its corporate headquarters, and amounts held in an escrow account to support warranties and indemnifications related to the sale of the retail mortgage lending platform to IndyMac.

Accounts and accrued interest receivable - Accounts and accrued interest receivable includes accrued interest receivable for investment securities and mortgage loans held in securitization trusts are also included.

Prepaid and other assets - Prepaid and other assets totaled \$2.3 million as of June 30, 2008. Prepaid and other assets consist mainly of \$1.2 million of capitalization expenses related to equity and bond issuance cost. These costs are being amortized into earnings over time related to the maturity of the underlying issuance. In addition, \$0.3 million of capitalization servicing costs related to our fourth securitization has been accounted for as a sale.

Assets Related to Discontinued Operations:

Mortgage Loans Held for Sale - Mortgage loans that we have originated but do not intend to hold for investment and are held pending sale to investors are classified as mortgage loans held for sale. We had mortgage loans held for sale (net) of \$6.2 million at June 30, 2008 as compared to \$8.1 million at December 31, 2007.

Balance Sheet Analysis - Financing Arrangements

Financing Arrangements, Portfolio Investments - As of June 30, 2008, there were approximately \$417.9 million of repurchase borrowings outstanding. Our repurchase agreements typically have terms of 30 days or less. As of June 30, 2008, the current weighted average borrowing rate on these financing facilities was 2.60%.

Collateralized Debt Obligations - As of June 30, 2008 we have CDOs outstanding of approximately \$365.2 million with an average interest rate of 2.87%.

Subordinated Debentures - As of December 31, 2007, we have trust preferred securities outstanding of \$45.0 million. The securities are fully guaranteed by the Company with respect to distributions and amounts payable upon liquidation, redemption or repayment. These securities are classified as subordinated debentures in the liability section of our balance sheet.

Convertible Preferred Debentures - As of June 30, 2008, there were 1.0 million shares of our Series A Preferred Stock outstanding, with an aggregate redemption value of \$20.0 million. We issued these shares on January 18, 2008 to JMP Group, Inc. and certain of its affiliates for an aggregate purchase price of \$20.0 million. The Series A Preferred Stock entitles the holders to receive a cumulative dividend of 10% per year, subject to an increase to the extent any future quarterly common stock dividends exceed \$0.20 per share. The Series A Preferred Stock is convertible into shares of our common stock based on a conversion price of \$8.00 per share of common stock, which represents a conversion rate of two and one-half (2 1/2) shares of common stock for each share of Series A Preferred Stock. The Series A Preferred Stock matures on December 31, 2010, at which time any outstanding shares must be redeemed by us at the \$20.00 per share liquidation preference. Pursuant to SFAS No. 150, because of this mandatory redemption feature, we classify these securities as convertible preferred debentures in the liability section of our balance sheet.

Derivative Assets and Liabilities - We generally attempt to hedge only the risk related to changes in the interest rates, usually a London Interbank Offered Rate, known as LIBOR, or a U.S. Treasury rate.

In order to mitigate these risks, we enter into interest rate swap agreements whereby we receive floating rate payments in exchange for fixed rate payments, effectively converting the borrowing to a fixed rate. We also enter into interest rate cap agreements whereby, in exchange for a fee, we are reimbursed for interest paid in excess of a contractually specified capped rate.

Derivative financial instruments contain credit risk to the extent that the institutional counterparties may be unable to meet the terms of the agreements. We minimize this risk by using multiple counterparties and limiting our counterparties to major financial institutions with good credit ratings. In addition, we regularly monitor the potential risk of loss with any one party resulting from this type of credit risk. Accordingly, we do not expect any material losses as a result of default by other parties.

We enter into derivative transactions solely for risk management purposes and not for speculation. The decision of whether or not a given transaction (or portion thereof) is hedged is made on a case-by-case basis, based on the risks involved and other factors as determined by senior management, including the financial impact on income and asset valuation and the restrictions imposed on REIT hedging activities by the Internal Revenue Code, among others. In determining whether to hedge a risk, we may consider whether other assets, liabilities, firm commitments and anticipated transactions already offset or reduce the risk. All transactions undertaken as a hedge are entered into with a view towards minimizing the potential for economic losses that could be incurred by us. Generally, all derivatives entered into are intended to qualify as hedges in accordance with GAAP, unless specifically precluded under SFAS No. 133, *Accounting for Derivatives Instruments and Hedging Activities*. To this end, the terms of the hedges are matched closely to the terms of the hedged items.

During the six months ended June 30, 2008, the Company terminated a total of \$517.7 million of notional interest rate swaps resulting in a realized loss of \$4.8 million.

The following table summarizes the estimated fair value of derivative assets as of June 30, 2008 and December 31, 2007 (dollar amounts in thousands):

	June 30, 2008	December 31, 2007
Derivative Assets:		
Interest rate caps	\$ 355	\$ 416
Interest rate swaps	2,085	—
Total derivative assets	\$ 2,440	\$ 416
Derivative Liabilities:		
Interest rate swaps	\$ —	\$ 3,517
Total derivative liabilities	\$ —	\$ 3,517

Balance Sheet Analysis - Stockholders' Equity

Stockholders' equity at June 30, 2008 was \$41.9 million and included \$12.4 million of net unrealized losses on available for sale securities and cash flow hedges presented as accumulated other comprehensive loss.

On February 21, 2008, the Company completed the issuance and sale of 7.5 million shares of its common stock in a private placement at a price of \$8.00 per share. This private offering of the Company's common stock generated net proceeds to the Company of \$56.6 million after payment of private placement fees and expenses. In connection with the private offering of our common stock, we entered into a registration rights agreement (the "Common Stock Registration Rights Agreement"), pursuant to which we were required, among other things, to file with the SEC a resale shelf registration statement registering for resale the 7.5 million shares sold in this private offering on or before March 12, 2008 and obtain listing for our common stock on the NASDAQ Stock Market on or before the effective date of the resale shelf registration statement. In the event we fail to satisfy these requirements, we may be subject to payment of liquidated damages to the investors in the transaction. We filed the resale shelf registration statement registering the resale of the 7.5 million shares on April 4, 2008, which became effective on April 18, 2008. As a result, we incurred a penalty fee (liquidated damages) of approximately \$0.2 million, which was paid on May 2, 2008. The Company obtained listing on the NASDAQ effective June 4, 2008; we incurred a penalty fee (liquidated damages) of approximately \$0.5 million, which was paid on July 3, 2008.

Prepayment Experience

The cumulative prepayment rate ("CPR") on our mortgage portfolio averaged approximately 14% during the three months ended June 30, 2008 as compared to 21% for the three months ended June 30, 2007. CPRs on our purchased portfolio of investment securities averaged approximately 9% while the CPRs on mortgage loans held in our securitization trusts averaged approximately 22% during the three months ended June 30, 2008. The CPR on our mortgage portfolio averaged 15% for the three months ended December 31, 2007. When prepayment expectations over the remaining life of assets increase, we have to amortize premiums over a shorter time period resulting in a reduced yield to maturity on our investment assets. Conversely, if prepayment expectations decrease, the premium would be amortized over a longer period resulting in a higher yield to maturity. We monitor our prepayment experience on a monthly basis and adjust the amortization of our net premiums accordingly.

Results of Operations

Our results of operations for our mortgage portfolio during a given period typically reflect the net interest spread earned on our investment portfolio of residential mortgage loans and mortgage-backed securities. The net interest spread is impacted by factors such as our cost of financing, the interest rate our investments are earning and our interest hedging strategies. Furthermore, the amount of premium or discount paid on purchased portfolio investments and the prepayment rates on portfolio investments will impact the net interest spread as such factors will be amortized over the expected term of such investments.

Other Operational Information

	2008	June 30 2007	% Change
Employees	6	12	(50.0)%

Comparative Net Income (Loss) (dollars in thousands)

	for the three months ended June 30,			for the six months ended June 30,		
	2008	2007	Difference	2008	2007	Difference
Net interest income on investment portfolio	\$ 3,964	\$ 1,006	\$ 2,958	\$ 6,703	\$ 1,635	\$ 5,068
Net interest income	2,499	112	2,387	3,773	(141)	3,914
Loan losses	(22)	(940)	918	(1,455)	(940)	(515)
Loss on securities and related hedges	(83)	(3,821)	3,738	(19,931)	(3,821)	(16,110)
Total Expenses	1,960	529	1,431	3,391	1,176	2,215
Income (loss) from continuing operations	434	(5,178)	5,612	(21,004)	(6,078)	(14,926)
Loss from discontinued operations - net of tax	829	(9,018)	9,847	1,009	(12,859)	13,868
Net Income (loss)	\$ 1,263	\$ (14,196)	\$ 15,459	\$ (19,995)	\$ (18,937)	\$ (1,058)
EPS Basic and Diluted	\$ 0.14	\$ (7.84)	\$ 7.98	\$ (2.77)	\$ (10.46)	\$ 7.69

For the three months ended June 30, 2008, we reported net income of \$1.3 million, as compared to a net loss of \$14.2 million for the three months ended June 30, 2007. The increase in net income of \$15.4 million is primarily due to the improvement in net interest margin of \$2.4 million, \$3.7 million decrease in realized loss on securities and related hedges, and a \$9.8 million improvement on earnings from the discontinued operations as a result of exiting the lending business on March 31, 2007. For the six months ended June 30, 2008, we reported a net loss of \$20.0 million, as compared to a net loss of \$18.9 million for the six months ended June 30, 2007.

Expenses increased by approximately \$1.4 million to \$2.0 million for three months ended June 30, 2008 as compared to the same period in 2007. Of this increase in expenses, approximately \$0.7 million was the result of allocating to the Company 100% of the salaries and benefits payable to the Company's employees, as well as certain professional fees. Previously, these expenses had been allocated to both the continuing and discontinued operations of the Company. The remaining increase in expenses was due primarily to an increase of approximately \$0.9 million in other expenses, which included \$0.2 million in management fees payable to JMPAM pursuant to the advisory agreement and \$0.5 million in penalty fees paid to certain holders of the Company's common stock pursuant to the Common Stock Registration Rights Agreement.

Expenses increased by approximately \$2.2 million to \$3.4 million for six months ended June 30, 2008 as compared to the same period in 2007. Of this increase in expenses, approximately \$1.1 million was the result of the re-allocation of expenses between the continuing and discontinued operations, as described above. The remaining increase in expenses was due primarily to an increase of approximately \$1.4 million in other expenses, which included \$0.3 million in management fees payable to JMPAM pursuant to the advisory agreement and \$0.7 million in penalty fees paid pursuant to the Common Stock Registration Rights Agreement.

Comparative Net Interest Income

The following table sets forth the changes in net interest income, yields earned on mortgage loans and securities and rates on financial arrangements for the three and six months ended June 30, 2008 and 2007 (dollar amounts in thousands, except as noted):

	For the Three Months Ended June 30,					
	2008			2007		
	Average Balance (\$ Millions)	Amount	Yield/ Rate	Average Balance (\$ Millions)	Amount	Yield/ Rate
Interest income:						
Investment securities and loans held in the securitization trusts	\$ 897.5	\$ 10,912	4.86%	\$ 945.4	\$ 13,388	5.77%
Amortization of net premium	1.8	(157)	(0.08)%	3.2	(490)	(0.22)%
Interest income/weighted average	\$ 899.3	\$ 10,755	4.78%	948.6	\$ 12,898	5.55%
Interest expense:						
Investment securities and loans held in the securitization trusts	\$ 800.9	\$ 6,791	3.35%	\$ 876.4	\$ 11,892	4.04%
Subordinated debentures	45.0	896	7.88%	45.0	894	7.95%
Convertible preferred debentures	20.0	569	11.25%	—	—	—%
Interest expense/weighted average	\$ 865.9	\$ 8,256	3.77%	\$ 921.4	\$ 12,786	5.55%
Net interest income/weighted average		\$ 2,499	1.01%		\$ 112	0.00%

	For the Six Months Ended June 30,					
	2008			2007		
	Average Balance (\$ Millions)	Amount	Yield/ Rate	Average Balance (\$ Millions)	Amount	Yield/ Rate
Interest income:						
Investment securities and loans held in the securitization trusts	\$ 958.5	\$ 24,258	5.06%	\$ 981.7	\$ 27,602	5.62%
Amortization of net premium	0.8	(250)	(0.05)%	4.0	(991)	(0.16)%
Interest income/weighted average	\$ 959.3	\$ 24,008	5.01%	985.70	\$ 26,611	5.46%
Interest expense:						
Investment securities and loans held in the securitization trusts	\$ 879.1	\$ 17,305	3.89%	\$ 928.3	\$ 24,976	5.43%

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Subordinated debentures	45.0	1,855	8.15%	45.00	1,776	7.94%
Convertible preferred debentures	20.0	1,075	10.63%	—	—	—%
Interest expense/weighted average	\$ 944.1	\$ 20,235	4.24%	\$ 973.30	\$ 26,752	5.47%
Net interest income/weighted average		\$ 3,773	0.77%		\$ (141)	(0.01)%

The increase in net interest income for both the three months and six months ended June 30, 2008 is due to a more favorable interest rate environment and significant portfolio restructuring in 2008.

The following table sets forth the net interest spread, since inception, for our portfolio of investment securities available for sale, mortgage loans held for investment and mortgage loans held in securitization trusts, excluding the costs of our subordinated debentures.

Quarter Ended	Average Interest Earning Assets (\$ millions)	Weighted Average Coupon	Weighted Average Cash Yield on Interest Earning Assets	Cost of Funds	Net Interest Spread
June 30, 2008	\$ 899.3	4.86%	4.78%	3.35%	1.43%
March 31, 2008	\$ 1,019.2	5.24%	5.20%	4.35%	0.85%
December 31, 2007	\$ 799.2	5.90%	5.79%	5.33%	0.46%
September 30, 2007	\$ 865.7	5.93%	5.72%	5.38%	0.34%
June 30, 2007	\$ 948.6	5.66%	5.55%	5.43%	0.12%
March 31, 2007	\$ 1,022.7	5.59%	5.36%	5.34%	0.02%
December 31, 2006	\$ 1,111.0	5.53%	5.35%	5.26%	0.09%
September 30, 2006	\$ 1,287.6	5.50%	5.28%	5.12%	0.16%
June 30, 2006	\$ 1,217.9	5.29%	5.08%	4.30%	0.78%
March 31, 2006	\$ 1,478.6	4.85%	4.75%	4.04%	0.71%
December 31, 2005	\$ 1,499.0	4.84%	4.43%	3.81%	0.62%
September 30, 2005	\$ 1,494.0	4.69%	4.08%	3.38%	0.70%
June 30, 2005	\$ 1,590.0	4.50%	4.06%	3.06%	1.00%
March 31, 2005	\$ 1,447.9	4.39%	4.01%	2.86%	1.15%
December 31, 2004	\$ 1,325.7	4.29%	3.84%	2.58%	1.26%
September 30, 2004	\$ 776.5	4.04%	3.86%	2.45%	1.41%

Off-Balance Sheet Arrangements

Since inception, we have not maintained any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as structured finance or special purpose entities, established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes. Further, we have not guaranteed any obligations of unconsolidated entities nor do we have any commitment or intent to provide funding to any such entities. Accordingly, we are not materially exposed to any market, credit, liquidity or financing risk that could arise if we had engaged in such relationships.

Liquidity and Capital Resources

Liquidity is a measure of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, fund and maintain investments, fund our operations, pay dividends to our stockholders and other general business needs. We recognize the need to have funds available for our operating businesses and meet these potential cash requirements. Our investments and assets generate liquidity on an ongoing basis through mortgage principal and interest payments, prepayments and net earnings held prior to payment of dividends. In addition, depending on market conditions, the sale of investment securities or capital market transactions may provide additional liquidity. We intend to meet our liquidity needs through normal operations with the goal of avoiding unplanned sales of assets or emergency borrowing of funds. However, in March 2008, news of potential security liquidations by certain of our competitors negatively impacted the market value of certain of the investment securities in our portfolio. In connection with this market disruption and the anticipated increase in collateral requirements by our lenders as a result of such decrease in the market value of such securities, we elected to increase our liquidity by reducing our leverage through the sale of an aggregate of approximately \$592.8 million of Agency MBS in March 2008, which resulted in an aggregate loss of approximately \$17.1 million, including losses related to the termination of interest rate swaps. At June 30, 2008, we had cash balances of \$4.9 million, \$31.6 million in unencumbered securities and borrowings of \$417.9 million under outstanding repurchase agreements. At June 30, 2008, we also had longer-term capital resources, including CDOs outstanding of \$365.2 million and subordinated debt of \$45.0 million. In addition, the Company received net proceeds of \$19.6 million and \$56.6 million from private offerings of its Series A Preferred Stock and common stock, respectively, in January and February 2008. The Series A Preferred Stock is convertible into shares of our common stock based on a conversion price of \$8.00 per share of common stock, which represents a conversion rate of two and one-half (2 ½) shares of common stock for each share of Series A Preferred Stock, and matures on December 31, 2010, at which time any outstanding shares must be redeemed by us at the \$20.00 per share liquidation preference. As of the date of this report, we believe our existing cash balances, funds available under our current repurchase agreements and cash flows from operations will meet our liquidity requirements for at least the next 12 months, absent any significant decline in financing availability or significant increase in cost to obtain financing. However, should further volatility and deterioration in the broader residential mortgage and MBS markets occur in the future, we cannot assure you that our existing sources of liquidity will be sufficient to meet our liquidity requirements during the next 12 months.

We had outstanding repurchase agreements, a form of collateralized short-term borrowing, with seven different financial institutions as of June 30, 2008. These agreements are secured by our mortgage-backed securities and bear interest rates that have historically moved in close relationship to LIBOR. Our borrowings under repurchase agreements are based on the fair value of our mortgage backed securities portfolio. Interest rate changes can have a negative impact on the valuation of these securities, reducing the amount we can borrow under these agreements. Our repurchase agreements allow the counterparties to determine a new market value of the collateral to reflect current market conditions. If a counterparty determines that the value of the collateral has decreased, whether as a result of interest rate changes, concern regarding the fair value of our mortgage-backed securities portfolio, or other liquidity concerns in the credit markets, it may initiate a margin call and require us to either post additional collateral to cover such decrease or repay a portion of the outstanding borrowing, on minimal notice. Moreover, because these lines of financing are not committed, the counterparty can call the loan at any time. In the event an existing counterparty elected to not reset the outstanding balance at its maturity into a new repurchase agreement, we would be required to repay the outstanding balance with proceeds received from a new counterparty or to surrender the mortgage-backed securities that serve as collateral for the outstanding balance. If we are unable to secure financing from a new counterparty and had to surrender the collateral, we would expect to incur a significant loss.

In addition, in response to the March 2008 market disruption, investors and financial institutions that lend in the mortgage securities repurchase market, including the lenders under our repurchase agreements, tightened lending standards in an effort to reduce the leverage of their borrowers. While the haircut required by our lenders increased in 2007, primarily on non-Agency MBS, during March 2008, we experienced further increases in the amount of haircut

required to obtain financing for both our Agency MBS and non-Agency MBS. As of June 30, 2008, our MBS securities portfolio consisted of approximately of \$472.3 million of Agency MBS and \$27.1 million of non-Agency MBS, which was financed with approximately \$417.9 million of repurchase agreement borrowing with an average haircut of 9%. Although average haircuts stabilized in the second quarter, if the haircuts required by our lenders increase again, our profitability and liquidity will be materially adversely affected.

The recent turmoil in the financial markets as it relates to the solvency of major financial institutions, including certain GSEs, has raised concerns that a material adverse development involving one or more major financial institutions could result in lenders reducing our access to funds available under our repurchase agreements. Any failure or anticipated failure of a major financial institution could adversely effect our ability to borrow under repurchase agreements.

To finance our MBS investment portfolio, we generally seek to borrow between eight and 12 times the amount of our equity, however given the current disruptions in the credit markets we have lowered our target leverage to seven to 10 times. At June 30, 2008 our leverage ratio for our MBS investment portfolio, which we define as our outstanding indebtedness under repurchase agreements divided by the sum of total stockholders' equity and the convertible preferred debentures, was 7:1. This definition of the leverage ratio is consistent with the manner in which the credit providers under our repurchase agreements calculate our leverage.

We enter into interest rate swap agreements to extend the maturity of our repurchase agreements as a mechanism to reduce the interest rate risk of the securities portfolio. At June 30, 2008, we had \$158.0 million in notional interest rate swaps outstanding. Should market rates for similar term interest rate swaps drop below the rates we have entered into on our interest rate swaps, we will be required to post additional margin to the swap counterparty, reducing available liquidity. The weighted average maturity of the swaps was 4.3 years at June 30, 2008.

Our ability to sell approximately \$6.2 million, net of loan loss reserve, of mortgage loans we own could adversely affect our profitability as any sale for less than the current reserved balance would result in a loss. Currently, these loans are not financed or pledged.

As it relates to loans sold previously under certain loan sale agreements by our discontinued mortgage lending business, we may be required to repurchase some of those loans or indemnify the loan purchaser for damages caused by a breach of the loan sale agreement. While in the past we complied with the repurchase demands by repurchasing the loan with cash and reselling it at a loss, thus reducing our cash position; more recently we have addressed these requests by negotiating a net cash settlement based on the actual or assumed loss on the loan in lieu of repurchasing the loans. As of June 30, 2008, the amount of repurchase requests outstanding was approximately \$1.5 million, against which we had a reserve of approximately \$0.5 million. We cannot assure you that we will be successful in settling the remaining repurchase demands on favorable terms, or at all. If we are unable to continue to resolve our current repurchase demands through negotiated net cash settlements, our liquidity could be adversely affected. In addition, we may be subject to new repurchase requests from investors with whom we have not settled or with respect to repurchase obligations not covered under the settlement.

On May 2, 2008 and July 3, 2008, pursuant to the Common Stock Registration Rights Agreement, we were required to pay liquidated damage penalties of approximately of \$0.2 million and \$0.5 million respectively. Although we do not expect to incur additional liquidated damages under the Common Stock Registration Rights Agreement, there can be no assurance that we will avoid breaching the liquidated damage provisions in the future.

In April 2008 we declared a first quarter cash dividend of \$0.12 per common share to common stockholders of record of April 30, 2008, that was paid on May 15, 2008. This dividend represented the first dividend paid on shares of our common stock since our Board of Directors elected to suspend the dividend in July 2007. On June 26, 2008, we declared a second quarter cash dividend of \$0.16 per common share to common stockholders of record of July 10, 2008 and was paid on July 25, 2008. On June 26, 2008, we declared a \$0.50 per share cash dividend, or approximately \$0.5 million in the aggregate, on shares of our Series A Preferred Stock to holders of record as of June 30, 2008. We also paid \$0.50 per share cash dividend on shares of our Series A Preferred Stock during the first quarter of 2008. The Series A Preferred Stock entitles the holders to receive a cumulative dividend of 10% per year (or \$0.50 per share per quarter), subject to increase to the extent any future quarterly common stock dividends exceed \$0.10 per share. Each of these dividends was paid out of the Company's working capital. Our board of directors will continue to evaluate our dividend policy each quarter and will make adjustments as necessary, based on a variety of factors, including, among other things, the need to maintain our REIT status, our financial condition, liquidity, earnings projections and business prospects. Our dividend policy does not constitute an obligation to pay dividends, which only occurs when our board of directors declares a dividend.

We intend to make distributions to our stockholders to comply with the various requirements to maintain our REIT status and to minimize or avoid corporate income tax and the nondeductible excise tax. However, differences in timing between the recognition of REIT taxable income and the actual receipt of cash could require us to sell assets or to borrow funds on a short-term basis to meet the REIT distribution requirements and to avoid corporate income tax and the nondeductible excise tax.

Certain of our assets may generate substantial mismatches between REIT taxable income and available cash. These assets could include mortgage-backed securities we hold that have been issued at a discount and require the accrual of

taxable income in advance of the receipt of cash. As a result, our REIT taxable income may exceed our cash available for distribution and the requirement to distribute a substantial portion of our net taxable income could cause us to:

- sell assets in adverse market conditions;
- borrow on unfavorable terms;
- distribute amounts that would otherwise be invested in assets or repayment of debt, in order to comply with the REIT distribution requirements.

Advisory Agreement

On January 18, 2008, we entered into an advisory agreement with JMPAM, pursuant to which JMPAM will advise, manage and make investments on behalf of two of our wholly-owned subsidiaries. Pursuant to the Advisory Agreement, JMPAM is entitled to receive the following compensation:

- base advisory fee equal to 1.50% per annum of the “equity capital” (as defined in Item 1 of this Annual Report) of the Managed Subsidiaries is payable by us to JMPAM in cash, quarterly in arrears; and
- incentive compensation equal to 25% of the GAAP net income of the Managed Subsidiaries attributable to the investments that are managed by JMPAM that exceed a hurdle rate equal to the greater of (a) 8.00% and (b) 2.00% plus the ten year treasury rate for such fiscal year will be payable by us to JMPAM in cash, quarterly in arrears; *provided, however*, that a portion of the incentive compensation may be paid in shares of our common stock.

If we terminate the advisory agreement (other than for cause) or elect not to renew it, we will be required to pay JMPAM a cash termination fee equal to the sum of (i) the average annual base advisory fee and (ii) the average annual incentive compensation earned during the 24-month period immediately preceding the date of termination.

Inflation

For the periods presented herein, inflation has been relatively low and we believe that inflation has not had a material effect on our results of operations.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market risk is the exposure to loss resulting from changes in interest rates, credit spreads, foreign currency exchange rates, commodity prices and equity prices. Because we are invested solely in U.S.-dollar denominated instruments, primarily residential mortgage instruments, and our borrowings are also domestic and U.S. dollar denominated, we are not subject to foreign currency exchange, or commodity and equity price risk; the primary market risk that we are exposed to is interest rate risk and its related ancillary risks. Interest rate risk is highly sensitive to many factors, including governmental monetary and tax policies, domestic and international economic and political considerations and other factors beyond our control. All of our market risk sensitive assets, liabilities and related derivative positions are for non-trading purposes only.

Management recognizes the following primary risks associated with our business and the industry in which we conduct our business:

- Interest rate risk
- Market (fair value) risk
- Credit spread risk
- Liquidity and funding risk
- Prepayment risk
- Credit risk

Interest Rate Risk

Interest rates are sensitive to many factors, including governmental, monetary, tax policies, domestic and international economic conditions, and political or regulatory matters beyond our control. Changes in interest rates affect the value of our MBS and ARM loans we manage and hold in our investment portfolio, the variable-rate borrowings we use to finance our portfolio, and the interest rate swaps and caps we use to hedge our portfolio. All of our interest rate related market risk sensitive assets, liabilities and related derivative positions are managed with a long term perspective and are not for trading purposes.

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Interest rate risk is measured by the sensitivity of our current and future earnings to interest rate volatility, variability of spread relationships, the difference in re-pricing intervals between our assets and liabilities and the effect that interest rates may have on our cash flows, especially the speed at which prepayments occur on our residential mortgage related assets. Changes in interest rates can affect our net interest income, which is the difference between the interest income earned on assets and our interest expense incurred in connection with our borrowings.

Our CMO Floaters have interest rates that adjust monthly, at a margin over LIBOR, as do the repurchase agreement liabilities that we use to finance those Floaters.

Our hybrid ARM assets reset on various dates that are not matched to the reset dates on our repurchase agreements. In general, the repricing of our repurchase agreements occurs more quickly than the repricing of our assets. First, our floating rate borrowings may react to changes in interest rates before our adjustable rate assets because the weighted average next re-pricing dates on the related borrowings may have shorter time periods than that of the ARM assets. Second, interest rates on ARM assets may be limited to a “periodic cap” or an increase of typically 1% or 2% per adjustment period, while our borrowings do not have comparable limitations. Third, our adjustable rate assets typically lag changes in the applicable interest rate indices by 45 days due to the notice period provided to ARM borrowers when the interest rates on their loans are scheduled to change.

We seek to manage interest rate risk in the portfolio by utilizing interest rate swaps, caps and Eurodollar futures, with the goal of optimizing the earnings potential while seeking to maintain long term stable portfolio values. We continually monitor the duration of our mortgage assets and have a policy to hedge the financing such that the net duration of the assets, our borrowed funds related to such assets, and related hedging instruments, are less than one year.

Interest rates can also affect our net return on hybrid ARM securities and loans net of the cost of financing hybrid ARMs. We continually monitor and estimate the duration of our hybrid ARMs and have a policy to hedge the financing of the hybrid ARMs such that the net duration of the hybrid ARMs, our borrowed funds related to such assets, and related hedging instruments are less than one year. During a declining interest rate environment, the prepayment of hybrid ARMs may accelerate (as borrowers may opt to refinance at a lower rate) causing the amount of liabilities that have been extended by the use of interest rate swaps to increase relative to the amount of hybrid ARMs, possibly resulting in a decline in our net return on hybrid ARMs as replacement hybrid ARMs may have a lower yield than those being prepaid. Conversely, during an increasing interest rate environment, hybrid ARMs may prepay slower than expected, requiring us to finance a higher amount of hybrid ARMs than originally forecast and at a time when interest rates may be higher, resulting in a decline in our net return on hybrid ARMs. Our exposure to changes in the prepayment speed of hybrid ARMs is mitigated by regular monitoring of the outstanding balance of hybrid ARMs, and adjusting the amounts anticipated to be outstanding in future periods and, on a regular basis, making adjustments to the amount of our fixed-rate borrowing obligations for future periods.

We utilize a model based risk analysis system to assist in projecting portfolio performances over a scenario of different interest rates. The model incorporates shifts in interest rates, changes in prepayments and other factors impacting the valuations of our financial securities, including mortgage-backed securities, repurchase agreements, interest rate swaps and interest rate caps.

Based on the results of the model, as of June 30, 2008, changes in interest rates would have the following effect on net interest income:

Changes in Net Interest Income	
Changes in Interest Rates (Basis Points)	Changes in Net Interest Income (Dollar amounts in thousands)
+200	\$ (7,986)

+100	\$	(4,095)
-100	\$	4,149

Interest rate changes may also impact our net book value as our mortgage assets and related hedge derivatives are marked-to-market each quarter. Generally, as interest rates increase, the value of our mortgage assets decreases and as interest rates decrease, the value of such investments will increase. In general, we would expect however that, over time, decreases in the value of our portfolio attributable to interest rate changes will be offset, to the degree we are hedged, by increases in value of our interest rate swaps, and vice versa. However, the relationship between spreads on securities and spreads on swaps may vary from time to time, resulting in a net aggregate book value increase or decline. Unless there is a material impairment in value that would result in a payment not being received on a security or loan, changes in the book value of our portfolio will not directly affect our recurring earnings or our ability to make a distribution to our stockholders.

Market (Fair Value) Risk

Changes in interest rates also expose us to market risk that the market (fair) value on our assets may decline. For certain of the financial instruments that we own, fair values will not be readily available since there are no active trading markets for these instruments as characterized by current exchanges between willing parties. Accordingly, fair values can only be derived or estimated for these investments using various valuation techniques, such as computing the present value of estimated future cash flows using discount rates commensurate with the risks involved. However, the determination of estimated future cash flows is inherently subjective and imprecise. Minor changes in assumptions or estimation methodologies can have a material effect on these derived or estimated fair values. These estimates and assumptions are indicative of the interest rate environments as of June 30, 2008, and do not take into consideration the effects of subsequent interest rate fluctuations.

We note that the values of our investments in mortgage-backed securities and in derivative instruments, primarily interest rate hedges on our debt, will be sensitive to changes in market interest rates, interest rate spreads, credit spreads and other market factors. The value of these investments can vary and has varied materially from period to period. Historically, the values of our mortgage loan portfolio have tended to vary inversely with those of its derivative instruments.

The following table presents the Company's financial instruments carried at fair value as of June 30, 2008, on the condensed consolidated balance sheet by the applicable FAS No. 157 valuation hierarchy.

<i>(In Thousands)</i>	Fair Value at June 30, 2008				Total
	Level 1	Level 2	Level 3		
Assets:					
Investment securities - available for sale	\$ —	\$ 499,404	\$ —	\$ —	\$ 499,404
Mortgage loans held for sale (net)	—	—	6,200	—	6,200
Interest Rate Caps	—	355	—	—	355
Interest Rate Swaps	—	2,085	—	—	2,085
Total assets carried at fair value	\$ —	\$ 501,844	\$ 6,200	\$ —	\$ 508,044

The fair value of our mortgage loans held for sale (net) decreased by \$0.4 million during the period that commenced on January 1, 2008 and ended on June 30, 2008. This decrease in fair value of our mortgage loans held for sale (net) is included in loan loss in our discontinued operations.

Any changes to the valuation methodology are reviewed by management to ensure the changes are appropriate. There has been no change in valuation methodology since the previous period. As markets and products develop and the pricing for certain products becomes more transparent, the Company continues to refine its valuation methodologies. The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date. The Company uses inputs that are current as of the measurement date, which may include periods of market dislocation, during which price transparency may be reduced. This condition could cause the Company's financial instruments to be reclassified from Level 2 to Level 3 in the future.

The market risk management discussion and the amounts estimated from the analysis that follows are forward-looking statements that assume that certain market conditions occur. Actual results may differ materially from these projected results due to changes in our portfolio assets and borrowings mix and due to developments in the domestic and global financial and real estate markets. Developments in the financial markets include the likelihood of changing interest

rates and the relationship of various interest rates and their impact on our portfolio yield, cost of funds and cash flows. The analytical methods that we use to assess and mitigate these market risks should not be considered projections of future events or operating performance.

As a financial institution that has only invested in U.S.-dollar denominated instruments, primarily residential mortgage instruments, and has only borrowed money in the domestic market, we are not subject to foreign currency exchange or commodity price risk. Rather, our market risk exposure is largely due to interest rate risk. Interest rate risk impacts our interest income, interest expense and the market value on a large portion of our assets and liabilities. In managing interest rate risk, we attempt to maximize earnings and to preserve capital by minimizing the negative impacts of changing market rates, asset and liability mix, and prepayment activity.

The table below presents the sensitivity of the market value changes of our portfolio using a discounted cash flow simulation model. Application of this method results in an estimation of the fair market value change of our assets, liabilities and hedging instruments per 100 basis point (“bp”) shift in interest rates, as well as this same value expressed in years - a measure commonly referred to as duration. Positive portfolio duration indicates that the market value of the total portfolio will decline if interest rates rise and increase if interest rates decline. The closer duration is to zero, the less interest rate changes are expected to affect earnings.

The use of hedging instruments is a critical part of our interest rate risk management strategies, and the effects of these hedging instruments on the market value of the portfolio are reflected in the model's output. This analysis also takes into consideration the value of options embedded in our mortgage assets including constraints on the re-pricing of the interest rate of assets resulting from periodic and lifetime cap features, as well as prepayment options. Assets and liabilities that are not interest rate-sensitive such as cash, payment receivables, prepaid expenses, payables and accrued expenses are excluded.

Changes in assumptions including, but not limited to, volatility, mortgage and financing spreads, prepayment behavior, defaults, as well as the timing and level of interest rate changes will affect the results of the model. Therefore, actual results are likely to vary from modeled results.

Changes in Interest Rates	Market Value Changes Changes in Market Value	Net Duration
(Basis Points)	(Dollar amounts in thousands)	(Years)
+200	(23,953)	0.97
+100	(10,740)	0.40
Base	—	0.19
-100	6,715	(0.14)

It should be noted that the model is used as a tool to identify potential risk in a changing interest rate environment but does not include any changes in portfolio composition, financing strategies, market spreads or changes in overall market liquidity.

Based on the assumptions used, the model output suggests a very low degree of portfolio price change given increases in interest rates, which implies that our cash flow and earning characteristics should be relatively stable for comparable changes in interest rates.

Although market value sensitivity analysis is widely accepted in identifying interest rate risk, it does not take into consideration changes that may occur such as, but not limited to, changes in investment and financing strategies, changes in market spreads and changes in business volumes. Accordingly, we make extensive use of an earnings simulation model to further analyze our level of interest rate risk.

There are a number of key assumptions in our earnings simulation model. These key assumptions include changes in market conditions that affect interest rates, the pricing of ARM products, the availability of investment assets and the

availability and the cost of financing for portfolio assets. Other key assumptions made in using the simulation model include prepayment speeds and management's investment, financing and hedging strategies, and the issuance of new equity. We typically run the simulation model under a variety of hypothetical business scenarios that may include different interest rate scenarios, different investment strategies, different prepayment possibilities and other scenarios that provide us with a range of possible earnings outcomes in order to assess potential interest rate risk. The assumptions used represent our estimate of the likely effect of changes in interest rates and do not necessarily reflect actual results. The earnings simulation model takes into account periodic and lifetime caps embedded in our assets in determining the earnings at risk.

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Credit Spread Risk

The mortgage-backed securities we currently, and will in the future, own are also subject to spread risk. The majority of these securities will be adjustable-rate securities that are valued based on a market credit spread to U.S. Treasury security yields. In other words, their value is dependent on the yield demanded on such securities by the market based on their credit relative to U.S. Treasury securities. Excessive supply of such securities combined with reduced demand will generally cause the market to require a higher yield on such securities, resulting in the use of a higher or wider spread over the benchmark rate (usually the applicable U.S. Treasury security yield) to value such securities. Under such conditions, the value of our securities portfolio would tend to decline. Conversely, if the spread used to value such securities were to decrease or tighten, the value of our securities portfolio would tend to increase. Such changes in the market value of our portfolio may affect our net equity, net income or cash flow directly through their impact on unrealized gains or losses on available-for-sale securities, and therefore our ability to realize gains on such securities, or indirectly through their impact on our ability to borrow and access capital.

Furthermore, shifts in the U.S. Treasury yield curve, which represents the market's expectations of future interest rates, would also affect the yield required on our securities and therefore their value. These shifts, or a change in spreads, would have a similar effect on our portfolio, financial position and results of operations.

Liquidity and Funding Risk

Liquidity is a measure of our ability to meet potential cash requirements, including ongoing commitments to repay borrowings, meet margin requirements, fund and maintain investments, pay dividends to our stockholders and meet other general business needs. We recognize the need to have funds available for our operating. It is our policy to have adequate liquidity at all times. We plan to meet liquidity through normal operations with the goal of avoiding unplanned sales of assets or emergency borrowing of funds.

As it relates to our investment portfolio, derivative financial instruments we use also subject us to “margin call” risk based on their market values. Under our interest rate swaps, we pay a fixed rate to the counterparties while they pay us a floating rate. When floating rates are low, on a net basis we pay the counterparty and visa-versa. In a declining interest rate environment, we would be subject to additional exposure for cash margin calls due to accelerating prepayments of mortgage assets. However, the asset side of the balance sheet should increase in value in a further declining interest rate scenario. Most of our interest rate swap agreements provide for a bi-lateral posting of margin, the effect being that either swap party must post margin, depending on the change in value of the swap over time. Unlike typical unilateral posting of margin only in the direction of the swap counterparty, this provides us with additional flexibility in meeting our liquidity requirements as we can call margin on our counterparty as swap values increase.

Incoming cash on our mortgage loans and securities is a principal source of cash. The volume of cash depends on, among other things, interest rates. The volume and quality of such incoming cash flows can be impacted by severe and immediate changes in interest rates. If rates increase dramatically, our short-term funding costs will increase quickly. While many of our Agency securities are hybrid ARMs, they typically will not reset as quickly as our funding costs creating a reduction in incoming cash flow. Our derivative financial instruments are used to mitigate the effect of interest rate volatility.

We manage liquidity to ensure that we have the continuing ability to maintain cash flows that are adequate to meet commitments on a timely and cost-effective basis. Our principal sources of liquidity are the repurchase agreement market, the issuance of CDOs, loan warehouse facilities, principal and interest payments from portfolio assets and, when market conditions permit, the issuance of common or preferred equity.

Prepayment Risk

When borrowers repay the principal on their mortgage loans before maturity or faster than their scheduled amortization, the effect is to shorten the period over which interest is earned, and therefore, reduce the cash flow and yield on our ARM assets. Furthermore, prepayment speeds exceeding or lower than our reasonable estimates for similar assets, impact the effectiveness of any hedges we have in place to mitigate financing and/or fair value risk. Generally, when market interest rates decline, borrowers have a tendency to refinance their mortgages. The higher the interest rate a borrower currently has on his or her mortgage the more incentive he or she has to refinance the mortgage when rates decline. Additionally, when a borrower has a low loan-to-value ratio, he or she is more likely to do a “cash-out” refinance. Each of these factors increases the chance for higher prepayment speeds during the term of the loan.

We mitigate prepayment risk by constantly evaluating our ARM portfolio at a range of reasonable market prepayment speeds observed at the time for assets with a similar structure, quality and characteristics. In addition, we utilize prepayment models to assist in evaluating our hedging strategy.

For the three months ended June 30, 2008, our mortgage assets paid down at an approximate average annualized constant paydown rate (“CPR”) of 14%, compared to 21% for the comparable period in 2007 and 15% for the quarter ended December 31, 2007. When prepayment experience increases, we have to amortize our premiums over a shorter time period, resulting in a reduced yield to maturity on our ARM assets. Conversely, if actual prepayment experience decreases, we would amortize the premium over a longer time period, resulting in a higher yield to maturity. We monitor our prepayment experience on a monthly basis and adjust the amortization of the net premium, as appropriate.

Credit Risk

Credit risk is the risk that we will not fully collect the principal we have invested in our MBS or mortgage loans held in securitization trusts. The Company minimizes the principal risk related to MBS securities by focusing its investment strategy on Agency MBS as well as the highest rated securities for non-Agency securities. As of June 30, 2008 the Company had \$499.4 million in MBS securities of which 94.7% were Agency MBS and 5.2% were rated AAA.

With regard to loans included in our securitization trusts, factors such as FICO score, LTV, debt-to-income ratio, and other borrower and collateral factors were evaluated. Credit enhancement features, such as mortgage insurance were also factored into the credit decision. In some instances, when the borrower exhibited strong compensating factors, exceptions to the underwriting guidelines were approved.

Our mortgage loans held in securitization trusts are concentrated in geographic markets that are generally supply constrained. We believe that these markets have less exposure to sudden declines in housing values than those markets which have an oversupply of housing.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures - We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934, as amended, is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and that such information is accumulated and communicated to our management as appropriate to allow timely decisions regarding required disclosures. An evaluation was performed under the supervision and with the participation of our management, including our Co-Chief Executive Officers and our Chief Financial Officer, of the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) as of June 30, 2008. Based upon that evaluation, our management, including our Co-Chief Executive Officers and our Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of June 30, 2008.

Changes in Internal Control over Financial Reporting – There has been no change in our internal control over financial reporting during the quarter ended June 30, 2008 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II: OTHER INFORMATION

Item 1. Legal Proceedings.

As previously disclosed in our Annual Report on Form 10-K for the year ended December 31, 2007, Steven B. Yang and Christopher Daubiere (“Plaintiffs”), filed suit in the United States District Court for the Southern District of New York against HC and us on December 13, 2006, alleging that we failed to pay them, and similarly situated employees, overtime in violation of the Fair Labor Standards Act (“FLSA”) and New York State law. The Plaintiffs, each of whom were former employees in our discontinued mortgage lending business, purported to bring a FLSA “collective action” on behalf of similarly situated loan officers in our now discontinued mortgage lending business and sought unspecified amounts for alleged unpaid overtime wages, liquidated damages, attorney’s fees and costs.

On December 30, 2007 we entered into an agreement in principle with the Plaintiffs to settle this suit. On June 2, 2008, the court granted a preliminary approval of settlement and authorized notification to plaintiffs and set a fairness hearing for September 18, 2008. As part of the preliminary settlement, we funded the settlement in the amount of \$1.4 million into an escrow account for the Plaintiffs. The amount was previously reserved and expensed in the year ended December 31, 2007.

Item 1A. Risk Factors

We previously disclosed risk factors under "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2007 and Part II. "Item 1A. Risk Factors " in our Quarterly Report on Form 10-Q for the three months ended March 31, 2008. In addition to those risk factors and the other information included elsewhere in this report, you should also carefully consider the risk factor discussed below. The risks described below and in our Annual Report on Form 10-K for the year ended December 31, 2007 and our Quarterly Report on Form 10-Q for the three months ended March 31, 2008 are not the only risks facing our company. Additional risks and uncertainties not currently known to us or that we deem to be immaterial also may materially adversely affect our business, financial condition and/or results of operations.

Since we invest in Agency MBS that are guaranteed by Fannie Mae and Freddie Mac, we are subject to the risk that these U.S. Government-sponsored entities may not be able to fully satisfy their guarantee obligations, which may adversely affect the value of our investment portfolio and our ability to sell or finance these securities.

The payments we receive on the Agency MBS in which we invest are guaranteed by Fannie Mae or Freddie Mac. Unlike the securities issued by Ginnie Mae, the principal and interest on securities issued by Fannie Mae and Freddie Mac are not guaranteed by the U.S. Government. The recent economic challenges in the residential mortgage market have affected the financial results of Fannie Mae and Freddie Mac. For the year ended December 31, 2007 and the six months ended June 30, 2008, both Fannie Mae and Freddie Mac reported substantial losses and have reported significant difficulties stemming from current market disruptions. Fannie Mae recently stated that it expects losses on guarantees of agency securities to continue and expects significant increases in credit-related expenses and credit losses through 2008. Freddie Mac has warned that it may not have enough capital to cover its mandatory reserves for mortgage commitments. If Fannie Mae and Freddie Mac continue to suffer significant losses, their ability to honor their respective Agency securities guarantees may be adversely affected. Further, any actual or perceived financial challenges at either Fannie Mae or Freddie Mac could cause rating agencies to downgrade the corporate credit ratings of Fannie Mae or Freddie Mac. Moody’s Investor Services, or Moody’s, Bank Financial Strength Rating, or BFSR, measures the likelihood that a financial institution will require financial assistance. In May 2008, Moody’s downgraded Freddie Mac’s A- BFSR to B+ and downgraded Fannie Mae’s B+ BFSR to B. On July 13, 2008, in connection with increased market uncertainty regarding Fannie Mae and Freddie Mac, the U.S. Department of the Treasury announced a proposal to make substantial equity investments in, and extend the lines of credit available to, Fannie Mae and Freddie Mac. In a separate announcement on the same day, the Federal Reserve indicated it would make one of its

short-term lending programs available to each of Fannie Mae and Freddie Mac. Any failure to honor guarantees on agency securities by Fannie Mae or Freddie Mac or any downgrade of securities issued by Fannie Mae or Freddie Mac by the Rating Agencies could cause a significant decline in the cash flow from, and the value of, any Agency MBS we may own, and we may then be unable to sell or finance Agency MBS on favorable terms or at all.

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

The Company held its 2008 annual meeting of stockholders on June 12, 2008. The following are the matters considered and voted upon at the annual meeting:

Election of Directors

Name	Term Expires	Number of Shares For	Number of Shares Withheld
Steven M. Abreu	2009	20,102,351	88,583
David A. Akre	2009	20,026,882	164,052
David R. Bock	2009	20,103,390	87,544
James J. Fowler	2009	20,102,276	88,658
Alan L. Hailey	2009	20,103,230	87,704
Steven R. Mumma	2009	20,027,687	163,247
Steven G. Norcutt	2009	20,103,398	87,536

Stockholders also ratified and approved the appointment of Deloitte & Touche LLP as the Company's independent registered public accounting firm for the fiscal year ending December 31, 2008: 18,669,262 shares voted in favor; 16,589 shares voted against and 4,958 shares abstained.

Item 6. Exhibits

The information set forth under "Exhibit Index" below is incorporated herein by reference.

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.

NEW YORK MORTGAGE TRUST, INC.

Date: August 11, 2008

By:

/s/ David A. Akre
David A. Akre
Co-Chief Executive Officer

Date: August 11, 2008

By:

/s/ Steven R. Mumma
Steven R. Mumma
Chief Financial Officer

EXHIBIT INDEX

No.	Description
3.1(a)	Articles of Amendment and Restatement of the Registrant (incorporated by reference to Exhibit 3.01 to our Registration Statement on Form S-11/A filed on June 18, 2004 (Registration No. 333-111668)).
3.1(b)	Articles of Amendment of the Registrant (incorporated by reference to Exhibit 3.1 to our Current Report on Form 8-K filed on October 4, 2007.)
3.1(c)	Articles of Amendment of the Registrant (incorporated by reference to Exhibit 3.2 to our Current Report on Form 8-K filed on October 4, 2007.)
3.1(d)	Articles of Amendment of the Registrant (incorporated by reference to Exhibit 3.1(d) to our Current Report on Form 8-K filed on May 16, 2008.)
3.1(e)	Articles of Amendment of the Registrant (incorporated by reference to Exhibit 3.1(e) to our Current Report on Form 8-K filed on May 16, 2008.)
3.2(a)	Bylaws of the Registrant (incorporated by reference to Exhibit 3.02 to our Registration Statement on Form S-11/ A filed on June 18, 2004 (Registration No. 333-111668)).
3.2(b)	Amendment No. 1 to Bylaws of Registrant (incorporated by reference to Exhibit 3.2(b) to Registrant's Annual Report on Form 10-K filed on March 16, 2006)
4.1	Form of Common Stock Certificate (incorporated by reference to Exhibit 4.01 to our Registration Statement on Form S-11/ A filed on June 18, 2004 (Registration No. 333-111668)).
4.2(a)	Junior Subordinated Indenture between The New York Mortgage Company, LLC and JPMorgan Chase Bank, National Association, as trustee, dated September 1, 2005 (incorporated by reference to Exhibit 4.1 to our Current Report on Form 8-K filed on September 6, 2005).
4.2(b)	Amended and Restated Trust Agreement among The New York Mortgage Company, LLC, JPMorgan Chase Bank, National Association, Chase Bank USA, National Association and the Administrative Trustees named therein, dated September 1, 2005 (incorporated by reference to Exhibit 4.2 to our Current Report on Form 8-K filed on September 6, 2005).
4.3(a)	Articles Supplementary Establishing and Fixing the Rights and Preferences of Series A Cumulative Redeemable Convertible Preferred Stock of the Company (Incorporated by reference to Exhibit 4.1 to the Company's Current Report on Form 8-K filed on January 25, 2008).
4.3(b)	Form of Series A Cumulative Redeemable Convertible Preferred Stock Certificate (Incorporated by reference to Exhibit 4.2 to the Company's Current Report on Form 8-K filed on January 25, 2008).
31.1	Certification of Co-Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley

Act of 2002.*

- 31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*
- 32.1 Certification of Co-Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*
- 32.2 Certification of Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*

* Filed herewith

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