

EASTMAN KODAK CO
Form 10-Q
July 30, 2009

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

For the quarterly period ended June 30, 2009
or

Transition report pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

For the transition period from ___ to ___

Commission File Number 1-87

EASTMAN KODAK COMPANY
(Exact name of registrant as specified in its charter)

NEW JERSEY
(State of incorporation)

16-0417150
(IRS Employer Identification No.)

343 STATE STREET, ROCHESTER, NEW
YORK

14650

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: 585-724-4000

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, and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months.

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.

Edgar Filing: EASTMAN KODAK CO - Form 10-Q

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

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

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

Title of each Class	Number of shares Outstanding at July 24, 2009
Common Stock, \$2.50 par value	268,201,646

Eastman Kodak Company
Form 10-Q
June 30, 2009

Table of Contents

	Page
<u>Part I. - Financial Information</u>	
<u>Item 1.</u>	
<u>Financial Statements</u>	3
<u>Consolidated Statement of Operations (Unaudited)</u>	3
<u>Consolidated Statement of Retained Earnings (Unaudited)</u>	4
<u>Consolidated Statement of Financial Position (Unaudited)</u>	5
<u>Consolidated Statement of Cash Flows (Unaudited)</u>	6
<u>Notes to Financial Statements (Unaudited)</u>	7
<u>Item 2.</u>	
<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	27
<u>Liquidity and Capital Resources</u>	45
<u>Item 3.</u>	
<u>Quantitative and Qualitative Disclosures About Market Risk</u>	50
<u>Item 4.</u>	
<u>Controls and Procedures</u>	50
<u>Part II. - Other Information</u>	
<u>Item 1.</u>	
<u>Legal Proceedings</u>	50
<u>Item 2.</u>	
<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	52
<u>Item 4.</u>	
<u>Submission of Matters to a Vote of Security Holders</u>	52
<u>Item 6.</u>	
<u>Exhibits</u>	52
<u>Signatures</u>	53
<u>Index to Exhibits</u>	54

Part I. FINANCIAL INFORMATION

Item 1. Financial Statements

EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF OPERATIONS (Unaudited)
(in millions, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Net sales	\$1,766	\$2,485	\$3,243	\$4,578
Cost of goods sold	1,440	1,899	2,723	3,568
Gross profit	326	586	520	1,010
Selling, general and administrative expenses	324	438	637	829
Research and development costs	84	135	189	269
Restructuring costs, rationalization and other	37	2	146	(8)
Other operating expenses (income), net	-	(7)	3	(17)
(Loss) earnings from continuing operations before interest expense,				
other income (charges), net and income taxes	(119)	18	(455)	(63)
Interest expense	23	26	48	54
Other income (charges), net	14	(5)	(1)	30
Loss from continuing operations before income taxes	(128)	(13)	(504)	(87)
Provision (benefit) for income taxes	63	(213)	47	(173)
(Loss) earnings from continuing operations	(191)	200	(551)	86
(Loss) earnings from discontinued operations, net of income taxes	(4)	295	3	294
Extraordinary item, net of tax	6	-	6	-
NET (LOSS) EARNINGS ATTRIBUTABLE TO EASTMAN KODAK COMPANY	\$(189)	\$495	\$(542)	\$380
Basic net (loss) earnings per share attributable to Eastman Kodak				
Company common shareholders:				
Continuing operations	\$(0.71)	\$0.69	\$(2.05)	\$0.30
Discontinued operations	(0.01)	1.03	0.01	1.02
Extraordinary item, net of tax	0.02	-	0.02	-
Total	\$(0.70)	\$1.72	\$(2.02)	\$1.32
Diluted net (loss) earnings per share attributable to Eastman Kodak				
Company common shareholders:				
Continuing operations	\$(0.71)	\$0.66	\$(2.05)	\$0.30
Discontinued operations	(0.01)	0.96	0.01	1.01
Extraordinary item, net of tax	0.02	-	0.02	-
Total	\$(0.70)	\$1.62	\$(2.02)	\$1.31

Number of common shares used in basic and diluted net (loss) earnings per share	268.2	288.2	268.2	288.2
Incremental shares from assumed issuance of unvested share-based awards	-	1.6	-	1.5
Convertible securities	-	18.5	-	-
Number of common shares used in diluted net (loss) earnings per share	268.2	308.3	268.2	289.7
Cash dividends declared per share	\$-	\$0.25	\$-	\$0.25

The accompanying notes are an integral part of these consolidated financial statements.

EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF RETAINED EARNINGS (Unaudited)
(in millions)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
Retained earnings at beginning of period	\$5,525	\$6,348	\$5,879	\$6,474
Net (loss) earnings	(189)	495	(542)	380
Cash dividends	-	(72)	-	(72)
(Loss) gain from issuance of treasury stock	(1)	1	(2)	(10)
Retained earnings at end of period	\$5,335	\$6,772	\$5,335	\$6,772

The accompanying notes are an integral part of these consolidated financial statements.

EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF FINANCIAL POSITION (Unaudited)

(in millions)	June 30, 2009	December 31, 2008
ASSETS		
Current Assets		
Cash and cash equivalents	\$1,132	\$2,145
Receivables, net	1,333	1,716
Inventories, net	918	948
Other current assets	216	195
Total current assets	3,599	5,004
Property, plant and equipment, net of accumulated depreciation of \$5,201 and \$5,254, respectively	1,407	1,551
Goodwill	901	896
Other long-term assets	1,199	1,728
TOTAL ASSETS	\$7,106	\$9,179
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable and other current liabilities	\$2,318	\$3,267
Short-term borrowings and current portion of long-term debt	52	51
Accrued income and other taxes	128	144
Total current liabilities	2,498	3,462
Long-term debt, net of current portion	1,259	1,252
Pension and other postretirement liabilities	2,380	2,382
Other long-term liabilities	1,078	1,119
Total liabilities	7,215	8,215
Commitments and Contingencies (Note 9)		
Shareholders' Equity		
Common stock, \$2.50 par value	978	978
Additional paid in capital	910	901
Retained earnings	5,335	5,879
Accumulated other comprehensive loss	(1,291)	(749)
	5,932	7,009
Less: Treasury stock, at cost	(6,044)	(6,048)
Total Eastman Kodak Company shareholders' equity	(112)	961
Noncontrolling interests	3	3
Total equity	(109)	964
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$7,106	\$9,179

The accompanying notes are an integral part of these consolidated financial statements.

EASTMAN KODAK COMPANY
CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)

(in millions)	Six Months Ended June 30,	
	2009	2008
Cash flows from operating activities:		
Net (loss) earnings	\$(542)	\$380
Adjustments to reconcile to net cash used in operating activities:		
Earnings from discontinued operations, net of income taxes	(3)	(294)
Earnings from extraordinary item, net of income taxes	(6)	-
Depreciation and amortization	219	252
Gain on sales of businesses/assets	(2)	(5)
Non-cash restructuring and rationalization costs, asset impairments and other charges	11	1
(Benefit) provision for deferred income taxes	(15)	102
Decrease in receivables	409	55
Decrease (increase) in inventories	34	(130)
Decrease in liabilities excluding borrowings	(1,087)	(921)
Other items, net	40	(41)
Total adjustments	(400)	(981)
Net cash used in continuing operations	(942)	(601)
Net cash provided by discontinued operations	-	299
Net cash used in operating activities	(942)	(302)
Cash flows from investing activities:		
Additions to properties	(60)	(123)
Proceeds from sales of businesses/assets	6	57
Acquisitions, net of cash acquired	-	(35)
Marketable securities - sales	18	95
Marketable securities - purchases	(17)	(96)
Net cash used in investing activities	(53)	(102)
Cash flows from financing activities:		
Proceeds from borrowings	9	86
Repayment of borrowings	(11)	(331)
Debt issuance costs	(13)	-
Net cash used in financing activities	(15)	(245)
Effect of exchange rate changes on cash	(3)	10
Net decrease in cash and cash equivalents	(1,013)	(639)
Cash and cash equivalents, beginning of period	2,145	2,947
Cash and cash equivalents, end of period	\$1,132	\$2,308

The accompanying notes are an integral part of these consolidated financial statements.

EASTMAN KODAK COMPANY
NOTES TO FINANCIAL STATEMENTS (Unaudited)

NOTE 1: BASIS OF PRESENTATION AND RECENT ACCOUNTING PRONOUNCEMENTS

BASIS OF PRESENTATION

The consolidated interim financial statements are unaudited, and certain information and footnote disclosures related thereto normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been omitted in accordance with Rule 10-01 of Regulation S-X. In the opinion of management, the accompanying unaudited consolidated financial statements were prepared following the same policies and procedures used in the preparation of the audited financial statements and reflect all adjustments (consisting of normal recurring adjustments) necessary to present fairly the results of operations, financial position and cash flows of Eastman Kodak Company and its subsidiaries (the Company). The results of operations for the interim periods are not necessarily indicative of the results for the entire fiscal year. These consolidated financial statements should be read in conjunction with the Company's Annual Report on Form 10-K for the year ended December 31, 2008.

The Company retrospectively applied Financial Accounting Standards Board (FASB) Statement No. 160, which is described in more detail below.

The Company has evaluated subsequent events for recognition or disclosure in the financial statements through the date of issuance, July 30, 2009.

Certain amounts for prior periods have been reclassified to conform to the current period classification.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

FASB Statement No. 168

In June 2009, the FASB issued SFAS No. 168, "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles: a replacement of FASB Statement No. 162." This Statement establishes two levels of U.S. generally accepted accounting principles (GAAP) – authoritative and nonauthoritative. The FASB Accounting Standards Codification (ASC) will become the source of authoritative, nongovernmental GAAP, except for rules and interpretive releases of the Securities and Exchange Commission (SEC). SFAS No. 168 is effective for financial statements issued for interim and annual periods ending after September 15, 2009, and will be adopted by the Company in the third quarter of 2009. The adoption of SFAS No. 168 will not have any impact on the Company's Consolidated Financial Statements.

FASB Statement No. 167

In June 2009, the FASB issued SFAS No. 167, "Amendments to FASB Interpretation No. 46(R)." This Statement requires entities to perform a qualitative analysis to determine whether a variable interest gives the entity a controlling financial interest in a variable interest entity. This Statement also requires an ongoing reassessment of variable interests and eliminates the quantitative approach previously required for determining whether an entity is the primary beneficiary. SFAS No. 167 is effective as of the beginning of an entity's first annual reporting period that begins after November 15, 2009 (January 1, 2010 for the Company). The Company is currently evaluating the potential impact, if any, of the adoption of SFAS No. 167 on its Consolidated Financial Statements.

FSP FAS 132(R)-1

In December 2008, the FASB issued FSP FAS 132(R)-1, "Employers' Disclosures About Postretirement Benefit Plan Assets," which amends SFAS No. 132(R), "Employers' Disclosures About Pensions and Other Postretirement Benefits" to require more detailed disclosures about employers' postretirement benefit plan assets. New disclosures include information regarding investment strategies, major categories of plan assets, concentrations of risk within plan assets and valuation techniques used to measure the fair value of plan assets. This FSP requires new disclosures only, and will have no impact on the Company's Consolidated Financial Statements. These new disclosures will be required for the Company beginning with its 2009 Annual Report on Form 10-K.

RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

FASB Statement No. 165

In May 2009, the FASB issued SFAS No. 165, "Subsequent Events." This Statement establishes general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued. SFAS No. 165 was effective for interim or annual financial periods ending after June 15, 2009, and the adoption did not have any impact on the Company's Consolidated Financial Statements.

FASB Staff Position FSP FAS 157-4

In April 2009, the FASB issued FASB Staff Position FAS 157-4, "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly." This FSP provides guidance regarding how to determine whether there has been a significant decrease in the volume and level of activity for the asset or liability when compared with normal market activity for the asset or liability. In such situation, an entity may conclude that transactions or quoted prices may not be determinative of fair value, and may adjust the transactions or quoted prices to arrive at the fair value of the asset or liability. This FSP is effective for interim and annual reporting period ending after June 15, 2009, and shall be applied prospectively. The adoption of this Staff Position did not have a material impact on the Company's Consolidated Financial Statements.

FSP FAS 107-1 and APB 28-1

In April 2009, the FASB issued FSP FAS 107-1 and APB 28-1, "Interim Disclosures about Fair Value of Financial Instruments," which requires that publicly traded companies include the fair value disclosures required by SFAS No. 107 in their interim financial statements. This FSP is effective for interim reporting periods ending after June 15, 2009, and the Company has included the required disclosures in this Form 10-Q.

FSP EITF 03-6-1

In June 2008, the FASB released FSP EITF 03-6-1 on Emerging Issues Task Force Issue 03-6, "Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities." The Staff Position requires that unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents are participating securities as defined in EITF 03-6, "Participating Securities and the Two Class Method under FASB Statement No. 128," and therefore, should be included in computing earnings per share using the two-class method. The Staff Position was effective for the Company as of January 1, 2009, and did not have a material impact on the Company's earnings per share.

FASB Statement No. 161

In March 2008, the FASB issued SFAS No. 161, "Disclosures about Derivative Instruments and Hedging Activities – an amendment of FASB Statement No. 133." This Statement amends and expands the disclosure requirements for derivative instruments and hedging activities, with the intent to provide users of financial statements with an enhanced understanding of how and why an entity uses derivative instruments, how derivative instruments and related hedged items are accounted for, and how derivative instruments and related hedged items affect an entity's financial statements. The Company adopted SFAS No. 161 as of January 1, 2009; see Note 17, "Financial Instruments."

FASB Statement No. 160

In December 2007, the FASB issued SFAS No. 160, "Noncontrolling Interests in Consolidated Financial Statements – an amendment of ARB No. 51." This Statement establishes accounting and reporting standards for ownership interests in subsidiaries held by parties other than the parent. Specifically, SFAS No. 160 requires the presentation of noncontrolling interests as equity in the Consolidated Statement of Financial Position, and separate identification and presentation in the Consolidated Statement of Operations of net income attributable to the entity and the noncontrolling interest. The Company adopted SFAS No. 160 as of January 1, 2009, and, as required, applied this standard to the prior period's financial statements. SFAS No. 160 also establishes accounting and reporting standards

regarding deconsolidation and changes in a parent's ownership interest, and these standards will be applied prospectively to any such transactions in 2009 onward. The adoption of SFAS No. 160 did not have a material impact on the Company's Consolidated Financial Statements.

FASB Statement No. 141(R)

In December 2007, the FASB issued SFAS No. 141(R), "Business Combinations," a revision to SFAS No. 141, "Business Combinations." SFAS No. 141(R) provides revised guidance for recognition and measurement of identifiable assets and goodwill acquired, liabilities assumed, and any noncontrolling interest in the acquiree at fair value. The Statement also establishes disclosure

requirements to enable the evaluation of the nature and financial effects of a business combination. Additionally, the FASB also issued FSP 141(R)-1 in April 2009, which modified the guidance in SFAS No. 141(R) related to contingent assets and contingent liabilities. SFAS No. 141(R), as modified by FSP 141(R)-1, is required to be applied prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2008. The adoption of SFAS No. 141(R), as modified by FSP 141(R)-1, as of January 1, 2009 did not have a material impact on the Company's Consolidated Financial Statements.

NOTE 2: RECEIVABLES, NET

(in millions)	As of June 30, 2009	December 31, 2008
Trade receivables	\$1,167	\$1,330
Miscellaneous receivables	166	386
Total (net of allowances of \$106 and \$113 as of June 30, 2009 and December 31, 2008, respectively)	\$1,333	\$1,716

Of the total trade receivable amounts of \$1,167 million and \$1,330 million as of June 30, 2009 and December 31, 2008, respectively, approximately \$136 million and \$218 million, respectively, are expected to be settled through customer deductions in lieu of cash payments. Such deductions represent rebates owed to customers and are included in Accounts payable and other current liabilities in the accompanying Consolidated Statement of Financial Position at each respective balance sheet date. The majority of the decrease in Miscellaneous receivables was the result of payments received in the first two quarters of 2009 related to an intellectual property licensing agreement for which the associated revenue was recognized in 2008.

NOTE 3: INVENTORIES, NET

(in millions)	As of June 30, 2009	December 31, 2008
Finished goods	\$577	\$610
Work in process	195	193
Raw materials	146	145
Total	\$918	\$948

NOTE 4: GOODWILL AND OTHER INTANGIBLE ASSETS

Goodwill was \$901 million and \$896 million at June 30, 2009 and December 31, 2008, respectively. The changes in the carrying amount of goodwill by reportable segment for the six months ended June 30, 2009 were as follows:

(in millions)	As of June 30, 2009			
	Consumer Digital Imaging Group	Film, Photofinishing and Entertainment Group	Graphic Communications Group	Consolidated Total
Balance as of December 31, 2008	\$ 195	\$ 613	\$ 88	\$ 896
Currency translation adjustments	-	2	3	5
Balance as of June 30, 2009	\$ 195	\$ 615	\$ 91	\$ 901

The gross carrying amount and accumulated amortization by major intangible asset category as of June 30, 2009 and December 31, 2008 were as follows:

(in millions)	As of June 30, 2009			
	Gross Carrying Amount	Accumulated Amortization	Net	Weighted-Average Amortization Period
Technology-based	\$ 304	\$ 218	\$ 86	7 years
Customer-related	263	155	108	10 years
Other	63	46	17	11 years
Total	\$ 630	\$ 419	\$ 211	9 years

(in millions)	As of December 31, 2008			
	Gross Carrying Amount	Accumulated Amortization	Net	Weighted-Average Amortization Period
Technology-based	\$ 300	\$ 190	\$ 110	7 years
Customer-related	276	156	120	10 years
Other	57	40	17	9 years
Total	\$ 633	\$ 386	\$ 247	8 years

Amortization expense related to purchased intangible assets for the three months ended June 30, 2009 and 2008 was \$19 million and \$20 million, respectively. Amortization expense related to purchased intangible assets for the six months ended June 30, 2009 and 2008 was \$36 million and \$40 million, respectively.

Estimated future amortization expense related to purchased intangible assets as of June 30, 2009 is as follows (in millions):

2009	\$34
------	------

Edgar Filing: EASTMAN KODAK CO - Form 10-Q

2010	58
2011	39
2012	24
2013	6
2014 and thereafter	50
Total	\$211

NOTE 5: OTHER LONG-TERM ASSETS

(in millions)	As of	
	June 30, 2009	December 31, 2008
Overfunded pension plans	\$255	\$773
Deferred income taxes, net of valuation allowance	498	506
Intangible assets	211	247
Other	235	202
Total	\$1,199	\$1,728

NOTE 6: ACCOUNTS PAYABLE AND OTHER CURRENT LIABILITIES

(in millions)	As of	
	June 30, 2009	December 31, 2008
Accounts payable, trade	\$681	\$1,288
Other current liabilities	1,637	1,979
Total	\$2,318	\$3,267

NOTE 7: SHORT-TERM BORROWINGS AND LONG-TERM DEBT

On March 31, 2009, the Company and its subsidiary, Kodak Canada Inc. (together, the "Borrowers"), together with the Company's U.S. subsidiaries as guarantors (the "Guarantors"), entered into an Amended and Restated Credit Agreement (the "Amended Credit Agreement"), with the named lenders (the "Lenders") and Citicorp USA, Inc. as agent, in order to amend and extend its Credit Agreement dated as of October 18, 2005 (the "Secured Credit Agreement").

The Amended Credit Agreement provides for an asset-based revolving credit facility of up to \$500 million, as further described below. The letters of credit previously issued under the former Secured Credit Agreement continue under the Amended Credit Agreement. Additionally, up to \$100 million of the Company's and its subsidiaries' obligations to various Lenders under treasury management services, hedge or other agreements or arrangements are secured by the asset-based collateral under the Amended Credit Agreement. The Amended Credit Agreement can be used for general corporate purposes, other than prepaying or redeeming the Company's outstanding 3.375% Senior Convertible Notes due 2033. The termination date of the Amended Credit Agreement with respect to the Lenders who agreed to the extension, and any future lenders, is March 31, 2012, and with respect to the other Lenders continues to be October 18, 2010. As of June 30, 2009, approximately 75% of the facility amount has been extended to the 2012 termination date, and additional lenders may be added to increase this amount.

Advances under the Amended Credit Agreement will be available based on the Borrowers' respective borrowing base from time to time. The borrowing base is calculated based on designated percentages of eligible accounts receivable, inventory, machinery and equipment and, once mortgages are recorded, certain real property, subject to applicable

reserves. The Amended Credit Agreement provides that advances made from time to time will bear interest at applicable margins over the Base Rate, as defined, or the Eurodollar Rate. The Company pays, on a quarterly basis, an annual fee ranging from 0.50% to 1.00% to the Lenders based on the unused commitments.

The obligations of the Borrowers are secured by liens on substantially all of their non-real estate assets and by a pledge of 65% of the stock of certain of the Company's material non-U.S. subsidiaries, pursuant to Amended and Restated U.S. and Canadian Security Agreements. In addition, the Company expects to mortgage certain U.S. real property for inclusion in the borrowing base for advances under the Amended Credit Agreement. The security interests are limited to the extent necessary so that they do not trigger the cross-collateralization requirements under the Company's indenture with Bank of New York as trustee, dated as of January 1, 1988, as amended by various supplemental indentures.

Under the terms of the Amended Credit Agreement, the Company has agreed to certain affirmative and negative covenants customary in similar asset-based lending facilities. In the event the Company's excess availability under the borrowing base formula under the Amended Credit Agreement falls below \$100 million for three consecutive business days, among other things, the Company must maintain a fixed charge coverage ratio of not less than 1.1 to 1.0 until the excess availability is greater than \$100 million for 30 consecutive days. As of June 30, 2009, excess availability was greater than \$100 million. The Company is also required to maintain cash and cash equivalents in the U.S. of at least \$250 million. The negative covenants limit, under certain circumstances, among other things, the Company's ability to incur additional debt or liens, make certain investments, make shareholder distributions or prepay debt, except as permitted under the terms of the Amended Credit Agreement. The Company was in compliance with all covenants under the Amended Credit Agreement as of June 30, 2009.

The Amended Credit Agreement contains customary events of default, including without limitation, payment defaults (subject to grace and cure periods in certain circumstances), breach of representations and warranties, breach of covenants (subject to grace and cure periods in certain circumstances), bankruptcy events, ERISA events, cross defaults to certain other indebtedness, certain judgment defaults and change of control. If an event of default occurs and is continuing, the Lenders may decline to provide additional advances, impose a default rate of interest, declare all amounts outstanding under the Amended Credit Agreement immediately due and payable, and require cash collateralization or similar arrangements for outstanding letters of credit.

As of June 30, 2009, the Company had no debt for borrowed money outstanding under the Amended Credit Agreement, but had outstanding letters of credit of \$131 million. In addition to the amounts outstanding under the Amended Credit Agreement, there were bank guarantees of \$33 million and surety bonds of \$31 million outstanding primarily to ensure the payment of possible casualty and workers' compensation claims, environmental liabilities, legal contingencies, rental payments, and to support various customs and trade activities.

In addition to the Amended Credit Agreement, the Company has other committed and uncommitted lines of credit as of June 30, 2009 totaling \$28 million and \$315 million, respectively. These lines primarily support operational and borrowing needs of the Company's subsidiaries, which include term loans, overdraft coverage, revolving credit lines, letters of credit, bank guarantees and vendor financing programs. Interest rates and other terms of borrowing under these lines of credit vary from country to country, depending on local market conditions. As of June 30, 2009, usage under these lines was approximately \$58 million, with \$2 million reflected in Short-term borrowings and current portion of long-term debt on the accompanying Consolidated Statement of Financial Position, and the balance supporting non-debt related obligations.

NOTE 8: INCOME TAXES

The Company's income tax provision (benefit) and effective tax rate were as follows:

(dollars in millions)	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
Loss from continuing operations before income taxes	\$(128)	\$(13)	\$(504)	\$(87)
Provision (benefit) for income taxes	\$63	\$(213)	\$47	\$(173)
Effective tax rate	(49.2)%	1638.5 %	(9.3)%	198.9 %
Benefit for income taxes @ 35%	\$(45)	\$(5)	\$(176)	\$(30)
Difference between tax at effective vs. statutory rate	\$108	\$(208)	\$223	\$(143)

For the three months ended June 30, 2009, the difference between the Company's recorded provision and the benefit that would result from applying the U.S. statutory rate of 35.0% is primarily attributable to: (1) losses generated within the U.S. and certain jurisdictions outside the U.S. that were not benefited due to management's conclusion that it was not more likely than not that the tax benefits would be realized; (2) the impact of previously established valuation allowances in jurisdictions with current earnings; (3) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S.; (4) tax accounting impacts related to items reported in Accumulated other comprehensive income; and (5) adjustments for uncertain tax positions and tax audits.

For the six months ended June 30, 2009, the difference between the Company's recorded provision and the benefit that would result from applying the U.S. statutory rate of 35.0% is primarily attributable to: (1) losses generated within the U.S. and certain jurisdictions outside the U.S. that were not benefited due to management's conclusion that it was not more likely than not that the tax benefits would be realized; (2) the impact of previously established valuation allowances in jurisdictions with current earnings; (3) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S.; and (4) adjustments for uncertain tax positions and tax audits.

In June 2008, the Company received a tax refund from the U.S. Internal Revenue Service (IRS). The refund is related to the audit of certain claims filed for tax years 1993-1998. The refund had a positive impact on the Company's net earnings of \$565 million for the three and six months ended June 30, 2008, of which \$295 million of the refund is reflected in earnings from discontinued operations. The balance of \$270 million, which represents interest, is reflected in earnings from continuing operations.

For the three and six months ended June 30, 2008, the difference between the Company's recorded benefit and the benefit that would result from applying the U.S. statutory rate of 35.0% is primarily attributable to: (1) interest earned on the IRS tax refund, partially offset by (2) losses generated within the U.S. and certain jurisdictions outside the U.S. that were not benefited due to previously established valuation allowances, (3) the impact of previously established valuation allowances in jurisdictions with current earnings, (4) the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S., and (5) adjustments for uncertain tax positions and tax audits.

NOTE 9: COMMITMENTS AND CONTINGENCIES

Environmental

The Company's undiscounted accrued liabilities for future environmental investigation, remediation, and monitoring costs are composed of the following items:

(in millions)	June 30, 2009	As of December 31, 2008
Eastman Business Park site, Rochester, NY	\$58	\$63
Other operating sites	11	12
Sites associated with former operations	21	21
Sites associated with the non-imaging health business sold in 1994	21	19
Total	\$111	\$115

These amounts are reported in Other long-term liabilities in the accompanying Consolidated Statement of Financial Position.

Cash expenditures for the aforementioned investigation, remediation and monitoring activities are expected to be incurred over the next twenty-seven years for several of the sites. For these known environmental liabilities, the accrual reflects the Company's best estimate of the amount it will incur under the agreed-upon or proposed work plans. The Company's cost estimates were determined using the ASTM Standard E 2137-06, "Standard Guide for Estimating Monetary Costs and Liabilities for Environmental Matters," and have not been reduced by possible recoveries from third parties. The overall method includes the use of a probabilistic model which forecasts a range of cost estimates for the remediation required at individual sites. The projects are closely monitored and the models are

reviewed as significant events occur, or at least once per year. The Company's estimate includes investigations, equipment and operating costs for remediation and long-term monitoring of the sites. The Company does not believe it is reasonably possible that the losses for the known exposures could exceed the current accruals by material amounts.

A Consent Decree was signed in 1994 in settlement of a civil complaint brought by the U.S. Environmental Protection Agency ("EPA") and the U.S. Department of Justice. In connection with the Consent Decree, the Company is subject to a Compliance Schedule, under which the Company has improved its waste characterization procedures, upgraded one of its incinerators, and has upgraded its industrial sewer system. The Company submitted a certification stating that it has completed the requirements of the Consent Decree in the fourth quarter of 2008, and expects to receive an acknowledgement of completion from the EPA before the end of 2009. No further

capital expenditures are expected under this program, but Kodak is required to continue the sewer inspection program until the Decree is closed by the Court. Costs associated with the sewer inspection program are not material.

The Company is presently designated as a potentially responsible party (PRP) under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, as amended (the Superfund Law), or under similar state laws, for environmental assessment and cleanup costs as the result of the Company's alleged arrangements for disposal of hazardous substances at eight Superfund sites. With respect to each of these sites, the Company's liability is minimal. In addition, the Company has been identified as a PRP in connection with the non-imaging health businesses in two active Superfund sites. Numerous other PRPs have also been designated at these sites. Although the law imposes joint and several liability on PRPs, the Company's historical experience demonstrates that these costs are shared with other PRPs. Settlements and costs paid by the Company in Superfund matters to date have not been material. Future costs are also not expected to be material to the Company's financial position, results of operations or cash flows.

Estimates of the amount and timing of future costs of environmental remediation requirements are by their nature imprecise because of the continuing evolution of environmental laws and regulatory requirements, the availability and application of technology, the identification of presently unknown remediation sites and the allocation of costs among the potentially responsible parties. Based upon information presently available, such future costs are not expected to have a material effect on the Company's competitive or financial position. However, such costs could be material to results of operations in a particular future quarter or year.

Other Commitments and Contingencies

As of June 30, 2009, the Company had outstanding letters of credit of \$131 million issued under the Amended Credit Agreement, as well as bank guarantees of \$33 million and surety bonds in the amount of \$31 million primarily to ensure the payment of possible casualty and workers' compensation claims, environmental liabilities, legal contingencies, rental payments, and to support various customs, tax and trade activities.

The Company's Brazilian operations are involved in governmental assessments of indirect and other taxes in various stages of litigation, primarily related to federal and state value-added taxes. The Company is disputing these matters and intends to vigorously defend its position. Based on the opinion of legal counsel, management does not believe that the ultimate resolution of these matters will materially impact the Company's results of operations, financial position or cash flows. The Company routinely assesses all these matters as to the probability of ultimately incurring a liability in its Brazilian operations, and records its best estimate of the ultimate loss in situations where it assesses the likelihood of loss as probable.

The Company recorded a contingency accrual of \$21 million in the fourth quarter of 2008 related to employment litigation matters. The employment litigation matters related to a number of cases, which had similar fact patterns related to legacy equal employment opportunity issues. On April 27, 2009, the plaintiffs filed an unopposed motion for preliminary approval of a settlement in this action pursuant to which the Company will establish a settlement fund in the amount of \$21 million that will be used for payments to plaintiffs and class members, as well as attorneys' fees, litigation costs, and claims administration costs. The settlement is subject to court approval.

The Company is being sued for infringement of patents alleged to be related to products in the Company's Graphic Communications Group. The plaintiff is seeking unspecified damages and other relief. The parties are presently in productive settlement discussions including cross-license negotiations that could result in balancing payments by the Company of at least \$30 million.

The Company and its subsidiaries are involved in various lawsuits, claims, investigations and proceedings, including commercial, customs, employment, environmental, and health and safety matters, which are being handled and defended in the ordinary course of business. In addition, the Company is subject to various assertions, claims, proceedings and requests for indemnification concerning intellectual property, including patent infringement suits involving technologies that are incorporated in a broad spectrum of the Company's products. These matters are in various stages of investigation and litigation and are being vigorously defended. Although the Company does not expect that the outcome in any of these matters, individually or collectively, will have a material adverse effect on its financial condition or results of operations, litigation is inherently unpredictable. Therefore, judgments could be rendered or settlements entered, that could adversely affect the Company's operating results or cash flow in a particular period. The Company

routinely assesses all its litigation and threatened litigation as to the probability of ultimately incurring a liability, and records its best estimate of the ultimate loss in situations where it assesses the likelihood of loss as probable.

NOTE 10: GUARANTEES

The Company guarantees debt and other obligations of certain customers. The debt and other obligations are primarily due to banks and leasing companies in connection with financing of customers' purchases of equipment and product from the Company. At June 30, 2009, the maximum potential amount of future payments (undiscounted) that the Company could be required to make under these customer-related guarantees was \$63 million. At June 30, 2009, the carrying amount of any liability related to these customer guarantees was not material.

The customer financing agreements and related guarantees, which mature between 2009 and 2014, typically have a term of 90 days for product and short-term equipment financing arrangements, and up to five years for long-term equipment financing arrangements. These guarantees would require payment from the Company only in the event of default on payment by the respective debtor. In some cases, particularly for guarantees related to equipment financing, the Company has collateral or recourse provisions to recover and sell the equipment to reduce any losses that might be incurred in connection with the guarantees. However, any proceeds received from the liquidation of these assets may not cover the maximum potential loss under these guarantees.

Eastman Kodak Company ("EKC") also guarantees potential indebtedness to banks and other third parties for some of its consolidated subsidiaries. The maximum amount guaranteed is \$282 million, and the outstanding amount for those guarantees is \$194 million with \$177 million recorded within the Short-term borrowings and current portion of long-term debt, and Long-term debt, net of current portion components in the accompanying Consolidated Statement of Financial Position. These guarantees expire in 2009 through 2014. Pursuant to the terms of the Company's Amended Credit Agreement, obligations of the Borrowers to the Lenders under the Amended Credit Agreement, as well as secured agreements in an amount not to exceed \$100 million, are guaranteed by the Company and the Company's U.S. subsidiaries and included in the above amounts.

During the fourth quarter of 2007, EKC issued a guarantee to Kodak Limited (the "Subsidiary") and the Trustees (the "Trustees") of the Kodak Pension Plan of the United Kingdom (the "Plan"). Under this arrangement, EKC guarantees to the Subsidiary and the Trustees the ability of the Subsidiary, only to the extent it becomes necessary to do so, to (1) make contributions to the Plan to ensure sufficient assets exist to make plan benefit payments, and (2) make contributions to the Plan such that it will achieve full funded status by the funding valuation for the period ending December 31, 2015. The guarantee expires upon the conclusion of the funding valuation for the period ending December 31, 2015 whereby the Plan achieves full funded status or earlier, in the event that the Plan achieves full funded status for two consecutive funding valuation cycles which are typically performed at least every three years. The limit of potential future payments is dependent on the funding status of the Plan as it fluctuates over the term of the guarantee. The Plan's most recent local funding valuation was completed in March 2009. EKC and the Subsidiary are in discussions with the Trustees regarding the amount of future annual contributions and the date by which the Plan will achieve full funded status. These negotiations may require changes to the existing guarantee described above. The funded status of the Plan (calculated in accordance with U.S. GAAP) is included in Pension and other postretirement liabilities presented in the Consolidated Statement of Financial Position.

Indemnifications

The Company issues indemnifications in certain instances when it sells businesses and real estate, and in the ordinary course of business with its customers, suppliers, service providers and business partners. Further, the Company indemnifies its directors and officers who are, or were, serving at the Company's request in such capacities. Historically, costs incurred to settle claims related to these indemnifications have not been material to the

Company's financial position, results of operations or cash flows. Additionally, the fair value of the indemnifications that the Company issued during the quarter ended June 30, 2009 was not material to the Company's financial position, results of operations or cash flows.

Warranty Costs

The Company has warranty obligations in connection with the sale of its products and equipment. The original warranty period is generally one year or less. The costs incurred to provide for these warranty obligations are estimated and recorded as an accrued liability at the time of sale. The Company estimates its warranty cost at the point of sale for a given product based on historical failure rates and related costs to repair. The change in the Company's accrued warranty obligations balance, which is reflected in Accounts payable and other current liabilities in the accompanying Consolidated Statement of Financial Position, was as follows:

(in millions)

Accrued warranty obligations as of December 31, 2008	\$65
Actual warranty experience during 2009	(44)
2009 warranty provisions	30
Accrued warranty obligations as of June 30, 2009	\$51

The Company also offers its customers extended warranty arrangements that are generally one year, but may range from three months to three years after the original warranty period. The Company provides repair services and routine maintenance under these arrangements. The Company has not separated the extended warranty revenues and costs from the routine maintenance service revenues and costs, as it is not practicable to do so. Therefore, these revenues and costs have been aggregated in the discussion that follows. Costs incurred under these arrangements for the six months ended June 30, 2009 amounted to \$92 million. The change in the Company's deferred revenue balance in relation to these extended warranty and maintenance arrangements from December 31, 2008 to June 30, 2009, which is reflected in Accounts payable and other current liabilities in the accompanying Consolidated Statement of Financial Position, was as follows:

(in millions)

Deferred revenue on extended warranties as of December 31, 2008	\$153
New extended warranty and maintenance arrangements in 2009	228
Recognition of extended warranty and maintenance arrangement revenue in 2009	(228)
Deferred revenue on extended warranties as of June 30, 2009	\$153

NOTE 11: RESTRUCTURING AND RATIONALIZATION LIABILITIES

2009 Program

On December 17, 2008, the Company committed to a plan to implement a targeted cost reduction program (the 2009 Program) to more appropriately size the organization as a result of the global economic slowdown which began in 2008. The program involves the rationalization of selling, marketing, administrative, research and development, supply chain and other business resources in certain areas and the consolidation of certain facilities.

In connection with the 2009 Program, the Company expects to incur total restructuring charges in the range of \$250 million to \$300 million, including \$225 million to \$265 million of cash related charges for termination benefits and other exit costs, and \$25 million to \$35 million of non-cash accelerated depreciation charges and asset write-offs. The 2009 Program will require expenditures from corporate cash in the range of \$125 million to \$175 million, as most of the termination benefits for U.S. employees will be provided in the form of special retirement benefits (Special

Termination Program (STP) benefits) payable from the Company's over-funded U.S. pension plan. All actions under the program are expected to be completed by the end of 2009. The 2009 Program is expected to result in employment reductions in the range of 2,000 to 3,000 positions when complete. When combined with rationalization actions taken in late 2008, the Company expects to reduce its worldwide employment by between 3,500 and 4,500 positions during 2009, approximately 14% to 18% of its total workforce. Including the impact of carryover actions from 2008, the Company expects to make payments from corporate cash in 2009 in the range of \$225 million to \$275 million.

The actual charges for restructuring and ongoing rationalization initiatives are recorded in the period in which the Company commits to formalized restructuring or ongoing rationalization plans, or executes the specific actions contemplated by the plans and all criteria for liability recognition under the applicable accounting guidance have been met.

Restructuring and Ongoing Rationalization Reserve Activity

The activity in the accrued balances and the non-cash charges and credits incurred in relation to restructuring initiatives and ongoing rationalization activities for the three and six months ended June 30, 2009 were as follows:

(in millions)	Severance Reserve	Exit Costs Reserve	Inventory Write-downs	Accelerated Depreciation	Total
Balance as of 12/31/08	\$ 109	\$ 21	\$ -	\$ -	130
Q1 2009 charges	94	15	3	4	116
Q1 2009 utilization/cash payments	(43)	(5)	(3)	(4)	(55)
Q1 2009 other adjustments & reclasses (1)	(40)	-	-	-	(40)
Balance as of 3/31/09	120	31	-	-	151
Q2 2009 charges	28	9	3	6	46
Q2 2009 utilization/cash payments	(47)	(8)	(3)	(6)	(64)
Q2 2009 other adjustments & reclasses (2)	(7)	2	-	-	(5)
Balance as of 6/30/09	\$ 94	\$ 34	\$ -	\$ -	\$ 128

(1) Includes \$37 million of severance-related charges for pension plan curtailments, settlements, and special termination benefits, which are reflected in Pension and other postretirement liabilities and Other long-term assets in the Consolidated Statement of Financial Position. The remaining \$3 million reflects foreign currency translation adjustments.

(2) The net \$5 million reserve reduction includes an \$11 million reduction for severance-related charges for pension plan curtailments, settlements, and special termination benefits, which are reflected in Pension and other postretirement liabilities and Other long-term assets in the Consolidated Statement of Financial Position. The remaining \$6 million of reserve increases reflects foreign currency translation adjustments.

The \$46 million of charges for the three months ended June 30, 2009 includes \$6 million of charges for accelerated depreciation and \$3 million of charges for inventory write-downs, which were reported in Cost of goods sold in the accompanying Consolidated Statement of Operations for the three months ended June 30, 2009. The remaining costs incurred, net of reversals, of \$37 million were reported as Restructuring costs, rationalization and other in the accompanying Consolidated Statement of Operations for the three months ended June 30, 2009. The severance and exit costs reserves require the outlay of cash, while accelerated depreciation and inventory write-downs represent non-cash items.

For the three months ended June 30, 2009, the severance costs related to the elimination of approximately 550 positions, including approximately 250 manufacturing, 75 research and development, and 225 administrative positions. The geographic composition of the positions eliminated includes approximately 175 in the United States and Canada, and 375 throughout the rest of the world.

The charges of \$46 million recorded in the second quarter of 2009 included \$8 million applicable to FPEG, \$2 million applicable to CDG, \$23 million applicable to GCG, and \$13 million that was applicable to manufacturing, research and development, and administrative functions, which are shared across all segments.

The \$162 million of charges for the six months ended June 30, 2009 includes \$10 million of charges for accelerated depreciation and \$6 million of charges for inventory write-downs, which were reported in Cost of goods sold in the accompanying Consolidated Statement of Operations for the six months ended June 30, 2009. The remaining costs incurred, net of reversals, of \$146 million were reported as Restructuring costs, rationalization and other in the accompanying Consolidated Statement of Operations for the six months ended June 30, 2009. The severance and exit costs reserves require the outlay of cash, while accelerated depreciation and inventory write-downs represent non-cash items.

For the six months ended June 30, 2009, the severance costs related to the elimination of approximately 2,150 positions, including approximately 1,100 manufacturing, 375 research and development and 675 administrative positions. The geographic composition of the positions eliminated includes approximately 1,225 in the United States and Canada, and 925 throughout the rest of the world.

The charges of \$162 million recorded in the first half of 2009 included \$41 million applicable to FPEG, \$16 million applicable to CDG, \$75 million applicable to GCG, and \$30 million that was applicable to manufacturing, research and development, and administrative functions, which are shared across all segments.

As a result of these initiatives, severance payments will be paid during periods through 2009 since, in many instances, the employees whose positions were eliminated can elect or are required to receive their payments over an extended period of time. In addition, certain exit costs, such as long-term lease payments, will be paid over periods throughout 2009 and beyond.

NOTE 12: RETIREMENT PLANS AND OTHER POSTRETIREMENT BENEFITS

Components of the net periodic benefit cost for all major funded and unfunded U.S. and Non-U.S. defined benefit plans for the three and six months ended June 30 are as follows:

(in millions)	Three Months Ended June 30,				Six Months Ended June 30,			
	2009		2008		2009		2008	
	U.S.	Non-U.S.	U.S.	Non-U.S.	U.S.	Non-U.S.	U.S.	Non-U.S.
Major defined benefit plans:								
Service cost	\$11	\$4	\$13	\$6	\$24	\$7	\$27	\$12
Interest cost	78	45	77	57	155	87	154	114
Expected return on plan assets	(122)	(50)	(136)	(69)	(240)	(97)	(272)	(137)
Amortization of:								
Recognized net actuarial loss	1	2	1	16	2	4	2	32
Pension (income) expense before special termination benefits, curtailments, and settlements	(32)	1	(45)	10	(59)	1	(89)	21
Special termination benefits	11	-	1	-	47	-	6	1
Curtailment losses (gains)	-	-	(3)	-	1	-	(12)	-
Net pension expense (income)	(21)	1	(47)	10	(11)	1	(95)	22
Other plans including unfunded plans	-	2	-	3	-	-	-	5
Total net pension expense (income) from continuing operations	\$(21)	\$3	\$(47)	\$13	\$(11)	\$1	\$(95)	\$27

For the three and six months ended June 30, 2009 and 2008, all amounts reflected in the table above as special termination benefits charges were incurred as a result of the Company's restructuring actions. For the six months ended June 30, 2009, \$1 million of curtailment losses for the major funded and unfunded U.S. and Non-U.S. defined benefit plans were incurred as a result of the Company's restructuring actions. In addition, curtailment gains for the major funded and unfunded U.S. and Non-U.S. defined benefit plans totaling \$7 million for the six months ended June 30, 2008 were also incurred as a result of the Company's restructuring actions. All special termination benefits, curtailments, and settlements incurred as a result of the Company's restructuring actions have been included in Restructuring costs, rationalization and other in the Consolidated Statement of Operations for the respective periods.

The Company made contributions (funded plans) or paid benefits (unfunded plans) totaling approximately \$40 million relating to its major U.S. and non-U.S. defined benefit pension plans for the six months ended June 30, 2009. The Company expects its contribution (funded plans) and benefit payment (unfunded plans) requirements for its major U.S. and non-U.S. defined benefit pension plans for the balance of 2009 to be approximately \$73 million.

Postretirement benefit costs for the Company's U.S., United Kingdom and Canada postretirement benefit plans, which represent the Company's major postretirement plans, include:

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Service cost	\$-	\$2	\$-	\$4
Interest cost	24	39	48	78
Amortization of:				
Prior service credit	(17)	(10)	(34)	(20)
Recognized net actuarial loss	5	5	10	11
Other postretirement benefit cost before curtailments and settlements	12	36	24	73
Curtailment gain	-	(2)	-	(7)
Settlement gain	-	-	-	(2)
Total net postretirement benefit expense	\$12	\$34	\$24	\$64

As a result of the Company's restructuring actions, its U.S., United Kingdom and Canada postretirement benefit plans incurred curtailment gains of \$3 million for the six months ended June 30, 2008, which have been included in Restructuring costs, rationalization and other in the Consolidated Statement of Operations for that period.

The Company paid benefits totaling approximately \$84 million relating to its U.S., United Kingdom and Canada postretirement benefit plans for the six months ended June 30, 2009. The Company expects to pay benefits of approximately \$86 million for these postretirement plans for the balance of 2009.

The Company accounts for its defined benefit pension and other postretirement plans in accordance with 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 No. 158 requires that the funded status of all overfunded plans be aggregated and presented as an asset. The funded status of all underfunded plans must also be aggregated and presented as a liability. As of June 30, 2009 and December 31, 2008 the funded status of all major overfunded plans was approximately \$255 million and \$765 million, respectively, which is reflected in Other long-term assets in the Company's Consolidated Statement of Financial Position. As of June 30, 2009 and December 31, 2008, the funded status of all major underfunded plans was approximately \$2.4 billion, which is reflected in Accounts payable and other current liabilities and Pension and other postretirement liabilities in the Company's Consolidated Statement of Financial Position. In accordance with SFAS No. 158 the measurement date used to determine the funded status of each of the Company's pension and other postretirement benefits plan is December 31 of the prior year unless certain remeasurement events occur.

Certain of the Company's retirement plans were remeasured during the second quarter of 2009. The remeasurement of the funded status of those plans during the quarter decreased the funded status of the Company's defined benefit and other postretirement benefit plans by \$618 million. This decrease was primarily due to actuarial losses related to asset return and discount rate assumptions.

The Kodak Retirement Income Plan ("KRIP") is the major U.S. defined benefit pension plan. During the fourth quarter of 2008, the Kodak Retirement Income Plan Committee ("KRIPCO," the committee that oversees KRIP) approved a change to KRIP's asset portfolio with the intention of re-assessing the asset allocation and completing a new asset and liability study in early 2009. During the first quarter of 2009, as intended, KRIPCO again approved a change in the

asset allocation for the KRIP. A new asset and liability study was completed and resulted in an 8.75% expected long-term rate of return on plan asset assumption ("EROA"). As the KRIP was remeasured as of March 31, 2009, the Company's long-term assumption for EROA for the remainder of 2009 was updated at that time to reflect the change in asset allocation.

NOTE 13: EXTRAORDINARY ITEM

The terms of the purchase agreement of the 2004 acquisition of NexPress Solutions LLC called for additional consideration to be paid by the Company if sales of certain products exceeded stated minimum number of units sold during a five-year period following the close of transaction. In May 2009, the earn-out period lapsed with no additional consideration required to be paid by the Company. Negative goodwill, representing the contingent consideration obligation of \$17 million, was therefore reduced to zero. The reversal of negative goodwill reduced Property, plant and equipment, net by \$2 million and Research and development expense by \$7 million and resulted in an extraordinary gain of \$6 million, net of tax, during the quarter ended June 30, 2009.

NOTE 14: EARNINGS PER SHARE

Basic earnings per share computations are based on the weighted-average number of shares of common stock outstanding during the period(s) presented. As a result of the net loss from continuing operations presented for the three and six months ended June 30, 2009, the Company calculated diluted earnings per share using weighted-average basic shares outstanding for each period, as utilizing diluted shares would be anti-dilutive to loss per share.

The following potential shares of the Company's common stock were not included in the computation of diluted earnings per share for the three and six months ended June 30, 2009 because the Company reported a net loss from continuing operations; therefore, the effects would be anti-dilutive:

(in millions of shares)	Three Months	For the Ended June 30, 2009	Six Months
Total employee stock options outstanding	22.8		23.0
Total unvested share-based awards outstanding	2.9		2.9
Total anti-dilutive potential common shares	25.7		25.9

The majority of the Company's outstanding stock options would not have been dilutive, and, therefore, would not have been included in the computation of diluted earnings per share if the Company had reported earnings from continuing operations for the three and six months ended June 30, 2009, because their exercise prices exceeded the average market price of the Company's stock for both periods presented. For the three and six months ended June 30, 2008, only those outstanding stock options which were dilutive were included in the computation of diluted earnings per share.

Diluted earnings per share calculations may also reflect approximately 18.5 million shares related to the assumed conversion of approximately \$575 million in outstanding contingent convertible notes (the "Convertible Securities"), if dilutive. For the three months ended June 30, 2009, and the six months ended June 30, 2009 and 2008, the Company's diluted earnings or loss per share amounts exclude the effect of the Convertible Securities because they were anti-dilutive for those periods.

The computation of basic and diluted earnings from continuing operations per share of common stock for the three and six months ended June 30, 2008 is shown below:

(in millions)	For the Three Months Ended June 30, 2008		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Basic EPS:			
Earnings from continuing operations available to common stockholders	\$200	288.2	\$0.69
Effect of dilutive securities:			
Unvested share-based awards	\$-	1.6	
Convertible securities	\$5	18.5	
Diluted EPS:			
Adjusted earnings from continuing operations available to common stockholders and assumed issuances and conversions	\$205	308.3	\$0.66

(in millions)	For the Six Months Ended June 30, 2008		
	Earnings (Numerator)	Shares (Denominator)	Per Share Amount
Basic EPS:			
Earnings from continuing operations available to common stockholders	\$86	288.2	\$0.30
Effect of dilutive securities:			
Unvested share-based awards	\$-	1.5	
Diluted EPS:			
Adjusted earnings from continuing operations available to common stockholders and assumed issuances and conversions	\$86	289.7	\$0.30

NOTE 15: SHAREHOLDERS' EQUITY

The Company has 950 million shares of authorized common stock with a par value of \$2.50 per share, of which 391 million shares had been issued as of June 30, 2009 and December 31, 2008. Treasury stock at cost consists of approximately 123 million shares as of June 30, 2009 and December 31, 2008.

Comprehensive (Loss) Income

(in millions)	Three Months Ended		Six Months Ended		
	June 30,		June 30,		
	2009	2008	2009	2008	
Net (loss) earnings	\$(189	) \$495	\$(542	) \$380
Realized and unrealized gain (loss) from hedging activity, net of tax	6	(7) 14	(11)
Currency translation adjustments	23	(29	) (12	) 91
Pension and other postretirement benefit plan obligation activity, net of tax	(595	) 31	(544	) 95
Total comprehensive (loss) income, net of tax	\$(755	) \$490	\$(1,084	) \$555

NOTE 16: SEGMENT INFORMATION

Current Segment Reporting Structure

The Company has three reportable segments: Consumer Digital Imaging Group (“CDG”), Film, Photofinishing and Entertainment Group (“FPEG”), and Graphic Communications Group (“GCG”). The balance of the Company’s continuing operations, which individually and in the aggregate do not meet the criteria of a reportable segment, are reported in All Other. A description of the segments is as follows:

Consumer Digital Imaging Group Segment (“CDG”): CDG encompasses digital still and video cameras, digital devices such as picture frames, kiosks and related media, APEX drylab systems, consumer inkjet printing systems, Kodak Gallery products and services, and imaging sensors. CDG also includes the licensing activities related to the Company’s intellectual property in digital imaging products.

Film, Photofinishing and Entertainment Group Segment (“FPEG”): FPEG encompasses consumer and professional film, one-time-use cameras, graphic arts film, aerial and industrial film, and entertainment imaging products and services. In addition, this segment also includes paper and output systems, and photofinishing services. This segment provides consumers, professionals, cinematographers, and other entertainment imaging customers with film-related products and services and also provides graphic arts film to the graphics industry. As previously announced, Kodak closed its Qualex central lab operations in the U.S. and Canada at the end of March 2009.

Graphic Communications Group Segment (“GCG”): GCG serves a variety of customers in the creative, in-plant, data center, commercial printing, packaging, newspaper and digital service bureau market segments with a range of software, media and hardware products that provide customers with a variety of solutions for prepress equipment, workflow software, analog and digital printing, and document scanning. Products and related services include workflow software and digital controllers; digital printing, which includes commercial inkjet and electrophotographic products, including equipment, consumables and service; prepress consumables; prepress equipment; and document scanners.

All Other: All Other is composed of Kodak’s display business and other small, miscellaneous businesses.

Segment financial information is shown below:

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008
Net sales from continuing operations:				
Consumer Digital Imaging Group	\$503	\$756	\$872	\$1,310
Film, Photofinishing and Entertainment Group	593	847	1,096	1,571
Graphic Communications Group	670	880	1,273	1,692
All Other	-	2	2	5
Consolidated total	\$1,766	\$2,485	\$3,243	\$4,578

(in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2009	2008	2009	2008

(Loss) earnings from continuing operations before interest expense, other income (charges), net and income taxes:

Consumer Digital Imaging Group	\$(99)	\$(49)	\$(256)	\$(160)
Film, Photofinishing and Entertainment Group	51	54	59	80
Graphic Communications Group	(28)	13	(88)	12
All Other	(3)	(4)	(6)	(8)
Total of segments	(79)	14	(291)	(76)
Restructuring costs, rationalization and other	(46)	(3)	(162)	6
Other operating income (expenses), net	-	7	(3)	17
Legal contingencies and settlements	(1)	-	(6)	(10)
Negative goodwill reversal	7	-	7	-
Interest expense	(23)	(26)	(48)	(54)
Other income (charges), net	14	(5)	(1)	30
Consolidated loss from continuing operations before income taxes	\$(128)	\$(13)	\$(504)	\$(87)

(in millions)	As of	
	June 30, 2009	December 31, 2008

Segment total assets:

Consumer Digital Imaging Group	\$1,194	\$1,647
Film, Photofinishing and Entertainment Group	2,301	2,563

Edgar Filing: EASTMAN KODAK CO - Form 10-Q

Graphic Communications Group	1,826	2,190
All Other	5	8
Total of segments	5,326	6,408
Cash and marketable securities	1,141	2,155
Deferred income tax assets	639	620
Other corporate assets/reserves	-	(4)
Consolidated total assets	\$7,106	\$9,179

NOTE 17: FINANCIAL INSTRUMENTS

The following table presents the carrying amounts, estimated fair values, and location in the Consolidated Statement of Financial Position for the Company's financial instruments:

(in millions)	Balance Sheet Location	Assets			
		June 30, 2009		December 31, 2008	
		Carrying Amount	Fair Value	Carrying Amount	Fair Value
Marketable securities:					
Available-for-sale (1)	Other long-term assets	\$7	\$7	\$7	\$7
Held-to-maturity (2)	Other current assets and Other long-term assets	10	10	12	12
Derivatives designated as hedging instruments:					
Commodity contracts (1)	Other current assets	5	5	1	1
Derivatives not designated as hedging instruments:					
Foreign exchange contracts (1)	Other current assets	11	11	18	18
Liabilities					
(in millions)	Balance Sheet Location	Liabilities			
		June 30, 2009		December 31, 2008	
		Carrying Amount	Fair Value	Carrying Amount	Fair Value
Long-term borrowings, net of current portion (2)	Long-term debt, net of current portion	\$1,259	\$880	\$1,252	\$926
Derivatives designated as hedging instruments:					
Commodity contracts (1)	Accounts payable and other current liabilities	-	-	4	4
Derivatives not designated as hedging instruments:					
Foreign exchange contracts (1)	Accounts payable and other current liabilities	4	4	80	80
Foreign exchange contracts (1)	Other long-term liabilities	6	6	3	3

(1) Recorded at fair value.

(2) Recorded at historical cost.

Long-term debt is generally used to finance long-term investments, while short-term borrowings are used to meet working capital requirements. The Company does not utilize financial instruments for trading or other speculative purposes.

Fair value

The fair values of marketable securities are determined using quoted prices in active markets for identical assets (Level 1 fair value measurements). Fair values of the Company's forward contracts are determined using significant other observable inputs (Level 2 fair value measurements), and are based on the present value of expected future cash flows considering the risks involved and using discount rates appropriate for the duration of the contracts. Fair values of long-term borrowings are determined by reference to

quoted market prices, if available, or by pricing models based on the value of related cash flows discounted at current market interest rates. The carrying values of cash and cash equivalents, trade receivables, short-term borrowings and payables (which are not shown in the table above) approximate their fair values.

Foreign exchange

Foreign exchange gains and losses arising from transactions denominated in a currency other than the functional currency of the entity involved are included in Other income (charges), net in the accompanying Consolidated Statement of Operations. The net effects of foreign currency transactions, including related hedging activities, are shown below:

(in millions)	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	2009	2008	2009	2008
Net gain (loss)	\$5	\$(9	) \$(21) \$-

Derivative financial instruments

The Company, as a result of its global operating and financing activities, is exposed to changes in foreign currency exchange rates, commodity prices, and interest rates, which may adversely affect its results of operations and financial position. The Company manages such exposures, in part, with derivative financial instruments.

Foreign currency forward contracts are used to hedge existing foreign currency denominated assets and liabilities, especially those of the Company's International Treasury Center. Silver forward contracts are used to mitigate the Company's risk to fluctuating silver prices. The Company's exposure to changes in interest rates results from its investing and borrowing activities used to meet its liquidity needs.

The Company's financial instrument counterparties are high-quality investment or commercial banks with significant experience with such instruments. The Company manages exposure to counterparty credit risk by requiring specific minimum credit standards and diversification of counterparties. The Company has procedures to monitor the credit exposure amounts. The maximum credit exposure at June 30, 2009 was not significant to the Company.

In the event of a default under the Company's Amended Credit Agreement, or a default under any derivative contract or similar obligation of the Company, the derivative counterparties would have the right, although not the obligation, to require immediate settlement of some or all open derivative contracts at their then-current fair value, but with liability positions netted against asset positions with the same counterparty. At June 30, 2009, the Company had open derivative contracts in liability positions with a total fair value of \$10 million.

The location and amounts of gains and losses related to derivatives reported in the Consolidated Statement of Operations are shown in the following tables:

Derivatives in Cash Flow Hedging Relationships (in millions)	Gain (Loss) Recognized in OCI on Derivative (Effective Portion) For the three months ended June 30,		Gain (Loss) Reclassified from Accumulated OCI Into Cost of Goods Sold (Effective Portion) For the three months ended June 30,		Gain (Loss) Recognized in Income on Derivative (Ineffective Portion and Amount Excluded from Effectiveness Testing) For the three months ended June 30,	
	2009	2008	2009	2008	2009	2008
Commodity contracts	\$1	\$(7)	\$2	\$6	\$-	\$-
	For the six months ended June 30,		For the six months ended June 30,		For the six months ended June 30,	
	2009	2008	2009	2008	2009	2008
Commodity contracts	\$14	\$(11)	\$(1)	\$13	\$-	\$-

Derivatives Not Designated as Hedging Instruments (in millions)	Location of Gain or (Loss) Recognized in Income on Derivative	Gain (Loss) Recognized in Income on Derivative			
		For the three months ended June 30,		For the six months ended June 30,	
		2009	2008	2009	2008
Foreign exchange contracts	Other income (charges), net	\$39	\$(18)	\$35	\$26

Foreign currency forward contracts

The Company's foreign currency forward contracts used to hedge existing foreign currency denominated assets and liabilities are not designated as hedges, and are marked to market through net (loss) earnings at the same time that the exposed assets and liabilities are remeasured through net (loss) earnings (both in Other income (charges), net). The notional amount of such contracts open at June 30, 2009 was \$1.1 billion. The majority of the contracts of this type held by the Company are denominated in euros and British pounds.

Additionally, the Company may enter into foreign currency forward contracts that are designated as cash flow hedges of exchange rate risk related to forecasted foreign currency denominated purchases, sales and intercompany sales. There were no open contracts of this type at June 30, 2009.

Silver forward contracts

The Company enters into silver forward contracts that are designated as cash flow hedges of commodity price risk related to forecasted purchases of silver. The value of the notional amounts of such contracts open at June 30, 2009 was \$25 million. Hedge gains and losses related to these silver forward contracts are reclassified into cost of goods

sold as the related silver-containing products are sold to third parties. These gains or losses transferred to cost of goods sold are generally offset by increased or decreased costs of silver purchased in the open market. The amount of existing gains and losses at June 30, 2009 to be reclassified into earnings within the next 12 months is a net gain of \$7 million. At June 30, 2009, the Company had hedges of forecasted purchases through December 2009.

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

Overview

The Company's key priorities for 2009 are:

- Align the Company's cost structure with external economic realities
 - Fund core investments
 - Transform portions of its product portfolio
 - Drive positive cash flow before restructuring

The recessionary trends in the global economy, which began in 2008, continued to significantly affect the Company's revenue during the second quarter of 2009. The Company expects these trends to continue to affect its results for the balance of the year. The Company cannot anticipate with precision the duration and severity of the current economic downturn or when the economy may improve. However, the Company believes that the actions being taken, as described below, will help to mitigate the impacts to its results in 2009 and position it well for the future when the global economy does begin to rebound. The demand for the Company's consumer products was very weak in the first and second quarters of 2009 as a result of the drop-off of consumer discretionary spending, consistent with trends that emerged in the fourth quarter of 2008. In addition, as it did in late 2008, the weak economic environment continued to affect global print demand, which is a key driver of the Company's GCG business. The GCG equipment businesses also continue to be affected by the lack of credit availability in the financial markets. In anticipation of the continuation of the recession in 2009, the Company began to formulate and implement in the fourth quarter of 2008, and continues to implement, a number of actions it deems necessary in order to successfully accomplish the key priorities listed above.

Specifically, the Company has implemented actions to focus business investments in certain areas that are core to the Company's strategy (see below), while also maintaining an intense focus on cash generation and conservation in 2009. On April 30, 2009, the Company announced that its Board of Directors decided to suspend future cash dividends on its common stock effective immediately. Further, the Company also implemented temporary compensation-related actions, which reduced compensation for the chief executive officer and several other senior executives, as well as the Board of Directors, of the Company for the rest of 2009. In addition, U.S. based employees of the Company are required to take one week of unpaid leave during 2009. These actions are in addition to a targeted cost reduction program announced earlier this year (the 2009 Program). This 2009 cost reduction program is designed to more appropriately size the organization's cost structure with its expected revenue reductions as a result of the current economic environment. The program involves the rationalization of selling, marketing, administrative, research and development, supply chain and other business resources in certain areas and the consolidation of certain facilities. Also, the Company has initiated other actions to curb discretionary expenditures and employment-related costs, as well as to reduce capital expenditures where possible.

As previously disclosed, the Company also made a decision in late 2008 to focus its investments on businesses at the core of its strategy, which are consumer inkjet, commercial inkjet (including Stream technology) and enterprise workflow. The Company will continue to build upon its other cash generating businesses and reposition certain other businesses to generate maximum value.

In addition, on March 31, 2009, as previously disclosed, the Company and its Canadian subsidiary entered into an Amended and Restated Credit Agreement (the "Amended Credit Agreement") with its lenders, which provides for an asset-based revolving credit facility of up to \$500 million, under certain conditions, including up to \$250 million of availability for letters of credit. The Amended Credit Agreement provides continued financial flexibility for the

Company in this challenging economic environment.

Kodak Operating Model and Reporting Structure

The Company has three reportable segments: Consumer Digital Imaging Group (“CDG”), Film, Photofinishing and Entertainment Group (“FPEG”), and Graphic Communications Group (“GCG”). Within each of the Company’s reportable segments are various components, or Strategic Product Groups (“SPGs”). Throughout the remainder of this document, references to the segments’ SPGs are indicated in italics. The balance of the Company’s continuing operations, which individually and in the aggregate do not meet the criteria of a reportable segment, are reported in All Other. A description of the segments is as follows:

Consumer Digital Imaging Group Segment (“CDG”): CDG encompasses digital still and video cameras, digital devices such as picture frames, kiosks and related media, APEX drylab systems, consumer inkjet printing systems, Kodak Gallery products and services, and imaging sensors. CDG also includes the licensing activities related to the Company's intellectual property in digital imaging products.

Film, Photofinishing and Entertainment Group Segment (“FPEG”): FPEG encompasses consumer and professional film, one-time-use cameras, graphic arts film, aerial and industrial film, and entertainment imaging products and services. In addition, this segment also includes paper and output systems, and photofinishing services. This segment provides consumers, professionals, cinematographers, and other entertainment imaging customers with film-related products and services and also provides graphic arts film to the graphics industry. As previously announced, Kodak closed its Qualex central lab operations in the U.S. and Canada at the end of March 2009.

Graphic Communications Group Segment (“GCG”): GCG serves a variety of customers in the creative, in-plant, data center, commercial printing, packaging, newspaper and digital service bureau market segments with a range of software, media and hardware products that provide customers with a variety of solutions for prepress equipment, workflow software, analog and digital printing, and document scanning. Products and related services include workflow software and digital controllers; digital printing, which includes commercial inkjet and electrophotographic products, including equipment, consumables and service; prepress consumables; prepress equipment; and document scanners.

All Other: All Other is composed of Kodak's display business and other small, miscellaneous businesses.

Net Sales from Continuing Operations by Reportable Segment and All Other

(in millions)	Three Months Ended June 30,				Six Months Ended June 30,				
	2009	2008	Change	Foreign Currency Impact*	2009	2008	Change	Foreign Currency Impact*	
Consumer Digital Imaging Group									
Inside the U.S.	\$277	\$401	-31	% 0	% \$471	\$692	-32	% 0	%
Outside the U.S.	226	355	-36	-10	401	618	-35	-11	
Total Consumer Digital Imaging Group	503	756	-33	-5	872	1,310	-33	-5	
Film, Photofinishing and Entertainment Group									
Inside the U.S.	123	237	-48	0	246	436	-44	0	
Outside the U.S.	470	610	-23	-8	850	1,135	-25	-9	
Total Film, Photofinishing and Entertainment Group	593	847	-30	-6	1,096	1,571	-30	-6	
Graphic Communications Group									
Inside the U.S.	212	273	-22	0	410	540	-24	0	
Outside the U.S.	458	607	-25	-7	863	1,152	-25	-8	
Total Graphic Communications Group	670	880	-24	-5	1,273	1,692	-25	-5	
All Other									
Inside the U.S.	1	2	-	-	4	5	-	-	
Outside the U.S.	(1)	-	-	-	(2)	-	-	-	
Total All Other	-	2	-	-	2	5	-	-	
Consolidated									
Inside the U.S.	613	913	-33	0	1,131	1,673	-32	0	
Outside the U.S.	1,153	1,572	-27	-8	2,112	2,905	-27	-9	
Consolidated Total	\$1,766	\$2,485	-29	% -5	% \$3,243	\$4,578	-29	% -6	%

* Represents the percentage point change in segment net sales for the period that is attributable to foreign currency fluctuations

(Loss) Earnings from Continuing Operations Before Interest Expense, Other Income (Charges), Net and Income Taxes by Reportable Segment and All Other

(in millions)	Three Months Ended			Six Months Ended		
	2009	June 30, 2008	Change	2009	June 30, 2008	Change
Consumer Digital Imaging Group	\$ (99)	\$ (49)	-102 %	\$ (256)	\$ (160)	-60 %
Film, Photofinishing and Entertainment Group	51	54	-6 %	59	80	-26 %
Graphic Communications Group	(28)	13	-315 %	(88)	12	-833 %
All Other	(3)	(4)	+25 %	(6)	(8)	+25 %
Total of segments	\$ (79)	\$ 14	-664 %	\$ (291)	\$ (76)	-283 %
Percent of Sales	(4)%	1 %		(9)%	(2)%	
Restructuring costs, rationalization and other	(46)	(3)		(162)	6	
Other operating income (expenses), net	-	7		(3)	17	
Legal contingencies and settlements	(1)	-		(6)	(10)	
Negative goodwill reversal	7	-		7	-	
Interest expense	(23)	(26)		(48)	(54)	
Other income (charges), net	14	(5)		(1)	30	
Consolidated loss from continuing operations before income taxes	\$ (128)	\$ (13)	-885 %	\$ (504)	\$ (87)	-479 %

2009 COMPARED WITH 2008

Second Quarter

RESULTS OF OPERATIONS – CONTINUING OPERATIONS

CONSOLIDATED

(dollars in millions)

	Three Months Ended June 30,				Increase	
	2009	% of Sales	2008	% of Sales	/(Decrease)	% Change
Net sales	\$1,766		\$2,485		\$ (719)	-29 %
Cost of goods sold	1,440		1,899		(459)	-24 %
Gross profit	326	18.5 %	586	23.6 %	(260)	-44 %
Selling, general and administrative expenses	324	18 %	438	18 %	(114)	-26 %
Research and development costs	84	5 %	135	5 %	(51)	-38 %
Restructuring costs, rationalization and other	37		2		35	
Other operating expenses (income), net	-		(7)		7	-100 %
Loss from continuing operations before interest expense, other income (charges), net and income taxes	(119)	-7 %	18	1 %	(137)	-761 %
Interest expense	23		26		(3)	-12 %
Other income (charges), net	14		(5)		19	380 %
Loss from continuing operations before income taxes	(128)		(13)		(115)	-885 %
Provision (benefit) for income taxes	63		(213)		276	130 %
(Loss) earnings from continuing operations	(191)	-11 %	200	8 %	(391)	-196 %
(Loss) earnings from discontinued operations, net of income taxes	(4)		295		(299)	-101 %
Extraordinary item, net of tax	6		-		6	
NET (LOSS) EARNINGS ATTRIBUTABLE TO EASTMAN KODAK COMPANY	\$(189)		\$495		\$ (684)	-138 %

Three Months Ended

Edgar Filing: EASTMAN KODAK CO - Form 10-Q

	June 30,			Percent Change vs. 2008				Manufacturing and Other Costs
	2009 Amount	Change vs. 2008	Volume	Price/Mix	Foreign Exchange			
Net sales	\$1,766	-28.9 %	-17.7 %	-6.1 %	-5.1 %	n/a		
Gross profit margin	18.5 %	-5.1pp	n/a	-6.9pp	-3.2pp	5.0pp		

Executive Summary

The Company's operating results in the second quarter of 2009 continued to be negatively impacted by the decline in demand as a result of the global economic slowdown which began in 2008. The demand for the Company's consumer products is largely discretionary in nature, and sales and earnings of the Company's consumer businesses are linked to the timing of holidays, vacations, and other leisure or gifting seasons. Continued declines in consumer spending have had significant impacts in the Company's digital camera and digital picture frame businesses in the CDG segment. In addition, intellectual property royalty revenue within CDG decreased versus the prior year. In the GCG segment, lack of credit availability, combined with the weak economy, has resulted in low capital spending by businesses, negatively impacting sales. The reduction of global print demand had a negative impact on the GCG business. The Entertainment Imaging business within the FPEG segment continued to be negatively impacted by delays in the creation of feature films caused by the uncertainty around the Screen Actors' Guild contract, which expired in June 2008, and was not replaced until June 2009. In addition, the economic climate adversely impacted financing availability for independent film makers. Also, the secular decline of Film Capture continues to impact the traditional businesses. In response to the global economic slowdown, the Company implemented a targeted cost-reduction program and other measures as discussed in the Overview above.

Revenues

For the three months ended June 30, 2009, net sales decreased compared with the same period in 2008 primarily due to volume declines within all three segments driven by lower demand as a result of the global economic slowdown, particularly within Digital Capture and Devices in the CDG segment, and Prepress Solutions in the GCG segment, as well as continuing secular declines in Traditional Photofinishing and Film Capture in the FPEG segment. Unfavorable price/mix was primarily driven by Digital Capture and Devices within CDG, Entertainment Imaging within FPEG, and Prepress Solutions within GCG. Foreign exchange negatively impacted sales across all three segments, due to a strong U.S. dollar.

Gross Profit

Gross profit declined in the second quarter of 2009 in dollars and as a percentage of sales, primarily due to lower sales volumes as discussed above, as well as unfavorable price/mix, which impacted all segments but was most prominent in CDG, and unfavorable foreign exchange. These items were partially offset by cost improvements, driven by ongoing cost reduction efforts across all segments and lower raw material costs in FPEG.

The current quarter results also include a decline of approximately \$46 million in intellectual property royalty revenues as compared with the prior year quarter related to certain arrangements under which the Company fulfilled its continuing obligations as of the end of 2008, as well as overall volume declines in the digital capture device market. The Company expects to secure future licensing arrangements, the timing and amounts of which are difficult to predict. These types of arrangements provide the Company with a return on portions of historical research and development investments.

Selling, General and Administrative Expenses

The decrease in consolidated selling, general and administrative expenses (SG&A) was a result of company-wide cost reduction actions in response to the current economic conditions.

Research and Development Costs

The decrease in consolidated research and development (R&D) costs was a result of focused cost reduction efforts.

Restructuring Costs, Rationalization and Other

These costs, as well as the restructuring and rationalization-related costs reported in cost of goods sold, are discussed under the "RESTRUCTURING COSTS, RATIONALIZATION AND OTHER" section.

Other Income (Charges), Net

The other income (charges), net category primarily includes interest income, income and losses from equity investments, and foreign exchange gains and losses. The increase in other income (charges), net was primarily attributable to gains on foreign exchange in the second quarter of 2009 as compared with losses on foreign exchange in the prior year quarter, and expense related to support of an educational institution in the second quarter of 2008. This was partially offset by a decrease in interest income due to lower interest rates and lower cash balances in the second quarter of 2009 as compared with 2008.

Income Tax Provision (Benefit)

In June 2008, the Company received a tax refund from the U.S. Internal Revenue Service (IRS). This refund was related to the audit of certain claims filed for tax years 1993-1998. The refund had a positive impact on the Company's net earnings of \$565 million for the three months ended June 30, 2008, of which \$295 million of the refund is reflected in earnings from discontinued operations. The balance of \$270 million, which represents interest, is reflected in earnings from continuing operations.

(dollars in millions)

	Three Months Ended June 30,	
	2009	2008
Loss from continuing operations before income taxes	\$(128)	\$(13)
Provision (benefit) for income taxes	\$63	\$(213)
Effective tax rate	(49.2)%	1638.5 %

The change in the Company's effective tax rate from continuing operations is primarily attributable to: (1) a \$270 million benefit recognized during the second quarter of 2008 related to the aforementioned IRS refund; (2) losses generated in the U.S. and in certain jurisdictions outside the U.S. that were not benefited due to management's conclusion that it was not more likely than not that the tax benefits would be realized; (3) the impact of previously established valuation allowances in jurisdictions with current earnings; (4) changes to the mix of earnings from operations in certain lower-taxed jurisdictions outside the U.S.; (5) tax accounting impacts related to items reported in Accumulated other comprehensive income; and (6) adjustments for uncertain tax positions and audit settlements.

CONSUMER DIGITAL IMAGING GROUP

(dollars in millions)

	Three Months Ended June 30,				Increase	
	2009	% of Sales	2008	% of Sales	/(Decrease)	% Change
Net sales	\$503		\$756		\$(253)	-33 %
Cost of goods sold	448		610		(162)	-27 %
Gross profit	55	10.9 %	146	19.3 %	(91)	-62 %
Selling, general and administrative expenses	119	24 %	143	19 %	(24)	-17 %
Research and development costs	35	7 %	52	7 %	(17)	-33 %
	\$(99)	-20 %	\$(49)	-6 %	\$(50)	-102 %

Loss from continuing
operations before interest
expense, other
income(charges), net and
income taxes

	Three Months Ended June 30,			Percent Change vs. 2008					
	2009 Amount	Change vs. 2008	Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs			
Net sales	\$503	-33.5 %	-16.3 %	-12.6 %	-4.6 %	n/a			
Gross profit margin	10.9 %	-8.4pp	n/a	-15.3pp	-5.2pp	12.1pp			

Revenues

CDG's second quarter performance reflects the continued weakness in the global economy, combined with lower intellectual property royalty revenues. The demand for many of the consumer products within the CDG portfolio is discretionary in nature and consumer discretionary spending remains weak, leading to declines in CDG revenues in the second quarter.

The decrease in net sales for CDG was primarily driven by volume declines in Digital Capture and Devices. Net sales of Digital Capture and Devices, which includes consumer digital still and video cameras, digital picture frames, accessories, memory products, and intellectual property royalties, decreased 44% in the second quarter of 2009 as compared with the prior year quarter, primarily reflecting lower volumes and unfavorable price/mix of digital cameras and digital picture frames as a result of continuing weakness in consumer demand, and lower intellectual property royalties (see gross profit discussion below).

Net sales of Retail Systems Solutions, which includes kiosks and related media and APEX drylab systems, decreased 14% in the second quarter of 2009, primarily driven by unfavorable foreign exchange and lower media volumes. The decline in media volumes was largely driven by continued inventory contractions at major U.S. retailers.

Net sales of Consumer Inkjet Systems, which includes inkjet printers and related consumables, increased 20% due to higher volumes for printers and ink cartridges, partially offset by declines in media volumes. The volume increases experienced by the Company during the current economic situation, despite overall declines in the consumer printing industry, are reflective of favorable consumer response to the Company's unique value proposition.

Gross Profit

The decrease in gross profit, both in dollars and as a percentage of sales, for CDG was primarily attributable to unfavorable price/mix within Digital Capture and Devices, including lower intellectual property royalty revenues, and unfavorable foreign exchange. In addition, the decrease in gross profit dollars for CDG was due to lower sales volumes as discussed above. Partially offsetting these unfavorable factors was the benefit of lower product costs versus prior year.

The current quarter results include a decline of approximately \$46 million in intellectual property royalty revenues as compared with the prior year quarter related to certain arrangements under which the Company fulfilled its continuing obligations as of the end of 2008, as well as overall volume declines in the digital capture device market. The Company expects to secure future licensing arrangements, the timing and amounts of which are difficult to predict. These types of arrangements provide the Company with a return on portions of historical research and

development investments.

Selling, General and Administrative Expenses

The decrease in SG&A expenses for CDG was primarily driven by focused cost reduction actions to respond to the current economic conditions, partially offset by increased advertising expense related to Consumer Inkjet Systems.

Research and Development Costs

The decrease in R&D costs for CDG was primarily attributable to lower spending related to Consumer Inkjet Systems, resulting from the movement of product offerings from the development phase into the market introduction and growth phases, as well as portfolio rationalization within the other CDG businesses.

FILM, PHOTOFINISHING AND ENTERTAINMENT GROUP

(dollars in millions)

	Three Months Ended June 30,				Increase	
	2009	% of Sales	2008	% of Sales	/(Decrease)	% Change
Net sales	\$593		\$847		\$ (254)	-30 %
Cost of goods sold	460		662		(202)	-31 %
Gross profit	133	22.4 %	185	21.8 %	(52)	-28 %
Selling, general and administrative expenses	73	12 %	117	14 %	(44)	-38 %
Research and development costs	9	2 %	14	2 %	(5)	-36 %
Earnings from continuing operations before interest expense, other income (charges), net and income taxes	\$51	9 %	\$54	6 %	\$ (3)	-6 %

	Three Months Ended June 30,			Percent Change vs. 2008		
	2009 Amount	Change vs. 2008	Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
Net sales	\$593	-30.0 %	-20.1 %	-4.0 %	-5.9 %	n/a
Gross profit margin	22.4 %	0.6pp	n/a	-5.0pp	-3.9pp	9.5pp

Revenues

The decrease in net sales for FPEG was driven by revenue declines across all SPGs within the segment. Net sales of Film Capture decreased 43% in the three months ended June 30, 2009 as compared with the second quarter of 2008 due to secular declines in the industry. The decrease in net sales for Entertainment Imaging of 25% from the prior year quarter primarily reflects lower volumes due to (1) the uncertainty around the Screen Actors' Guild contract, which expired in June 2008 and was not replaced until June 2009, and (2) the impact of the economic climate on financing availability for independent film makers, which together have resulted in delays in the creation of feature films. Unfavorable foreign exchange and price/mix also negatively impacted sales for Entertainment Imaging. Traditional Photofinishing sales decreased 28% from the prior year quarter, primarily driven by volume declines resulting from the previously announced closure of the Qualex central lab operations in the U.S. and Canada at the end of March 2009.

Gross Profit

The decrease in FPEG gross profit dollars was primarily driven by lower sales volumes as mentioned above, and unfavorable foreign exchange and price/mix within Entertainment Imaging. The increase in gross profit as a percentage of sales was primarily reflective of the lower costs of silver, paper, and petroleum-based raw materials, lower benefit costs as a result of amendments made in the third quarter of 2008 to certain of the Company's U.S. postemployment benefits, and other cost improvements.

Selling, General and Administrative Expenses

The decline in SG&A expenses for FPEG was attributable to focused cost reduction actions to respond to current economic conditions, as well as lower postemployment benefit costs and the aforementioned closure of Qualex operations in the U.S. and Canada.

GRAPHIC COMMUNICATIONS GROUP

(dollars in millions)

	Three Months Ended June 30,				Increase	
	2009	% of Sales	2008	% of Sales	/(Decrease)	% Change
Net sales	\$670		\$880		\$ (210)	-24 %
Cost of goods sold	522		626		(104)	-17 %
Gross profit	148	22.1 %	254	28.9 %	(106)	-42 %
Selling, general and administrative expenses	132	20 %	178	20 %	(46)	-26 %
Research and development costs	44	7 %	63	7 %	(19)	-30 %
(Loss) earnings from continuing operations before interest expense, other income (charges), net and income taxes	\$(28)	-4 %	\$13	1 %	\$(41)	-315 %

	Three Months Ended June 30,			Percent Change vs. 2008		
	2009 Amount	Change vs. 2008	Volume	Price/Mix	Foreign Exchange	Manufacturing and Other Costs
Net sales	\$670	-23.9 %	-16.6 %	-2.4 %	-4.9 %	n/a
Gross profit margin	22.1 %	-6.8pp	n/a	-2.8pp	-1.0pp	-3.0pp

Revenues

GCG's second quarter revenue declines reflect the impact of ongoing global economic uncertainties, which have depressed global print demand and associated capital investments in the printing industry.

The decrease in GCG net sales for the quarter was driven by volume declines and unfavorable foreign exchange across all product lines. Unfavorable price/mix, primarily within Prepress Solutions and Digital Printing Solutions, reflects both a shift in demand toward products requiring lower levels of investment and increased price pressures due to the economic downturn in the industry.

Net sales of Prepress Solutions decreased 27%, primarily driven by volume declines, as well as unfavorable foreign exchange and price/mix. The volume decreases resulted from the decline in worldwide print demand, which reduced demand for plate consumables and prepress equipment.

Net sales of Digital Printing Solutions decreased 20%, resulting from unfavorable volume, price/mix and foreign exchange. Equipment volumes decreased as the printing industry remains cautious regarding capital investments in the current economic environment. While overall consumable volumes also decreased, color electrophotographic consumable volumes increased due to an increase in the equipment installed base for that product line. Unfavorable price/mix was driven by general price erosion and capital investments that were skewed toward lower-priced models.

Net sales of Document Imaging decreased by 4%, primarily driven by unfavorable foreign exchange. The volume declines for scanning and imaging products were largely offset by volume increases in business process services, and favorable price/mix.

Net sales of Enterprise Solutions decreased 43%, primarily due to volume declines in sales of workflow software and print controllers, as a result of fewer prepress equipment placements and third party digital printer sales that resulted from the decline in worldwide print demand.

Gross Profit

Gross profit declined both in dollars and as a percentage of sales across all SPGs, as volume, price/mix, foreign exchange, and manufacturing cost were unfavorable. The decline in global print demand negatively impacted equipment and consumables sales volumes, driving down gross profit dollars while also leading the Company to reduce its production levels, which resulted in lower levels of factory absorption and higher unit manufacturing costs. This impact was most pronounced in Prepress Solutions but was also a factor in the performance of all other SPGs. Constrained demand drove increased price pressures in the industry as capital investments continue to be depressed, which drove unfavorable price/mix in Prepress Solutions and Digital Printing Solutions.

Selling, General and Administrative Expenses

The decrease in SG&A expenses for GCG was primarily attributable to focused cost reduction actions to respond to the current economic conditions.

Research and Development Costs

The decrease in R&D costs for GCG was largely driven by a rationalization and refocusing of investments.

Year to Date

RESULTS OF OPERATIONS – CONTINUING OPERATIONS

CONSOLIDATED

(dollars in millions)

	Six Months Ended		Six Months Ended		Increase / (Decrease)	% Change
	2009	% of Sales	2008	% of Sales		
Net sales	\$3,243		\$4,578		\$ (1,335)	-29 %
Cost of goods sold	2,723		3,568		(845)	-24 %
Gross profit	520	16.0 %	1,010	22.1 %	(490)	-49 %
Selling, general and administrative expenses	637	20 %	829	18 %	(192)	-23 %
Research and development costs	189	6 %	269	6 %	(80)	-30 %
Restructuring costs, rationalization and other	146		(8)		154	1925 %
Other operating expenses (income), net	3		(17)		20	118 %
Earnings (loss) from continuing operations before interest expense, other (charges) income, net and						
income taxes	(455)	-14 %	(63)	-1 %	(392)	-622 %
Interest expense	48		54			