ALLEGHENY TECHNOLOGIES INC
Form 10-Q
August 02, 2007

Table of Contents

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

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the Quarterly Period Ended June 30, 2007

OR

o **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 1-12001

ALLEGHENY TECHNOLOGIES INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware	25-1792394
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1000 Six PPG Place Pittsburgh, Pennsylvania	15222-5479
(Address of Principal Executive Offices)	(Zip Code)

(412) 394-2800

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes þ No o

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o

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

Yes o No þ

At July 27, 2007, the registrant had outstanding 102,217,501 shares of its Common Stock.

ALLEGHENY TECHNOLOGIES INCORPORATED
SEC FORM 10-Q
QUARTER ENDED June 30, 2007
INDEX

Table of Contents

PART I. FINANCIAL INFORMATION
Item 1. Financial Statements
ALLEGHENY TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In millions, except share and per share amounts)

	June 30, 2007 (Unaudited)	December 31, 2006 (Audited)
ASSETS		
Cash and cash equivalents	$ 529.6	$ 502.3
Accounts receivable, net	709.9	610.9
Inventories, net	1,054.0	798.7
Deferred income taxes	26.4	26.6
Prepaid expenses and other current assets	34.7	49.4
Total Current Assets	2,354.6	1,987.9
Property, plant and equipment, net	980.2	871.7
Cost in excess of net assets acquired	209.4	206.5
Deferred income taxes	117.9	119.0
Prepaid pension cost	11.2	
Other assets	112.8	95.4
Total Assets	**$ 3,786.1**	**$ 3,280.5**
LIABILITIES AND STOCKHOLDERS EQUITY		
Accounts payable	$ 445.3	$ 355.1
Accrued liabilities	229.9	241.6
Accrued income taxes	66.2	22.7
Short-term debt and current portion of long-term debt	22.2	23.7
Total Current Liabilities	763.6	643.1
Long-term debt	518.5	529.9
Retirement benefits	452.0	464.4
Other long-term liabilities	170.2	140.2
Total Liabilities	**1,904.3**	**1,777.6**
Stockholders Equity:		
Preferred stock, par value $0.10: authorized- 50,000,000 shares; issued-none		
Common stock, par value $0.10, authorized-500,000,000 shares; issued-102,404,256 shares at June 30, 2007 and 101,201,411 at December 31, 2006; outstanding-102,207,876 shares at June 30, 2007 and 101,201,328 shares at December 31, 2006	10.2	10.1
Additional paid-in capital	656.9	637.0
Retained earnings	1,524.1	1,166.6

Treasury stock: 196,380 shares at June 30, 2007 and 83 shares at December 31, 2006		(19.5)		
Accumulated other comprehensive loss, net of tax		(289.9)		(310.8)
Total Stockholders Equity		**1,881.8**		**1,502.9**
Total Liabilities and Stockholders Equity	**$**	**3,786.1**	**$**	**3,280.5**

The accompanying notes are an integral part of these statements.

Table of Contents

ALLEGHENY TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(In millions except per share amounts)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Sales	$ 1,471.3	$ 1,210.8	$ 2,843.9	$ 2,251.3
Costs and expenses:				
Cost of sales	1,069.8	918.7	2,055.9	1,711.1
Selling and administrative expenses	72.7	75.4	150.8	148.3
Income before interest, other income (expense), and income taxes	328.8	216.7	637.2	391.9
Interest expense, net	(2.6)	(5.8)	(6.9)	(13.3)
Other income (expense)	(0.3)	(1.2)	0.2	(2.5)
Income before income tax provision	325.9	209.7	630.5	376.1
Income tax provision	119.4	65.4	226.2	125.3
Net income	$ 206.5	$ 144.3	$ 404.3	$ 250.8
Basic net income per common share	$ 2.03	$ 1.45	$ 3.98	$ 2.53
Diluted net income per common share	$ 2.00	$ 1.41	$ 3.93	$ 2.46
Dividends declared per common share	$ 0.13	$ 0.10	$ 0.26	$ 0.20

The accompanying notes are an integral part of these statements.

Table of Contents

ALLEGHENY TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)
(Unaudited)

	Six Months Ended June 30, 2007	Six Months Ended June 30, 2006
Operating Activities:		
Net income	$ 404.3	$ 250.8
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	48.6	39.9
Deferred income taxes	9.2	(5.6)
Change in operating assets and liabilities:		
Inventories	(255.3)	(228.5)
Accounts receivable	(99.0)	(118.3)
Accounts payable	90.2	83.8
Accrued income taxes, net of tax benefits on share-based compensation	43.5	8.5
Retirement benefits	4.4	26.1
Accrued liabilities and other	(59.2)	(25.6)
Cash provided by operating activities	**186.7**	**31.1**
Investing Activities:		
Purchases of property, plant and equipment	(151.5)	(103.5)
Asset disposals and other	4.2	1.5
Cash used in investing activities	**(147.3)**	**(102.0)**
Financing Activities:		
Payments on long-term debt and capital leases	(9.6)	(5.9)
Net borrowings (repayments) under credit facilities	(3.4)	3.5
Net decrease in debt	(13.0)	(2.4)
Dividends paid	(26.5)	(20.0)
Tax benefits on share-based compensation	22.4	16.5
Exercises of stock options	5.0	27.3
Cash provided by (used in) financing activities	**(12.1)**	**21.4**
Increase (decrease) in cash and cash equivalents	**27.3**	**(49.5)**
Cash and cash equivalents at beginning of the year	**502.3**	**362.7**
Cash and cash equivalents at end of period	**$ 529.6**	**$ 313.2**

The accompanying notes are an integral part of these statements.

Table of Contents

ALLEGHENY TECHNOLOGIES INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
Unaudited

Note 1. Accounting Policies

Basis of Presentation

The interim consolidated financial statements include the accounts of Allegheny Technologies Incorporated and its subsidiaries. Unless the context requires otherwise, Allegheny Technologies , ATI and the Company refer to Allegheny Technologies Incorporated and its subsidiaries.

These unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles for interim financial information and with the instructions for Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and note disclosures required by U.S. generally accepted accounting principles for complete financial statements. In management s opinion, all adjustments (which include only normal recurring adjustments) considered necessary for a fair presentation have been included. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company s 2006 Annual Report on Form 10-K. The results of operations for these interim periods are not necessarily indicative of the operating results for any future period.

Recent Accounting Pronouncements

In the 2007 first quarter, as required, the Company adopted Financial Accounting Standards Board (FASB) Staff Position (FSP) titled Accounting for Planned Major Maintenance Activities (FSP PMMA). This FSP amends an AICPA Industry Audit guide and is applicable to all industries that accrue for planned major maintenance activities. The FSP PMMA prohibits the use of the accrue-in-advance method of accounting for planned major maintenance activities, which was the policy the Company previously used to record planned plant outage costs on an interim basis within a fiscal year, and also to record the costs of major equipment rebuilds which extend the life of capital equipment. The FSP PMMA was effective as of the beginning of ATI s 2007 fiscal year, with retrospective application to all prior periods presented. Under the FSP PMMA, the Company reports results using the deferral method whereby major equipment rebuilds are capitalized as costs are incurred and amortized to expense over the estimated useful lives, and planned plant outage costs are fully recognized in the interim period of the outage. The adoption of the FSP PMMA on January 1, 2007, resulted in an increase in net property, plant and equipment of $4.1 million, a decrease in non-current deferred income tax assets of $5.8 million, a decrease in accrued liabilities of $2.4 million, a decrease in long-term liabilities of $9.6 million, and an increase to retained earnings of $10.3 million, net of related taxes. As required by the FSP PMMA, the Company s financial statements have been restated to reflect this FSP as if this standard had been applied to the earliest period presented. As a result, net income for the three and six months ended June 30, 2006 increased $3.9 million, or $0.04 per share, and $7.9 million, or $0.08 per share, respectively.

In the 2007 first quarter, as required, the Company also adopted FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes (FIN 48), an interpretation of FASB Statement No. 109, Accounting for Income Taxes . FIN 48 prescribes recognition and measurement standards for a tax position taken or expected to be taken in a tax return. The evaluation of a tax position in accordance with FIN 48 is a two step process. The first step is the determination of whether a tax position should be recognized in the financial statements. Under FIN 48, a tax position taken or expected to be taken in a tax return is to be recognized only if the Company determines that it is more-likely-than-not that the tax position will be sustained upon examination by the tax authorities based upon the technical merits of the position. In step two, for those tax positions which should be recognized, the measurement of a tax position is determined as being the largest amount of benefit that is greater than 50% likely of being realized upon ultimate settlement. FIN 48 was effective for the beginning of ATI s 2007 fiscal year, with adoption treated as a cumulative-effect type reduction to retained earnings of $5.6 million as of the beginning of 2007. Upon adoption of FIN 48, the Company made an accounting policy election to classify interest and penalties on estimated liabilities for uncertain tax positions as components of the provision for income taxes.

Table of Contents

Note 2. Inventories

Inventories at June 30, 2007 and December 31, 2006 were as follows (in millions):

	June 30, 2007	December 31, 2006
Raw materials and supplies	$ 214.4	$ 190.7
Work-in-process	1,180.8	931.7
Finished goods	173.3	148.0
Total inventories at current cost	1,568.5	1,270.4
Less allowances to reduce current cost values to LIFO basis	(509.3)	(466.7)
Progress payments	(5.2)	(5.0)
Total inventories, net	$ 1,054.0	$ 798.7

Inventories are stated at the lower of cost (last-in, first-out (LIFO), first-in, first-out (FIFO), and average cost methods) or market, less progress payments. Most of the Company s inventory is valued utilizing the LIFO costing methodology. Inventory of the Company s non-U.S. operations is valued using average cost or FIFO methods. The effect of using the LIFO methodology to value inventory, rather than FIFO, increased cost of sales by $21.7 million for the 2007 second quarter and $42.6 million for the first six months of 2007, compared to $45.5 million for the 2006 second quarter and $52.4 million for the first six months of 2006. The LIFO inventory valuation reserve charge for the 2007 second quarter includes approximately $16 million associated with the effects of projected liquidations of LIFO inventory quantities carried at the lower costs prevailing in prior years as compared to current costs.

Note 3. Supplemental Financial Statement Information

Property, plant and equipment at June 30, 2007 and December 31, 2006 were as follows (in millions):

	June 30, 2007	December 31, 2006
Land	$ 24.2	$ 23.9
Buildings	245.2	242.1
Equipment and leasehold improvements	1,834.1	1,690.3
	2,103.5	1,956.3
Accumulated depreciation and amortization	(1,123.3)	(1,084.6)
Total property, plant and equipment, net	$ 980.2	$ 871.7

Table of Contents

Note 4. Debt

Debt at June 30, 2007 and December 31, 2006 was as follows (in millions):

	June 30, 2007	December 31, 2006
Allegheny Technologies $300 million 8.375% Notes due 2011, net (a)	$ 305.9	$ 306.5
Allegheny Ludlum 6.95% debentures, due 2025	150.0	150.0
Promissory note for J&L asset acquisition	48.4	54.0
Domestic Bank Group $325 million secured credit agreement		
Foreign credit agreements	21.5	24.2
Industrial revenue bonds, due through 2020	10.9	10.9
Capitalized leases and other	4.0	8.0
Total short-term and long-term debt	540.7	553.6
Short-term debt and current portion of long-term debt	(22.2)	(23.7)
Total long-term debt	$ 518.5	$ 529.9

(a) Includes fair value adjustments for settled interest rate swap contracts of $9.6 million at June 30, 2007 and $10.5 million at December 31, 2006.

Interest expense was $17.7 million and $19.8 million for the six months ended June 30, 2007 and 2006, respectively. Interest expense was reduced by $3.2 million and $2.2 million for the six months ended June 30, 2007 and 2006, respectively, for interest capitalization on capital projects. Net interest expense includes interest income of $10.8 million and $6.5 million for the six months ended June 30, 2007 and 2006, respectively.

The Company had a $325 million senior secured domestic revolving credit facility (the former facility), which was secured by all accounts receivable and inventory of its U.S. operations, and included capacity for up to $175 million in letters of credit. As of June 30, 2007, there had been no borrowings made under the former facility, although a portion of the former facility was used to support approximately $81 million in letters of credit. In addition, STAL, the Company s Chinese joint venture company in which ATI has a 60% interest, had approximately $17 million in letters of credit outstanding as of June 30, 2007, related to the expansion of its operations in Shanghai, China. These letters of credit are supported solely by STAL s financial capability without any guarantees from the joint venture partners.

Effective July 31, 2007, the Company replaced the existing $325 million senior secured domestic revolving credit facility with a new five-year $400 million senior unsecured domestic revolving credit facility (the new unsecured facility). The new unsecured facility includes a $200 million sublimit for the issuance of letters or credit. Under the new unsecured facility, the Company may increase the size of the credit facility by up to $100 million without seeking the further approval of the lending group. The new unsecured facility requires the Company to maintain a leverage ratio (consolidated total indebtedness divided by consolidated earnings before interest, taxes and depreciation and amortization) of not greater than 3.25, and maintain an interest coverage ratio (consolidated earnings before interest and taxes divided by interest expense) of not less than 2.0.

Borrowings or letter of credit issuance under the new unsecured facility bear interest at the Company s option at either: (1) the one-, two-, three- or six-month LIBOR rate plus a margin ranging from 0.625% to 1.25% depending upon the value of the leverage ratio as defined by the new unsecured facility agreement; or (2) a base rate announced from time-to-time by the lending group (i.e. the Prime lending rate). In addition, the new unsecured facility contains a facility fee of 0.15% to 0.30% depending upon the value of the leverage ratio, and a letter of credit issuance fee of 0.125%. The Company s overall borrowing costs under the new unsecured facility are not affected by changes in the Company s credit ratings.

Table of Contents

Note 5. Per Share Information

The following table sets forth the computation of basic and diluted net income per common share (in millions, except share and per share amounts):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Numerator for basic and diluted net income per common share net income	$ 206.5	$ 144.3	$ 404.3	$ 250.8
Denominator:				
Denominator for basic net income per common share-weighted average shares	101.8	99.7	101.6	99.2
Effect of dilutive securities:				
Option equivalents	0.6	1.2	0.6	1.4
Contingently issuable shares	0.6	1.5	0.7	1.5
Denominator for diluted net income per common share adjusted weighted average shares and assumed conversions	103.0	102.4	102.9	102.1
Basic net income per common share	$ 2.03	$ 1.45	$ 3.98	$ 2.53
Diluted net income per common share	$ 2.00	$ 1.41	$ 3.93	$ 2.46

For the quarter and six months ended June 30, 2007, there were no weighted average shares issuable upon the exercise of stock options which were antidilutive. The 2006 quarter and six month periods included a negligible amount of antidilutive weighted average shares issuable upon the exercise of stock options.

Note 6. Comprehensive Income

The components of comprehensive income, net of tax, were as follows (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Net income	$ 206.5	$ 144.3	$ 404.3	$ 250.8
Foreign currency translation gains	3.1	18.1	11.1	21.8
Unrealized gains (losses) on energy, raw material and currency hedges, net of tax	(19.5)	4.4	(7.9)	(6.4)
Retirement benefits	5.6		18.2	
Unrealized gains (losses) on securities	(0.9)	0.1	(0.5)	0.1
	(11.7)	22.6	20.9	15.5
Comprehensive income	$ 194.8	$ 166.9	$ 425.2	$ 266.3

Note 7. Income Taxes

Results for the second quarter 2007 included a provision for income taxes of $119.4 million, or 36.6% of income before tax, compared to an income tax provision of $65.4 million, or 31.2% of income before tax, for the comparable 2006 quarter. The second quarter 2006 benefited from the elimination of a $10.2 million deferred tax valuation allowance with respect to certain state tax credits. The income tax provision for the six months ended June 30, 2007 was $226.2 million, or 35.9% of income before tax, compared to an income tax provision of $125.3 million, or 33.3% of tax for the comparable prior year period.

Table of Contents

As required, the Company adopted FIN 48 on January 1, 2007. As a result of implementing this Interpretation, the Company recognized a $19.4 million increase in the long-term liability for unrecognized tax benefits, and a $13.8 million increase in deferred tax assets for tax positions which the ultimate deductibility is highly certain, but for which there is uncertainty about the timing of such deductibility. Because of the impact of deferred tax accounting, other than interest and penalties, the disallowance of the shorter deductibility period would not affect the annual effective tax rate but would accelerate the payment of cash to the taxing authority to an earlier period. The net result of these recognized assets and liabilities was a reduction to beginning retained earnings of $5.6 million. Including liabilities recognized in the FIN 48 adoption, the Company s total liabilities for unrecognized tax benefits at January 1, 2007 were $26.3 million. Interest and penalties recognized at the FIN 48 adoption were $3.5 million. It is the Company s policy to classify interest and penalties recognized on underpayment of income taxes as income tax expense. For the six months ended June 30, 2007, the Company s income tax provision included $6.8 million of expense related to uncertain tax positions including $1.0 million of interest and penalties, which increased the long-term liability to $33.1 million, which included $4.5 million of interest and penalties.

Including tax positions for which the Company determined that the tax position would not meet the more-likely-than-not recognition threshold upon examination by the tax authorities based upon the technical merits of the position, the total estimated unrecognized tax benefit that, if recognized, would affect the Company s effective tax rate was approximately $16 million. At this time, the Company does not believe that it is reasonably possible that there will be a material change in the estimated unrecognized tax benefits within the next twelve months.

The Company, and/or one of its subsidiaries, files income tax returns in the U.S. Federal jurisdiction and in various states and foreign jurisdictions. A summary of tax years that remain subject to examination, by major tax jurisdiction, is as follows:

Jurisdiction	Earliest Year Open to Examination
U.S. Federal	2003
States:	
Pennsylvania	2003
North Carolina	2003
Texas	2002
Foreign:	
Germany	2000
United Kingdom	2005

Note 8. Pension Plans and Other Postretirement Benefits

The Company has defined benefit pension plans and defined contribution plans covering substantially all employees. Benefits under the defined benefit pension plans are generally based on years of service and/or final average pay. The Company funds the U.S. pension plans in accordance with the Employee Retirement Income Security Act of 1974, as amended, and the Internal Revenue Code.

The Company also sponsors several postretirement plans covering certain salaried and hourly employees. The plans provide health care and life insurance benefits for eligible retirees. In most plans, Company contributions towards premiums are capped based on the cost as of a certain date, thereby creating a defined contribution. For the non-collectively bargained plans, the Company maintains the right to amend or terminate the plans at its discretion.

Table of Contents

For the three months and six months ended June 30, 2007 and 2006, the components of pension expense for the Company s defined benefit plans and components of other postretirement benefit expense included the following (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Pension Benefits:				
Service cost benefits earned during the year	$ 6.9	$ 7.1	$ 13.8	$ 14.2
Interest cost on benefits earned in prior years	31.8	32.0	63.7	64.1
Expected return on plan assets	(46.7)	(40.6)	(93.4)	(81.2)
Amortization of prior service cost	4.4	4.8	8.8	9.6
Amortization of net actuarial loss	7.8	12.6	15.6	25.2
Total pension expense	$ 4.2	$ 15.9	$ 8.5	$ 31.9

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Other Postretirement Benefits:				
Service cost benefits earned during the year	$ 0.7	$ 0.7	$ 1.5	$ 1.4
Interest cost on benefits earned in prior years	7.8	7.9	15.5	16.0
Expected return on plan assets	(1.8)	(1.6)	(3.6)	(3.2)
Amortization of prior service cost (credit)	(5.5)	(6.6)	(11.7)	(13.2)
Amortization of net actuarial loss	2.1	4.0	4.9	8.0
Total other postretirement benefit expense	$ 3.3	$ 4.4	$ 6.6	$ 9.0
Total retirement benefit expense	$ 7.5	$ 20.3	$ 15.1	$ 40.9

Table of Contents

Note 9. Business Segments

Following is certain financial information with respect to the Company s business segments for the periods indicated (in millions):

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
Total sales:				
High Performance Metals	$ 612.6	$ 486.1	$ 1,131.3	$ 917.4
Flat-Rolled Products	822.3	667.5	1,633.0	1,206.3
Engineered Products	115.6	114.4	233.4	229.5
	1,550.5	1,268.0	2,997.7	2,353.2
Intersegment sales:				
High Performance Metals	54.9	35.9	96.2	55.1
Flat-Rolled Products	17.7	16.7	44.7	38.3
Engineered Products	6.6	4.6	12.9	8.5
	79.2	57.2	153.8	101.9
Sales to external customers:				
High Performance Metals	557.7	450.2	1,035.1	862.3
Flat-Rolled Products	804.6	650.8	1,588.3	1,168.0
Engineered Products	109.0	109.8	220.5	221.0
	$ 1,471.3	$ 1,210.8	$ 2,843.9	$ 2,251.3
Operating profit:				
High Performance Metals	$ 180.2	$ 157.2	$ 347.7	$ 302.4
Flat-Rolled Products	166.3	86.5	326.5	138.0
Engineered Products	10.7	15.2	23.3	33.0
Total operating profit	357.2	258.9	697.5	473.4
Corporate expenses	(17.4)	(18.0)	(38.4)	(31.9)
Interest expense, net	(2.6)	(5.8)	(6.9)	(13.3)
Other expense, net of gains on asset sales	(3.8)	(5.1)	(6.6)	(11.2)
Retirement benefit expense	(7.5)	(20.3)	(15.1)	(40.9)
Income before income taxes	$ 325.9	$ 209.7	$ 630.5	$ 376.1

The adoption of FSP PMMA on January 1, 2007 resulted in restating prior periods as if this standard had been applied to the earliest period presented. For the quarter and six months ended June 30, 2006, the restatement had the following effect on operating profit by business segment: High Performance Metals increased $2.0 million and $4.5 million, respectively, Flat-Rolled Products increased $4.2 million and $7.7 million, respectively, and Engineered Products had no change in the second quarter 2006 and increased $0.2 million in the first half 2006. Segment operating profit and income before income taxes for the quarter and six months ended June 30, 2006 increased $6.2

million and $12.4 million, respectively.

Retirement benefit expense represents pension expense and other postretirement benefit expense. Operating profit with respect to the Company s business segments excludes any retirement benefit expense.

In March 2007, the Company reached early resolution on new labor agreements for ATI Allegheny Ludlum and ATI s Allvac Albany, OR employees. Operating profit for the six months ended June 30, 2007 for the High Performance Metals and Flat-Rolled Products segments was negatively impacted by $0.7 million and $4.8 million, respectively, of pre-tax, one-time costs related to the new labor agreements.

Corporate expenses for the three months ended June 30, 2007 were $17.4 million, compared to $18.0 million for the comparable period of 2006. This decrease was primarily due to lower expenses associated with long-term performance-based cash incentive compensation programs. For the six months ended June 30, 2007, corporate expenses increased to $38.4 million compared to $31.9 million primarily related to annual and long-term performance-based incentive compensation programs.

Other expense, net of gains on asset sales, includes charges incurred in connection with closed operations, pretax gains and losses on the sale of surplus real estate and other assets, and other non-operating income or expense. These items are presented primarily in selling and administrative expenses and in other expense in the statement of income.

Note 10. Financial Information for Subsidiary and Guarantor Parent

The payment obligations under the $150 million 6.95% debentures due 2025 issued by Allegheny Ludlum Corporation (the Subsidiary) are fully and unconditionally guaranteed by Allegheny Technologies Incorporated (the Guarantor Parent). In accordance with positions established by the Securities and Exchange Commission, the following financial information sets forth separately financial information with respect to the Subsidiary, the non-guarantor subsidiaries and the Guarantor Parent. The principal elimination entries eliminate investments in subsidiaries and certain intercompany balances and transactions. Investments in subsidiaries, which are eliminated in consolidation, are included in other assets on the balance sheets.

Allegheny Technologies is the plan sponsor for the U.S. qualified defined benefit pension plan (the Plan) which covers certain current and former employees of the Subsidiary and the non-guarantor subsidiaries. As a result, the balance sheets presented for the Subsidiary and the non-guarantor subsidiaries do not include any Plan assets or liabilities, or the related deferred taxes. The Plan assets, liabilities and related deferred taxes and pension income or expense are recognized by the Guarantor Parent. Management and royalty fees charged to the Subsidiary and to the non-guarantor subsidiaries by the Guarantor Parent have been excluded solely for purposes of this presentation.

Table of Contents

Allegheny Technologies Incorporated
Financial Information for Subsidiary and Guarantor Parent
Balance Sheets
June 30, 2007

(In millions)	Guarantor Parent	Subsidiary	Non-guarantor Subsidiaries	Eliminations	Consolidated
Assets:					
Cash and cash equivalents	$ 0.4	$ 164.3	$ 364.9	$	$ 529.6
Accounts receivable, net	0.3	295.5	414.1		709.9
Inventories, net		385.8	668.2		1,054.0
Deferred income taxes	26.4				26.4
Prepaid expenses and other current assets	0.7	6.0	28.0		34.7
Total current assets	27.8	851.6	1,475.2		2,354.6
Property, plant and equipment, net	1.0	333.1	646.1		980.2
Cost in excess of net assets acquired		112.1	97.3		209.4
Deferred income taxes	117.9				117.9
Prepaid pension cost	11.2				11.2
Investments in subsidiaries and other assets	3,512.5	1,010.9	1,087.3	(5,497.9)	112.8
Total assets	$ 3,670.4	$ 2,307.7	$ 3,305.9	$ (5,497.9)	$ 3,786.1
Liabilities and stockholders equity:					
Accounts payable	$ 4.8	$ 236.9	$ 203.6	$	$ 445.3
Accrued liabilities	1,372.2	72.0	592.0	(1,806.3)	229.9
Accrued income taxes	66.2				66.2
Short-term debt and current portion of long-term debt		10.8	11.4		22.2
Total current liabilities	1,443.2	319.7	807.0	(1,806.3)	763.6
Long-term debt	305.9	389.6	23.0	(200.0)	518.5
Retirement benefits	11.3	273.4	167.3		452.0
Other long-term liabilities	28.2	16.7	125.3		170.2
Total liabilities	1,788.6	999.4	1,122.6	(2,006.3)	1,904.3
Total stockholders equity	1,881.8	1,308.3	2,183.3	(3,491.6)	1,881.8
Total liabilities and stockholders equity	$ 3,670.4	$ 2,307.7	$ 3,305.9	$ (5,497.9)	$ 3,786.1

14

Table of Contents

Note 10. CONTINUED
Allegheny Technologies Incorporated
Financial Information for Subsidiary and Guarantor Parent
Statements of Income
For the six months ended June 30, 2007

(In millions)	Guarantor Parent	Subsidiary	Non-guarantor Subsidiaries	Eliminations	Consolidated
Sales	$	$ 1,480.4	$ 1,363.5	$	$ 2,843.9
Cost of sales	5.1	1,146.5	904.3		2,055.9
Selling and administrative expenses	50.9	20.9	79.0		150.8
Interest income (expense), net	(9.8)	(2.5)	5.4		(6.9)
Other income (expense) including equity in income of unconsolidated subsidiaries	696.3	15.4	(3.9)	(707.6)	0.2
Income before income tax provision	630.5	325.9	381.7	(707.6)	630.5
Income tax provision	226.2	122.6	128.2	(250.8)	226.2
Net income	$ 404.3	$ 203.3	$ 253.5	$ (456.8)	$ 404.3

Condensed Statements of Cash Flows
For the six months ended June 30, 2007

(In millions)	Guarantor Parent	Subsidiary	Non-guarantor Subsidiaries	Eliminations	Consolidated
Cash flows provided by (used in) operating activities	$ (0.8)	$ 26.8	$ 160.7	**$**	$ 186.7
Cash flows used in investing activities	(0.2)	(32.9)	(114.2)		(147.3)
Cash flows provided by (used in) financing activities	0.9	(5.6)	(7.4)		(12.1)
Increase (decrease) in cash and cash equivalents	$ (0.1)	$ (11.7)	$ 39.1	$	$ 27.3

Table of Contents

Note 10. CONTINUED
Allegheny Technologies Incorporated
Financial Information for Subsidiary and Guarantor Parent
Balance Sheets
December 31, 2006

(In millions)	Guarantor Parent	Subsidiary	Non-guarantor Subsidiaries	Eliminations	Consolidated
Assets:					
Cash and cash equivalents	$ 0.5	$ 176.1	$ 325.7	$	$ 502.3
Accounts receivable, net	0.1	260.2	350.6		610.9
Inventories, net		287.6	511.1		798.7
Deferred income taxes	26.6				26.6
Prepaid expenses, and other current assets	0.1	5.4	43.9		49.4
Total current assets	27.3	729.3	1,231.3		1,987.9
Property, plant and equipment, net	0.9	319.4	551.4		871.7
Cost in excess of net assets acquired		112.1	94.4		206.5
Deferred income taxes	119.0				119.0
Investment in subsidiaries and other assets	3,295.0	799.7	914.0	(4,913.3)	95.4
Total assets	$ 3,442.2	$ 1,960.5	$ 2,791.1	$ (4,913.3)	$ 3,280.5
Liabilities and stockholders equity:					
Accounts payable	$ 5.8	$ 173.3	$ 176.0	$	$ 355.1
Accrued liabilities	1,551.3	70.1	457.2	(1,814.3)	264.3
Short-term debt and current portion of long-term debt		11.2	12.5		23.7
Total current liabilities	1,557.1	254.6	645.7	(1,814.3)	643.1
Long-term debt	306.5	394.9	28.5	(200.0)	529.9
Retirement benefits	35.8	267.8	160.8		464.4
Other long-term liabilities	39.9	18.3	82.0		140.2
Total liabilities	1,939.3	935.6	917.0	(2,014.3)	1,777.6
Total stockholders equity	1,502.9	1,024.9	$ 1,874.1	(2,899.0)	1,502.9
Total liabilities and stockholders equity	$ 3,442.2	$ 1,960.5	$ 2,791.1	$ (4,913.3)	$ 3,280.5

Table of Contents

Note 10. CONTINUED
Allegheny Technologies Incorporated
Financial Information for Subsidiary and Guarantor Parent
Statements of Income
For the six months ended June 30, 2006

(In millions)	Guarantor Parent	Subsidiary	Non-guarantor Subsidiaries	Eliminations	Consolidated
Sales	$	$ 1,099.8	$ 1,151.5	$	$ 2,251.3
Cost of sales	21.5	955.5	734.1		1,711.1
Selling and administrative expenses	52.1	20.2	76.0		148.3
Interest expense, net	(16.6)	1.5	1.8		(13.3)
Other income (expense) including equity in income of unconsolidated subsidiaries	466.3	1.6	(4.1)	(466.3)	(2.5)
Income before income tax provision	376.1	127.2	339.1	(466.3)	376.1
Income tax provision	125.3	48.1	112.6	(160.7)	125.3
Net income	$ 250.8	$ 79.1	$ 226.5	$ (305.6)	$ 250.8

Condensed Statements of Cash Flows
For the six months ended June 30, 2006

(In millions)	Guarantor Parent	Subsidiary	Non-guarantor Subsidiaries	Eliminations	Consolidated
Cash flows provided by (used in) operating activities	$ (23.8)	$ 19.6	$ 35.3	$	$ 31.1
Cash flows used in investing activities	(0.6)	(22.0)	(79.4)		(102.0)
Cash flows provided by (used in) financing activities	23.8	(0.1)	(2.3)		21.4
Decrease in cash and cash equivalents	$ (0.6)	$ (2.5)	$ (46.4)	$	$ (49.5)

Note 11. Commitments and Contingencies

The Company is subject to various domestic and international environmental laws and regulations that govern the discharge of pollutants and disposal of wastes, and which may require that it investigate and remediate the effects of the release or disposal of materials at sites associated with past and present operations. The Company could incur substantial cleanup costs, fines, and civil or criminal sanctions, third party property damage or personal injury claims as a result of violations or liabilities under these laws or noncompliance with environmental permits required at its facilities. The Company is currently involved in the investigation and remediation of a number of its current and former sites, as well as third party sites.

Environmental liabilities are recorded when the Company s liability is probable and the costs are reasonably estimable. In many cases, however, the Company is not able to determine whether it is liable or, if liability is probable, to reasonably estimate the loss or range of loss. Estimates of the Company s liability remain subject to additional uncertainties, including the nature and extent of site contamination, available remediation alternatives, the extent of corrective actions that may be required, and the number, participation, and financial condition of other potentially responsible parties (PRPs). The Company expects that it will adjust its accruals to reflect new information as appropriate. Future adjustments could have a material adverse effect on the Company s results of operations in a given period, but the Company cannot reliably predict the amounts of such future adjustments.

Table of Contents

Based on currently available information, the Company does not believe that there is a reasonable possibility that a loss exceeding the amount already accrued for any of the sites with which the Company is currently associated (either individually or in the aggregate) will be an amount that would be material to a decision to buy or sell the Company s securities. Future developments, administrative actions or liabilities relating to environmental matters, however, could have a material adverse effect on the Company s financial condition or results of operations.

At June 30, 2007, the Company s reserves for environmental remediation obligations totaled approximately $24 million, of which approximately $12 million were included in other current liabilities. The reserve includes estimated probable future costs of $10 million for federal Superfund and comparable state-managed sites; $8 million for formerly owned or operated sites for which the Company has remediation or indemnification obligations; $4 million for owned or controlled sites at which Company operations have been discontinued; and $2 million for sites utilized by the Company in its ongoing operations. The Company continues to evaluate whether it may be able to recover a portion of future costs for environmental liabilities from third parties.

The timing of expenditures depends on a number of factors that vary by site. The Company expects that it will expend present accruals over many years and that remediation of all sites with which it has been identified will be completed within thirty years.

See Note 14. Commitments and Contingencies to the Company s consolidated financial statements in the Company s Annual Report on Form 10-K for its fiscal year ended December 31, 2006 for a discussion of legal proceedings affecting the Company. The following are updates to that discussion.

TDY has conducted an environmental assessment of the San Diego facility pursuant to an October 2004 Order, as revised and amended, from the San Diego Regional Water Quality Control Board (Regional Board). TDY will perform remediation activities pursuant to the Order. At June 30, 2007, the Company had adequate reserves for these matters. However, the cost of the remediation cannot be predicted with certainty and could have a material adverse affect on the Company s results of operations and financial condition.

The consent judgment reflecting the agreement among TDY, the other PRPs and the U.S. Government relating to the Li Tungsten Superfund Site was executed, published for comment and lodged with the court. Under the consent judgment, TDY will complete the remediation of the remaining portions of the site and will receive contribution from other PRPs. Based on information presently available, the Company believes its reserves on this matter are adequate. However, the cost of the remediation cannot be predicted with certainty and could have a material adverse affect on the Company s results of operations and financial condition.

A number of other lawsuits, claims and proceedings have been or may be asserted against the Company relating to the conduct of its currently and formerly owned businesses, including those pertaining to product liability, patent infringement, commercial, employment, employee benefits, taxes, environmental and health and safety, and stockholder matters. While the outcome of litigation cannot be predicted with certainty, and some of these lawsuits, claims or proceedings may be determined adversely to the Company, management does not believe that the disposition of any such pending matters is likely to have a material adverse effect on the Company s financial condition or liquidity, although the resolution in any reporting period of one or more of these matters could have a material adverse effect on the Company s results of operations for that period.

Reserves for restructuring charges recorded in prior years involving future payments were approximately $2 million at June 30, 2007 and $3 million at December 31, 2006. The reserves relate to severance obligations and environmental exit costs.

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

Overview

Allegheny Technologies Incorporated (ATI) is a Delaware corporation with its principal executive offices located at 1000 Six PPG Place, Pittsburgh, Pennsylvania 15222-5479, telephone number (412) 394-2800. Allegheny Technologies was formed on August 15, 1996 as a result of the combination of Allegheny Ludlum Corporation and Teledyne, Inc. References to Allegheny Technologies, ATI, the Company, the Registrant, we, our and us a terms mean Allegheny Technologies Incorporated and its subsidiaries, unless the context otherwise requires.

Table of Contents

Allegheny Technologies is one of the largest and most diversified specialty metals producers in the world. We use innovative technologies to offer growing global markets a wide range of specialty metals solutions. Our products include titanium and titanium alloys, nickel-based alloys and superalloys, zirconium, hafnium and niobium, stainless and specialty steel alloys, grain-oriented silicon electrical steel and tool steels, tungsten-based materials, and forgings and castings. Our specialty metals are produced in a wide range of alloys and product forms and are selected for use in environments that demand metals having exceptional hardness, toughness, strength, resistance to heat, corrosion or abrasion, or a combination of these characteristics.

Results of Operations

We operate in three business segments: High Performance Metals, Flat-Rolled Products, and Engineered Products. These segments represented the following percentages of our total revenues and segment operating profit for the first six months of 2007 and 2006:

	2007		**2006**	
	Revenue	Operating Profit	Revenue	Operating Profit
High Performance Metals	36%	50%	38%	64%
Flat-Rolled Products	56%	47%	52%	29%
Engineered Products	8%	3%	10%	7%

Sales for the second quarter 2007 were $1.47 billion, an increase of 21.5% compared to the second quarter 2006, and 7% higher than the first quarter 2007. Compared to the 2006 second quarter, sales for the 2007 second quarter increased 24% in both the High Performance Metals and Flat-Rolled Products segments, and were essentially flat for the Engineered Products segment. For the first six months of 2007, sales were $2.84 billion, a 26% increase over the first six months of 2006. Sales increased 20% in the High Performance Metals segment and 36% in the Flat-Rolled Products segment, while Engineered Products segment sales were unchanged, compared to the first six months of 2006. Over 63% of year-to-date sales were generated by our key growth markets, namely aerospace and defense, chemical process industry, oil and gas, and electrical energy. Total shipments of ATI s titanium and titanium alloy products were 8.8 million pounds in the second quarter, nearly 14% higher than the second quarter 2006 and 2% higher than the first quarter 2007. Aerospace and defense was the largest of our markets at 30% of year-to-date 2007 sales. Our international sales growth continued, as direct international sales for the first six months of 2007 were $718.2 million, or 25.3% of total sales.

Segment operating profit for the second quarter 2007 was a record $357.2 million, an increase of $98.3 million, or 38%, compared to the second quarter 2006, as a result of strong performance in the High Performance Metals and Flat-Rolled Products business segments. For the first six months of 2007, segment operating profit was $697.5 million, an increase of $224.1 million, or 47%, over the first six months of 2006. Operating performance in 2007 continued to benefit from strong end-market demand and higher selling prices for most of our products, and from reduced costs and improved productivity resulting from ATI Business System initiatives. Segment operating profit as a percentage of sales for the three month and six month periods ended June 30, 2007 and 2006 were:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2007	2006	2007	2006
High Performance Metals	32.3%	34.9%	33.6%	35.1%
Flat-Rolled Products	20.7%	13.3%	20.6%	11.8%
Engineered Products	9.8%	13.8%	10.6%	14.9%

Our measure of segment operating profit, which we use to analyze the performance and results of our business segments, excludes income taxes, corporate expenses, net interest expense, retirement benefit expense, and other costs net of gain on asset sales. We believe segment operating profit, as defined, provides an appropriate measure of controllable operating results at the business segment level.

Results for the second quarter 2007 included a LIFO inventory valuation reserve charge of $21.7 million, due primarily to higher nickel and nickel-bearing scrap prices. For the same 2006 period, the LIFO inventory valuation reserve charge was $45.5 million. For the first six months of 2007, LIFO inventory valuation reserve charges were $42.6 million, compared to $52.4 million for the comparable 2006 period.

Table of Contents

Second quarter 2007 cost reductions, before the effects of inflation, totaled $26.6 million. Year-to-date cost reductions, before the effects of inflation, totaled $54.3 million.

Income before tax for the second quarter 2007 was $325.9 million, an increase of $116.2 million compared to the second quarter 2006. Net income for the second quarter 2007 was $206.5 million, or $2.00 per share, compared to the second quarter 2006 of $144.3 million, or $1.41 per share. Second quarter 2007 results include an income tax provision of $119.4 million, or 36.6% of income before tax. Second quarter 2006 results include an income tax provision of $65.4 million, or 31.2% of income before tax, which benefited from a $10.2 million reduction of the deferred tax valuation allowance due to the expected future realization of state income tax credits.

In the first quarter 2007, we entered into new four-year labor agreements with United Steelworkers represented employees at ATI Allegheny Ludlum and at ATI s Albany, OR titanium operations. The new agreements expire on June 30, 2011, and succeeded contracts that ran through June 30, 2007. The new agreements include wage and benefit increases that are in line with anticipated inflation. The ATI Allegheny Ludlum contract provides for profit sharing above a specified minimum pre-tax profit at the ATI Allegheny Ludlum operations, and is capped to provide for no more than $20 million of profit sharing payments under this provision over the four-year life of the contract. Any profit sharing payments made under this provision are contributed to an independently administered VEBA (Voluntary Employee Benefit Association) trust. As a result of the new agreements, we recognized a non-recurring charge of $5.8 million, or $3.7 million after-tax, in the first half 2007, which is primarily reflected in the operating results of the High Performance Metals and Flat-Rolled Products business segments.

Income before tax for the first six months of 2007 was $630.5 million, a 68% increase over the first six months of 2006. Net income for the six months ended June 30, 2007 was $404.3 million, or $3.93 per share, compared to $250.8 million, or $2.46 per share for the first half of 2006. First half 2007 results include an income tax provision of $226.2 million, or 35.9% of income before tax, which included the benefit of a $4.2 million reduction in the valuation allowances associated with state deferred tax assets recorded in the first quarter 2007. Results for the first six months of 2006 include an income tax provision of $125.3 million, or 33.3% of income before tax, and benefited from the second quarter 2006 $10.2 million deferred tax adjustment.

Looking ahead, we expect ATI s overall performance in the second half 2007 to be at least as good as that achieved in the first half 2007, with fourth quarter earnings stronger than the third quarter. We expect third quarter earnings to reflect higher costs of approximately $0.07 to $0.09 per share associated with scheduled major maintenance outages at several plants. The second half 2007 could be impacted by continued volatility in raw materials costs. In our High Performance Metals segment, titanium alloy shipments under long-term agreements are expected to continue to grow with the robust aerospace build rate. We also expect key growth markets in our Flat-Rolled Products segment to remain strong in 2007. We expect third quarter flat-rolled products shipments to be comparable to the second quarter. Flat-rolled products orders and shipments should improve once the price of nickel stabilizes.

High Performance Metals Segment

Sales increased 24% to a record $557.7 million, compared to the second quarter 2006. Demand for our titanium alloys, nickel-based superalloys, and vacuum-melted specialty alloys was strong from the aerospace and defense, and oil and gas markets. Demand was strong for our exotic alloys from the global chemical process industry, aerospace and defense, and nuclear electrical energy markets. Segment operating profit in the quarter increased to $180.2 million, or 32.3% of sales, a $23.0 million increase compared to the second quarter 2006.

Sales of our titanium and titanium alloys continued to grow. High Performance Metals segment titanium product shipments in the second quarter 2007 were 16% higher than the second quarter 2006 and 10% higher than the first quarter 2007. Part of this increase is due to the expanding use of titanium in airframes. Specifically, in the second quarter 2007, sales of our titanium alloys to airframe customers were 43% higher than the first quarter 2007 and more than four times higher than the second quarter 2006. Nickel-based and specialty alloys shipments in the second quarter 2007 were 6% higher than the second quarter 2006 and 14% higher than the first quarter 2007 driven largely by increased demand from the jet engine market. Exotic alloys shipments in the second quarter 2007 were 39% higher than the second quarter 2006 and 45% higher than the first quarter 2007 driven by strong demand from the global chemical process industry and nuclear energy markets, and by strong demand from aerospace and defense. Average selling prices in the second quarter 2007 compared to the second quarter 2006 decreased 7% for titanium products due primarily to reduced index pricing associated with lower scrap raw material costs. Average selling prices in the second quarter 2007 compared to the second quarter 2006 increased 43% for nickel-based and specialty alloys due primarily to improved product mix and increased index pricing associated with higher raw material costs, primarily nickel. Average selling prices in the second quarter 2007 compared to the second quarter 2006 for exotic alloys decreased by 7% primarily due to product mix.

The increase in operating profit primarily resulted from increased shipments and the benefits of gross cost reductions. Raw material cost inflation and higher inventory levels resulted in a LIFO inventory valuation reserve charge of $1.6 million in the second quarter 2007, compared to an $18.5 million charge in the second quarter 2006.

The High Performance Metals segment benefited from year-to-date 2007 gross cost reductions of $19.6 million, before the effects of inflation.

Certain comparative information on the segment s major products for the three months ended June 30,