PHELPS DODGE CORP
Form 10-Q
October 24, 2006

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

(Mark One)

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2006**

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: 1-82
PHELPS DODGE CORPORATION
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

New York	13-1808503
(State of Incorporation)	(I.R.S. Employer Identification No.)

One North Central Avenue, Phoenix, AZ 85004
(Address of principal executive offices)(Zip Code)
(602) 366-8100
(Registrant s telephone number, including area code)
N/A
(Former name, former address and former fiscal year, if changed since last report)

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.

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

Number of Common Shares outstanding at October 20, 2006: 203,988,751 shares.

- i -

PHELPS DODGE CORPORATION
Quarterly Report on Form 10-Q
For the Quarter Ended September 30, 2006
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PHELPS DODGE CORPORATION AND SUBSIDIARIES

Part I. Financial Information

Item 1. Financial Statements

PHELPS DODGE CORPORATION

CONSOLIDATED STATEMENT OF INCOME

(Unaudited; in millions except per share amounts)

	Third Quarter		Nine Months Ended September 30,	
	2006	2005	2006	2005
Sales and other operating revenues	$ 3,458.3	2,179.0	8,675.1	6,031.5
Operating costs and expenses				
Cost of products sold (exclusive of items shown separately below)	1,899.4	1,396.5	5,171.0	3,769.7
Depreciation, depletion and amortization	109.7	109.5	324.6	333.9
Selling and general administrative expense	42.9	42.4	141.5	118.4
Exploration and research expense	39.8	25.3	103.9	67.3
Special items and provisions, net (see Note 4)	32.5	45.0	62.6	481.3
	2,124.3	1,618.7	5,803.6	4,770.6
Operating income	1,334.0	560.3	2,871.5	1,260.9
Interest expense	(18.5)	(17.5)	(52.6)	(62.0)
Capitalized interest	17.0	6.7	41.2	9.1
Early debt extinguishment costs (see Note 12)		(54.0)		(54.0)
Gain on sale of cost-basis investment (see Note 13)				438.4
Change in interest gain (see Note 14)				159.5
Miscellaneous income and expense, net (see Note 16)	136.3	20.0	196.9	75.7
Income from continuing operations before taxes, minority interests in consolidated subsidiaries and equity in net earnings (losses) of affiliated companies	1,468.8	515.5	3,057.0	1,827.6
Provision for taxes on income (see Note 9)	(375.3)	(104.3)	(823.8)	(300.4)
Minority interests in consolidated subsidiaries	(206.0)	(51.6)	(525.3)	(116.5)
Equity in net earnings (losses) of affiliated companies	1.6	0.5	3.3	1.9
Income from continuing operations	889.1	360.1	1,711.2	1,412.6
Discontinued operations:				
Income (loss) from discontinued operations, net of taxes (see Note 3)	(1.1)	6.0	(17.7)	22.5
Net income	888.0	366.1	1,693.5	1,435.1
Preferred stock dividends				(6.8)
Net income applicable to common shares	$ 888.0	366.1	1,693.5	1,428.3

Weighted average number of common shares outstanding basic*	202.5	197.2	202.3	193.7
Basic earnings per common share:				
Income from continuing operations	$ 4.39	1.83	8.46	7.26
Income (loss) from discontinued operations	(0.01)	0.03	(0.09)	0.11
Basic earnings per common share	$ 4.38	1.86	8.37	7.37
Weighted average number of common shares outstanding diluted*	203.5	202.7	203.4	202.2
Diluted earnings per common share:				
Income from continuing operations	$ 4.37	1.78	8.42	6.99
Income (loss) from discontinued operations	(0.01)	0.03	(0.09)	0.11
Diluted earnings per common share	$ 4.36	1.81	8.33	7.10

* Refer to Note 15 for discussion of the March 10, 2006, stock split.

See Notes to Consolidated Financial Information.

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PHELPS DODGE CORPORATION
CONSOLIDATED BALANCE SHEET
(Unaudited; in millions except per share prices)

		September 30, 2006	December 31, 2005
Assets			
Current assets:			
Cash and cash equivalents	$	4,086.1	1,916.7
Restricted cash		40.1	20.8
Accounts receivable, less allowance for doubtful accounts (2006 - $7.2; 2005 - $6.9)		1,529.9	1,028.0
Mill and leach stockpiles		99.9	36.6
Inventories		374.0	329.5
Supplies		227.1	199.7
Prepaid expenses and other current assets		128.9	83.6
Deferred income taxes		192.1	82.0
Assets held for sale			373.8
Current assets		6,678.1	4,070.7
Investments and long-term receivables		192.3	142.6
Property, plant and equipment, net		5,370.3	4,830.9
Long-term mill and leach stockpiles		176.9	133.3
Deferred income taxes		76.9	99.6
Goodwill		12.5	22.3
Intangible assets, net		7.1	7.5
Long-term assets held for sale			431.4
Trust assets		579.2	258.4
Other assets and deferred charges		355.8	361.3
	$	13,449.1	10,358.0
Liabilities			
Current liabilities:			
Short-term debt	$	63.0	14.3
Current portion of long-term debt		62.2	2.5
Accounts payable and accrued expenses		2,102.9	1,445.7
Accrued income taxes		248.0	23.6
Liabilities related to assets held for sale			123.2
Current liabilities		2,476.1	1,609.3
Long-term debt		796.4	677.7
Deferred income taxes		835.1	558.0
Long-term liabilities related to assets held for sale			61.3

Other liabilities and deferred credits		1,430.3	934.2
		5,537.9	3,840.5
Commitments and contingencies (see Notes 6, 7 and 9)			
Minority interests in consolidated subsidiaries		1,427.3	915.9
Shareholders equity*			
Common shares, par value $6.25; 300.0 shares authorized; 204.0 outstanding (2005 - 203.2) after deducting 16.0 shares (2005 - 16.7) held in treasury, at cost		1,274.9	635.1
Capital in excess of par value		1,365.9	1,998.8
Retained earnings**		3,937.5	3,158.8
Accumulated other comprehensive loss		(94.4)	(154.5)
Other			(36.6)
		6,483.9	5,601.6
	$	13,449.1	10,358.0

* Refer to Note 15 for discussion of the March 10, 2006, stock split.

** Included cumulative effect adjustment credit of $19.8 million for the adoption of EITF Issue No. 04-6 in the 2006 first quarter. Refer to Note 5 for further discussion.

See Notes to Consolidated Financial Information.

PHELPS DODGE CORPORATION
CONSOLIDATED STATEMENT OF CASH FLOWS
(Unaudited; $ in millions)

	Nine Months Ended September 30,	
	2006	2005
Operating activities		
Net income	$ 1,693.5	1,435.1
Adjustments to reconcile net income to net cash provided by operating activities:		
Unrealized losses on copper collars and copper put options	1,215.1	164.5
Depreciation, depletion and amortization	324.9	377.3
Deferred income tax provision (benefit)	145.8	(3.9)
Equity in net earnings (losses) of affiliated companies, net of dividends received	(1.2)	0.3
Gain on sale of cost-basis investment		(438.4)
Change in interest gain		(159.5)
Special items and provisions, net	62.6	481.3
Early debt extinguishment costs		54.0
Minority interests in consolidated subsidiaries	525.7	117.4
Loss on disposition of discontinued operations	29.7	
Changes in current assets and liabilities:		
Accounts receivable	(543.4)	(240.1)
Repayment of securitized accounts receivable		(85.0)
Mill and leach stockpiles	(59.2)	0.5
Inventories	(34.0)	(69.4)
Supplies	(28.1)	(26.1)
Prepaid expenses and other current assets	(50.5)	(54.6)
Interest payable	9.4	4.6
Other accounts payable	35.9	71.3
Accrued income taxes	218.8	(18.4)
Realized losses on 2005 copper collars	(187.2)	
Other accrued expenses	14.7	(0.4)
Pension plan contributions		(250.0)
Other operating, net	(46.3)	(61.4)
Net cash provided by operating activities	3,326.2	1,299.1
Investing activities		
Capital outlays	(830.3)	(392.5)
Capitalized interest	(41.6)	(9.9)
Investments in subsidiaries and other, net of cash received	0.3	(11.2)
Proceeds from the sale of Columbian Chemicals	505.6	
Proceeds from the sale of Magnet Wire North American assets	136.6	
Proceeds from the sale of HPC	49.2	
Proceeds from asset dispositions	21.1	6.2

Proceeds from sale of cost-basis investments, net of expenses		451.6
Restricted cash	(19.3)	(89.1)
Global environmental trust contribution	(300.0)	
Other investing, net	(0.1)	(2.3)
Net cash used in investing activities	(478.5)	(47.2)
Financing activities		
Net increase (decrease) in short-term debt	47.7	(48.7)
Proceeds from issuance of debt	182.0	
Payment of debt	(2.6)	(313.8)
Common dividends	(934.6)	(84.8)
Preferred dividends		(10.1)
Minority interest dividends	(3.1)	(28.4)
Issuance of shares, net	25.6	52.4
Debt issue costs	(2.7)	(5.8)
Proceeds from issuance of Cerro Verde stock, net of expenses		441.8
Other financing, net		(55.8)
Net cash used in financing activities	(687.7)	(53.2)
Effect of exchange rate impact on cash and cash equivalents	9.4	17.4
Increase in cash and cash equivalents	2,169.4	1,216.1
Cash and cash equivalents at beginning of period	1,916.7	1,200.1
Cash and cash equivalents at end of period	$ 4,086.1	2,416.2

See Notes to Consolidated Financial Information.

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PHELPS DODGE CORPORATION
CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY
(Unaudited; in millions)

	Common Shares Number of Shares	Common Shares At Par Value	Capital in Excess of Par Value	Retained Earnings	Accumulated Other Comprehensive Income (Loss)*	Other	Shareholders Equity
Balance at December 31, 2005	101.6	$ 635.1	$ 1,998.8	$ 3,158.8	$ (154.5)	$ (36.6)	$ 5,601.6
Cumulative effect adjustment**				19.8			19.8
Transition adjustment***			(36.6)			36.6	
Stock options exercised including tax benefit	0.7	4.1	25.6				29.7
Restricted shares issued/cancelled, net, including tax benefit	0.1	0.7	13.8				14.5
Directors stock compensation		0.1	1.4				1.5
Common shares purchased		(0.2)	(2.0)				(2.2)
Dividends on common shares				(934.6)			(934.6)
Comprehensive income (loss):							
Net income				1,693.5			1,693.5
Other comprehensive income (loss), net of tax:							
Translation adjustment					35.6		35.6
Net loss on derivative instruments					(5.3)		(5.3)
Other investment adjustments					0.2		0.2
Unrealized gain on securities					20.9		20.9
Minimum pension liability					8.7		8.7
Other comprehensive income					60.1		60.1
Comprehensive income							1,753.6
Stock split****	101.6	635.1	(635.1)				
Balance at September 30, 2006	204.0	$ 1,274.9	$ 1,365.9	$ 3,937.5	$ (94.4)	$	$ 6,483.9

*

As of September 30, 2006, this balance comprised $136.3 million of cumulative translation adjustments and $17.5 million of cumulative minimum pension liability adjustments; partially offset by $0.5 million of cumulative unrealized gains on securities and $58.9 million of cumulative unrealized gains on derivative instruments.

** Refer to Note 5 for discussion of adoption of EITF Issue No. 04-6.

*** Refer to Note 2 for discussion of adoption of SFAS No. 123-R.

**** Refer to Note 15 for discussion of the March 10, 2006, stock split.

See Notes to Consolidated Financial Information.

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PHELPS DODGE CORPORATION
FINANCIAL DATA BY BUSINESS SEGMENT
(Unaudited; $ in millions)

	U.S. Mines					South American Mines			
				Chino/		Candelaria/			Primary
						Ojos del	Cerro		
	Morenci	Bagdad	Sierrita	Cobre	Tyrone	Salado	Verde	El Abra	Molybdenum
Third Quarter 2006									
Sales and other operating revenues:									
Unaffiliated customers	$		1.8	6.6		289.5	29.1	273.3	442.0
Intersegment	497.4	172.6	241.8	129.9	46.1	40.2	159.7	190.0	
Depreciation, depletion and amortization	15.4	6.0	4.3	5.9	3.0	10.1	8.5	30.2	10.2
Operating income (loss) before special items and provisions	308.0	98.1	163.3	67.4	23.0	250.6	92.6	336.4	100.4
Special items and provisions, net	(0.6)			(6.8)	(1.8)				7.0
Operating income (loss)	307.4	98.1	163.3	60.6	21.2	250.6	92.6	336.4	107.4
Interest income	0.1			0.7		4.6	2.8	9.9	0.2
Interest expense, net							10.6	0.4	
Benefit (provision) for taxes on income						(80.7)	16.7	(121.2)	
Minority interests in consolidated subsidiaries						(34.8)	(58.3)	(110.4)	
Equity in net earnings (losses) of affiliated companies						0.1			
Loss from discontinued operations									
Equity basis investments at September 30			0.2			0.7			
Assets at September 30	1,145.2	445.4	330.7	456.1	119.1	1,404.5	1,636.0	1,822.1	938.6
Expenditures for segment assets	60.6	6.1	6.9	6.3	4.0	3.7	123.2	3.0	18.6

Third Quarter 2005*
Sales and other operating revenues:

Unaffiliated customers	$		6.9	8.2		133.6	14.2	78.1	468.0
Intersegment	283.0	180.1	223.4	79.1	31.8	59.5	80.1	80.8	
Depreciation, depletion and amortization	15.7	7.6	3.5	5.1	0.2	9.6	7.0	28.6	9.7
Operating income (loss) before special items and provisions	128.2	112.4	153.9	18.6	3.0	73.1	55.8	52.6	71.9
Special items and provisions, net	0.4		(8.6)						
Operating income (loss)	128.6	112.4	145.3	18.6	3.0	73.1	55.8	52.6	71.9
Interest income	0.1			0.6		2.6	2.6	0.8	0.2
Interest expense, net						0.1	4.9	(0.5)	
Provision for taxes on income						(13.0)	(15.7)	(18.0)	
Minority interests in consolidated subsidiaries						(9.5)	(23.8)	(16.6)	
Equity in net earnings (losses) of affiliated companies									
Income from discontinued operations									
Equity basis investments at September 30			0.2			0.3			
Assets at September 30	918.3	446.0	328.5	429.8	73.2	1,041.4	913.8	1,003.2	934.9
Expenditures for segment assets	16.1	10.6	5.0	2.9	2.7	4.6	106.7	6.4	18.1

	Manufac-turing	Sales	PDMC Segments	PDMC Other	PDMC Subtotal	PDI Wire & Cable	Corporate, Other & Eliminations	Discontinued Operations	Totals
Third Quarter 2006									
Sales and other operating revenues:									
Unaffiliated customers	$ 1,833.7	219.6	3,095.6	47.4	3,143.0	315.3			3,458.3
Intersegment	1.4	1.5	1,480.6	(1,480.6)		0.2	(0.2)		
Depreciation, depletion and amortization	6.3		99.9	4.0	103.9	3.7	2.1		109.7
Operating income (loss) before special items and	(7.7)	0.3	1,432.4	(53.4)	1,379.0	22.1	(34.6)		1,366.5

provisions									
Special items and provisions, net	(1.0)		(3.2)	0.2	(3.0)	(7.1)	(22.4)		(32.5)
Operating income (loss)	(8.7)	0.3	1,429.2	(53.2)	1,376.0	15.0	(57.0)		1,334.0
Interest income			18.3	0.5	18.8	0.9	29.3		49.0
Interest expense, net	(1.1)	(0.3)	9.6	1.2	10.8	(2.4)	(9.9)		(1.5)
Provision for taxes on income			(185.2)		(185.2)		(190.1)		(375.3)
Minority interests in consolidated subsidiaries			(203.5)		(203.5)	(2.5)			(206.0)
Equity in net earnings (losses) of affiliated companies			0.1	0.2	0.3	0.8	0.5		1.6
Loss from discontinued operations								(1.1)	(1.1)
Equity basis investments at September 30			0.9	1.0	1.9	6.9	23.5		32.3
Assets at September 30	932.9	111.3	9,341.9	49.8	9,391.7	585.6	3,471.8		13,449.1
Expenditures for segment assets	3.4		235.8	5.0	240.8	4.7	2.4		247.9
Third Quarter 2005*									
Sales and other operating revenues:									
Unaffiliated customers	$ 894.2	249.2	1,852.4	7.3	1,859.7	319.3			2,179.0
Intersegment	30.6	77.3	1,125.7	(1,046.6)	79.1	0.3	(79.4)		
Depreciation, depletion and amortization	11.2		98.2	2.6	100.8	7.0	1.7		109.5
Operating income (loss) before special items and provisions	0.2	2.3	672.0	(45.1)	626.9	11.2	(32.8)		605.3
Special items and provisions, net	0.1		(8.1)	(0.4)	(8.5)	(1.8)	(34.7)		(45.0)
Operating income (loss)	0.3	2.3	663.9	(45.5)	618.4	9.4	(67.5)		560.3
Interest income		0.1	7.0		7.0	0.5	11.7		19.2
Interest expense, net	(0.8)	(0.2)	3.5	0.9	4.4	(1.9)	(13.3)		(10.8)
			(46.7)		(46.7)		(57.6)		(104.3)

Provision for taxes on income									
Minority interests in consolidated subsidiaries			(49.9)	0.1	(49.8)	(1.8)			(51.6)
Equity in net earnings (losses) of affiliated companies				(0.2)	(0.2)	0.2	0.5		0.5
Income from discontinued operations								6.0	6.0
Equity basis investments at September 30			0.5	0.9	1.4	6.4	23.8		31.6
Assets at September 30	330.6	36.7	6,456.4	6.6	6,463.0	686.9	2,407.1	685.0	10,242.0
Expenditures for segment assets	5.0		178.1	24.0	202.1	4.7	5.0	12.3	224.1

* In the 2005 fourth quarter, the Company reassessed its reportable segments considering the increase in copper and molybdenum prices. Based upon our assessment, we are no longer separately disclosing Miami/Bisbee as an individual reportable segment. Segment information for 2005 has been revised to conform to the 2006 presentation.

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PHELPS DODGE CORPORATION
FINANCIAL DATA BY BUSINESS SEGMENT
(Unaudited; $ in millions)

	U.S. Mines					South American Mines			
	Morenci	Bagdad	Sierrita	Chino/ Cobre	Tyrone	Candelaria/ Ojos del Salado	Cerro Verde	El Abra	Primary Molybdenum
Nine Months Ended September 30, 2006									
Sales and other operating revenues:									
Unaffiliated customers	$		19.4	26.3		781.6	96.1	692.9	1,295.6
Intersegment	884.6	391.5	587.7	256.5	82.9	190.1	394.2	510.3	
Depreciation, depletion and amortization	44.4	17.6	12.2	19.0	8.9	31.4	22.8	91.1	31.7
Operating income (loss) before special items and provisions	393.2	171.6	360.4	72.1	11.1	657.3	327.5	846.3	319.1
Special items and provisions, net	(0.6)	2.2	(5.1)	(16.9)	(1.8)				6.9
Operating income (loss)	392.6	173.8	355.3	55.2	9.3	657.3	327.5	846.3	326.0
Interest income	0.2			2.1		7.3	6.6	17.0	0.7
Interest expense, net						0.1	26.7	1.2	
Provision for taxes on income						(222.1)	(11.2)	(311.8)	
Minority interests in consolidated subsidiaries						(84.7)	(164.2)	(271.4)	
Equity in net earnings (losses) of affiliated companies						0.1			
Loss from discontinued operations									
Equity basis investments at September 30			0.2			0.7			
Assets at September 30	1,145.2	445.4	330.7	456.1	119.1	1,404.5	1,636.0	1,822.1	938.6
Expenditures for segment assets	145.1	18.9	22.6	13.2	14.2	12.3	445.1	14.8	34.8

Nine Months Ended September 30, 2005*									
Sales and other operating revenues:									
Unaffiliated customers	$		12.2	14.0		356.0	47.5	238.5	1,470.9
Intersegment	773.3	526.8	635.3	243.6	94.6	155.1	196.2	233.8	
Depreciation, depletion and amortization	46.9	23.3	11.2	15.5	7.2	28.8	20.2	90.1	31.6
Operating income (loss) before special items and provisions	328.9	313.3	424.0	49.2	7.5	213.1	131.4	160.9	257.4
Special items and provisions, net	(0.2)		(8.6)	(64.5)	(215.7)				
Operating income (loss)	328.7	313.3	415.4	(15.3)	(208.2)	213.1	131.4	160.9	257.4
Interest income	0.1			1.6		4.8	4.9	1.2	0.4
Interest expense, net						0.2	6.6	(5.0)	
Gain on sale of cost-basis investment									87.2
Change in interest gain							159.5		
Provision for taxes on income						(42.1)	(11.5)	(56.4)	
Minority interests in consolidated subsidiaries						(25.9)	(38.8)	(48.3)	
Equity in net earnings (losses) of affiliated companies									
Income from discontinued operations									
Equity basis investments at September 30			0.2			0.3			
Assets at September 30	918.3	446.0	328.5	429.8	73.2	1,041.4	913.8	1,003.2	934.9
Expenditures for segment assets	23.0	21.9	11.6	11.9	4.5	12.5	178.1	15.8	25.1

Manufac-turing	Sales	PDMC Segments	PDMC Other	PDMC Subtotal	PDI Wire & Cable	Corporate, Other & Eliminations	Discontinued Operations	Totals

Nine Months Ended September 30, 2006									
Sales and other operating revenues:									
Unaffiliated customers	$ 4,832.5	(70.2)	7,674.2	67.8	7,742.0	933.1			8,675.1
Intersegment	93.5	57.2	3,448.5	(3,393.9)	54.6	0.5	(55.1)		
Depreciation, depletion and amortization	17.7		296.8	9.9	306.7	11.9	6.0		324.6
Operating income (loss) before special items and provisions	(0.7)	8.2	3,166.1	(174.6)	2,991.5	52.9	(110.3)		2,934.1
Special items and provisions, net	(2.2)		(17.5)	(5.4)	(22.9)	(15.8)	(23.9)		(62.6)
Operating income (loss)	(2.9)	8.2	3,148.6	(180.0)	2,968.6	37.1	(134.2)		2,871.5
Interest income			33.9	1.4	35.3	1.7	68.9		105.9
Interest expense, net	(3.2)	(0.5)	24.3	3.3	27.6	(7.0)	(32.0)		(11.4)
Provision for taxes on income			(545.1)		(545.1)		(278.7)		(823.8)
Minority interests in consolidated subsidiaries			(520.3)		(520.3)	(5.0)			(525.3)
Equity in net earnings (losses) of affiliated companies			0.1	0.6	0.7	1.1	1.5		3.3
Loss from discontinued operations								(17.7)	(17.7)
Equity basis investments at September 30			0.9	1.0	1.9	6.9	23.5		32.3
Assets at September 30	932.9	111.3	9,341.9	49.8	9,391.7	585.6	3,471.8		13,449.1
Expenditures for segment assets	9.1		730.1	65.9	796.0	11.4	13.2	9.4	830.0

Nine Months Ended September 30, 2005*									
Sales and other operating revenues:									
Unaffiliated customers	$ 2,316.6	687.5	5,143.2	19.0	5,162.2	869.3			6,031.5
Intersegment	136.4	195.9	3,191.0	(2,990.1)	200.9	0.7	(201.6)		
	23.7		298.5	7.6	306.1	22.7	5.1		333.9

Depreciation, depletion and amortization									
Operating income (loss) before special items and provisions	11.2	1.8	1,898.7	(95.8)	1,802.9	30.0	(90.7)		1,742.2
Special items and provisions, net	(148.6)		(437.6)	8.2	(429.4)	(3.3)	(48.6)		(481.3)
Operating income (loss)	(137.4)	1.8	1,461.1	(87.6)	1,373.5	26.7	(139.3)		1,260.9
Interest income		0.1	13.1	0.4	13.5	1.2	22.6		37.3
Interest expense, net	(2.3)	(0.7)	(1.2)	2.4	1.2	(5.8)	(48.3)		(52.9)
Gain on sale of cost-basis investment			87.2	351.2	438.4				438.4
Change in interest gain			159.5		159.5				159.5
Provision for taxes on income			(110.0)		(110.0)		(190.4)		(300.4)
Minority interests in consolidated subsidiaries			(113.0)	0.1	(112.9)	(3.6)			(116.5)
Equity in net earnings (losses) of affiliated companies				(0.7)	(0.7)	1.0	1.6		1.9
Income from discontinued operations								22.5	22.5
Equity basis investments at September 30			0.5	0.9	1.4	6.4	23.8		31.6
Assets at September 30	330.6	36.7	6,456.4	6.6	6,463.0	686.9	2,407.1	685.0	10,242.0
Expenditures for segment assets	14.4		318.8	40.3	359.1	12.0	10.0	22.6	403.7

* In the 2005 fourth quarter, the Company reassessed its reportable segments considering the increase in copper and molybdenum prices. Based upon our

assessment, we are no longer separately disclosing Miami/Bisbee as an individual reportable segment. Segment information for 2005 has been revised to conform to the 2006 presentation.

NOTES TO CONSOLIDATED FINANCIAL INFORMATION

(Unaudited)

1. General Information

The unaudited consolidated financial information of Phelps Dodge Corporation (the Company, which may be referred to as Phelps Dodge, PD, we, us or our) presented herein has been prepared in accordance with the instructions to Form 10-Q and does not include all of the information and note disclosures required by U.S. generally accepted accounting principles (GAAP). Therefore, this information should be read in conjunction with the Consolidated Financial Statements and notes thereto included in our Form 10-K for the year ended December 31, 2005. This information reflects all adjustments that are, in the opinion of management, necessary to a fair statement of the results for the interim periods reported. The results of operations for the quarter and nine months ended September 30, 2006, are not necessarily indicative of the results to be expected for the full year.

Our business consists of two divisions, Phelps Dodge Mining Company (PDMC) and Phelps Dodge Industries (PDI). Prior to the 2005 fourth quarter, PDI included, among other manufacturing businesses, our Specialty Chemicals segment, which consisted of Columbian Chemicals Company and its subsidiaries (Columbian Chemicals or Columbian). On November 15, 2005, the Company entered into an agreement to sell Columbian Chemicals to a company owned jointly by One Equity Partners LLC, a private equity affiliate of JPMorgan Chase & Co., and South Korea-based DC Chemical Co., Ltd. The transaction was completed on March 16, 2006. As a result of this transaction, the operating results of Columbian have been reported separately from continuing operations and shown as discontinued operations in the Consolidated Statement of Income for all periods presented. (Refer to Note 3, Divestitures, for further discussion.)

In addition, on November 15, 2005, the Company entered into an agreement to sell substantially all of its North American magnet wire assets, previously reported as part of the Wire and Cable segment in the PDI division, to Rea Magnet Wire Company, Inc. (Rea). This transaction was completed on February 10, 2006. On March 4, 2006, Phelps Dodge entered into an agreement to sell High Performance Conductors of SC & GA, Inc. (HPC), previously reported as part of the Wire and Cable segment in the PDI division, to International Wire Group, Inc. (IWG). This transaction was completed on March 31, 2006. Neither transaction met the criteria for classification as discontinued operations as the Company is continuing to supply Rea with copper rod and IWG with copper rod and certain copper alloys. (Refer to Note 3, Divestitures, for further discussion of these transactions.)

Interests in our majority-owned subsidiaries are reported using the full consolidation method. We fully consolidate the results of operations and the assets and liabilities of these subsidiaries and report the minority interests in our Consolidated Financial Statements. All material intercompany balances and transactions are eliminated. Other investments in undivided interests and unincorporated mining joint ventures that are limited to the extraction of minerals are accounted for using the proportional consolidation method, which include the Morenci copper mine, located in Arizona, in which we hold an 85 percent undivided interest.

All references to shares of common stock and per share amounts for the quarter and nine months ended September 30, 2005, have been adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15, Shareholders Equity, for further discussion.)

For comparative purposes, certain amounts for the quarter and nine months ended September 30, 2005, have been reclassified to conform to current period presentation.

2. Share-Based Compensation

On January 1, 2006, the Company adopted Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment (SFAS No. 123-R). SFAS No. 123-R requires all share-based payments to employees, including employee stock options, be measured at fair value and expensed over the requisite service period (generally the vesting period) for awards expected to vest. The Company elected to use the modified prospective method for adoption, which required compensation expense to be recognized for all unvested stock options and restricted stock beginning in the first quarter of adoption. The fair value of restricted stock is determined based on the quoted price of our common stock on the date of grant, and the fair value of stock options is determined using the Black-Scholes valuation model, which is consistent with our valuation techniques previously utilized for stock options in footnote

disclosures under SFAS No. 123, Accounting for Stock-Based Compensation, as amended by SFAS No. 148, Accounting for Stock-Based Compensation Transition and Disclosure. Such value is recognized as expense over the requisite service period, net of estimated forfeitures. Under SFAS No. 123-R, any unearned or deferred compensation related to awards granted prior to the adoption of SFAS No. 123-R should be eliminated against the appropriate equity accounts upon adoption. Therefore, in the 2006 first quarter, we made an adjustment to beginning capital in excess of par value of $36.6 million with the offset to the contra-equity account. Prior to adoption, we applied the disclosure-only provisions of SFAS No. 123. In accordance with the provisions of SFAS No. 123, we accounted for our stock option plans by measuring compensation cost using the intrinsic-value-based method presented by Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. No compensation cost was reflected in consolidated net income for stock option plans, as all options granted under the plans had an exercise price equal to the market value of the underlying common stock on the date of the grant.

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The following table presents the effect on net income and earnings per common share as if we had applied the fair value recognition provisions of SFAS No. 123 for the quarter and nine months ended September 30, 2005:

(Unaudited; $ in millions except per share amounts)

		2005 Third Quarter
Net income as reported	$	366.1
Deduct:		
Total compensation cost assuming fair value method for stock options, net of tax		(0.5)
Pro forma net income	$	365.6
Basic earnings per common share:*		
As reported	$	1.86
Pro forma	$	1.85
Diluted earnings per common share:*		
As reported	$	1.81
Pro forma	$	1.80

(Unaudited; $ in millions except per share amounts)

		Nine Months Ended September 30, 2005
Net income as reported	$	1,435.1
Deduct:		
Total compensation cost assuming fair value method for stock options, net of tax		(2.4)
Pro forma net income	$	1,432.7
Basic earnings per common share:*		
As reported	$	7.37
Pro forma	$	7.36
Diluted earnings per common share:*		
As reported	$	7.10
Pro forma	$	7.09

* Earnings per common share for the quarter and nine months

ended September 30, 2005, have been adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15, Shareholders Equity, for further discussion.)

The fair value of each option grant is estimated on the date of grant using a Black-Scholes option-pricing model based on the following assumptions:

(Unaudited)

	Nine Months Ended September 30,	
	2006	2005
Expected dividend yield	0.95%	1.04%
Expected stock price volatility	37.34%	39.83%
Risk-free interest rate	4.48%	3.76%
Expected life of options	5 years	5 years

The expected dividend yield is based on historical dividend payments. Expected stock price volatility is based on historical volatility of the Company s stock. The risk-free interest rate is based upon the interest rates appropriate for the term of the Company s employee stock options. The expected life of options granted is based on evaluations of historical and expected future employee exercise behavior and represents the period of time that options granted are expected to be outstanding.

Executives and other key employees have been granted options to purchase common shares under stock option plans adopted in 1993, 1998 and 2003. The option price equals the fair market value of the common shares on the day of the grant, and an option s maximum term is 10 years. Options granted vest ratably over a three-year period.

At September 30, 2006, 7,417,586 shares were available for option grants (including 3,256,018 shares as Restricted Stock awards) under the 2003 plan. These amounts are subject to future adjustment as described in the plan document. No further options may be granted under the 1998 or 1993 plans.

In connection with the 1999 acquisition, former Cyprus Amax stock options were converted into 1,870,804 Phelps Dodge options, which retain the terms by which they were originally granted under the Management Incentive Program of Cyprus Amax Minerals Company. These options carry a maximum term of 10 years and became fully vested upon the acquisition of Cyprus Amax in October 1999. Exercise periods ranged up to eight years at acquisition. No further options may be granted under this plan.

The Phelps Dodge Corporation Directors Stock Unit Plan (effective January 1, 1997) provided to each non-employee director serving on the board since November 15 of the preceding year an annual award of stock units having a value of $75,000 as of the date of grant. This plan replaced the Company s 1989 Directors Stock Option Plan. On February 1, 2006, the plan was amended to provide pro rata awards for those directors elected after November 15, 2005, based on the number of days in 2006 the director is expected to serve on the board. On May 26, 2006, the Phelps Dodge Corporation 2007 Directors Stock Unit Plan was approved by the Company s shareholders. The options granted under the 1989 Directors Stock Option Plan expire three years after the termination of service as a director. No further options may be granted under the 1989 plan.

Stock option plans at December 31, 2005, and September 30, 2006, and changes for the first nine months of 2006 for the combined plans were as follows:

(Unaudited)

	Shares	Weighted-Average Exercise Price
Outstanding at December 31, 2005*	1,111,174	$ 29.82
Granted	143,000	79.00
Exercised	(658,807)	26.81
Forfeited or expired	(38,476)	45.79
Outstanding at September 30, 2006	556,891	44.90
Exercisable at September 30, 2006	211,461	22.59

* Outstanding shares and the weighted-average exercise price at December 31, 2005, have been adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15, Shareholders Equity, for further discussion.)

At September 30, 2006, the aggregate intrinsic value of options outstanding was $21.9 million with a weighted-average remaining contractual term of 7.2 years, and the aggregate intrinsic value of options exercisable was $13.0 million with a weighted-average remaining contractual term of 5.0 years.

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Exercisable options by plan at September 30, 2006, were as follows:

(Unaudited)

	Shares	Weighted-Average Exercise Price
PD Plans		
2003 Plan	14,987	$ 43.15
1998 Plan	190,984	20.71
1993 Plan	5,000	32.69
Cyprus Amax Plans	490	22.23
	211,461	22.59

For the nine months ended September 30, 2006 and 2005, the weighted-average grant-date fair value of stock options granted was $28.91 per common share and $17.77 per common share, respectively, and the total intrinsic value of options exercised was $34.1 million and $70.2 million, respectively.

The 2003 plan provides (and the 1993 and 1998 plan provided) for the award to executives and other key employees, without any payment by them, of common shares subject to certain restrictions (Restricted Stock). At September 30, 2006, there were 1,551,385 shares of Restricted Stock outstanding and 3,256,018 shares available for award.

Restricted Stock at December 31, 2005, and September 30, 2006, and changes for the first nine months of 2006 were as follows:

(Unaudited)

	Shares	Weighted-Average Grant-Date Fair Value Price
Outstanding at December 31, 2005*	1,548,734	$ 36.62
Granted	297,440	78.22
Released	(122,443)	26.25
Forfeited	(172,346)	38.78
Outstanding at September 30, 2006	1,551,385	45.17

* Outstanding shares and the weighted-average grant-date fair value price at December 31, 2005, have been

adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15, Shareholders Equity for further discussion.)

For the nine months ended September 30, 2006 and 2005, the weighted-average grant-date fair value of Restricted Stock was $78.22 per common share and $49.15 per common share, respectively. Restricted Stock generally becomes fully vested in five years. Although the 2006, 2005 and 2004 awards become fully vested in five years, a majority of the shares included in those awards have graded-vesting features in which a portion of the shares will vest on the third and fourth anniversaries of the award. For the nine months ended September 30, 2006 and 2005, the total fair value of shares released or vested was $9.7 million and $10.3 million, respectively.

Compensation cost for the stock option and restricted stock plans in the 2006 and 2005 third quarters was $5.4 million and $3.2 million, respectively (included as selling and general administrative expense in the Consolidated Statement of Income). For the 2006 and 2005 third quarters, the total tax benefit recognized was $1.4 million and $0.8 million, respectively. For the nine months ended September 30, 2006 and 2005, compensation cost was $18.1 million and $9.2 million, respectively. For the nine months ended September 30, 2006 and 2005, the total income tax benefit recognized was $4.4 million and $2.2 million, respectively. At September 30, 2006, there was $42.0 million of total unrecognized compensation cost related to nonvested, share-based compensation arrangements. That cost is expected to be recognized over a weighted-average period of 2.0 years.

In the 2006 and 2005 third quarters, cash received from option exercises under all share-based payment arrangements was $0.7 million and $20.6 million, respectively, and the actual tax benefit realized for the tax deductions for share-based payment arrangements totaled $1.1 million and $4.6 million, respectively.

For the nine months ended September 30, 2006 and 2005, cash received from option exercises under all share-based payment arrangements was $17.7 million and $56.0 million, respectively, and the actual tax benefit realized for the tax deductions for share-based payment arrangements totaled $10.1 million and $14.6 million, respectively.

3. Divestitures

Columbian Chemicals Company

On November 15, 2005, Phelps Dodge entered into an agreement to sell Columbian Chemicals to a company owned jointly by One Equity Partners LLC, a private equity affiliate of JPMorgan Chase & Co., and South Korea-based DC Chemical Co., Ltd. The transaction was completed on March 16, 2006, resulting in net sales proceeds of approximately $595 million (including approximately $100 million of Columbian s foreign-held cash and net of approximately $27 million in taxes and related expenses). As a result of the transaction, the operating results of Columbian have been reported separately from continuing operations and shown as discontinued operations in the Consolidated Statement of Income for all periods presented.

The transaction resulted in net charges of $124.5 million ($72.9 million after-tax and net of minority interest), which were recorded in discontinued operations. Of this amount, $94.8 million ($42.6 million after-tax and net of minority interest) was recognized in the 2005 fourth quarter, which consisted of a goodwill impairment charge of $89.0 million ($67.0 million after-tax and net of minority interest) to reduce the carrying value of Columbian to its estimated fair value less costs to sell, a loss on disposal of $5.8 million ($5.0 million after-tax) associated with transaction and employee-related costs, and taxes of $7.6 million associated with the sale and dividends paid in 2005; partially offset by a deferred income tax benefit of $37.0 million. An additional $29.7 million ($30.3 million after-tax) was recognized for the first nine months of 2006, which consisted of a loss on disposal of $15.4 million ($14.7 million after-tax), transaction and employee-related costs of $14.3 million (before and after taxes) and a deferred income tax benefit reduction of $1.3 million.

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The following table details selected financial information, which has been reported as discontinued operations for the quarters and nine months ended September 30, 2006 and 2005:

(Unaudited; $ in millions)

	Third Quarter	
	2006	2005
Sales and other operating revenues	$	180.8
Income from discontinued operations before taxes and loss on disposal	$	10.3
Loss on disposal	(0.2)	
Provision for taxes on income	(0.9)	(4.3)
Income (loss) from discontinued operations	$ (1.1)	6.0

(Unaudited; $ in millions)

	Nine Months Ended September 30,	
	2006	2005
Sales and other operating revenues	$ 179.8	546.4
Income from discontinued operations before taxes and loss on disposal	$ 17.0	36.5
Loss on disposal	(29.7)	
Provision for taxes on income	(5.0)	(14.0)
Income (loss) from discontinued operations	$ (17.7)	22.5

We have not separately identified cash flows from discontinued operations for the quarters and nine months ended September 30, 2006 and 2005, in the Company s Consolidated Statement of Cash Flows.

Magnet Wire North America

On November 15, 2005, Phelps Dodge entered into an agreement to sell substantially all of its North American magnet wire assets, including certain copper inventory, to Rea. The transaction was completed on February 10, 2006, resulting in net sales proceeds of approximately $132 million (net of approximately $10 million in taxes and related expenses).

The transaction resulted in total special, net charges of $18.3 million ($15.8 million after-tax). Of this amount, $13.2 million ($10.7 million after-tax) was recognized in the 2005 fourth quarter, which consisted of an asset impairment charge of $5.4 million ($4.8 million after-tax) to reduce the carrying value of the assets to their estimated fair value less costs to sell, and transaction and employee-related costs of $7.8 million ($5.9 million after-tax). An additional $5.1 million (before and after taxes) was recognized for the first nine months of 2006, which consisted of a loss on disposal of $1.0 million ($2.0 million after-tax) and transaction and employee related costs of $4.1 million ($3.1 million after-tax).

The North American magnet wire asset sale did not meet the criteria for classification as discontinued operations as the Company is continuing to supply Rea with copper rod.

High Performance Conductors of SC & GA, Inc.

On March 4, 2006, Phelps Dodge entered into an agreement to sell HPC to IWG. Under the agreement, IWG purchased the stock of HPC, as well as certain copper inventory. The agreement also includes a contingent payment of up to $3 million based on HPC s 2006 results. The transaction was completed on March 31, 2006. During the 2006 third quarter, net sales proceeds, including settlement of negotiated working capital items, were finalized, which resulted in total net sales proceeds, exclusive of the contingent payment, of approximately $48 million (net of approximately $4 million in taxes and related expenses).

The transaction resulted in total special, net charges of $3.9 million ($4.7 million after-tax), which were recognized in the first nine months of 2006 and consisted of a loss on disposal of $1.0 million ($1.8 million after-tax) and transaction and employee-related costs of $2.9 million (before and after taxes).

The HPC sale did not meet the criteria for classification as discontinued operations as the Company is continuing to supply IWG with copper rod and certain copper alloys.

4. Special Items and Provisions, Net

Following is supplemental information regarding special items and provisions, net, included in operating income that management believes should be separately disclosed to assist in the understanding of the financial performance of the Company and the comparability of its results. This supplemental information is not a substitute for any U.S. GAAP measure. Such special items and provisions are primarily unpredictable and atypical of the Company s operations in a given period. In certain instances, certain transactions such as restructuring costs, asset impairment charges, certain asset disposals or certain legal matters are reflected as special items as they are not considered to be representative of the normal course of business. Additionally, environmental provisions and recoveries are included due to their nature and the impact of these amounts on comparisons between periods. In addition, management measures the performance of its reportable segments excluding special items. The tax impacts of the special items were determined at the marginal effective tax rate of the appropriate taxing jurisdictions, including provision for a valuation allowance, if warranted.

The following table summarizes the pre-tax special items and provisions, net, included in operating income for the quarter and nine months ended September 30, 2006:

	2006 Third Quarter	Nine Months Ended September 30, 2006
PDMC		
Environmental provisions, net	$ (9.9)	(29.5)
Environmental insurance recoveries, net	(0.1)	(0.2)
Historical legal matters	7.0	6.8
	(3.0)	(22.9)
PDI		
Asset impairment charges	(5.6)	(5.6)
Dissolution of international wire and cable entity	(1.2)	(1.2)
Sale of North American magnet wire assets:		
Loss on disposal	(1.2)	(1.0)
Transaction and employee-related costs	0.6	(4.1)
Sale of HPC:		
Gain (loss) on disposal	0.5	(1.0)
Transaction and employee-related costs	(0.2)	(2.9)
	(7.1)	(15.8)
Corporate and Other		
Environmental provisions, net	(19.5)	(21.6)
Environmental insurance recoveries, net	0.1	0.2
Asset impairment charges	(2.8)	(2.8)
Historical legal matters	(0.2)	(0.2)
Sale of non-core real estate		0.5
	(22.4)	(23.9)
	$ (32.5)	(62.6)

For the quarter and nine months ended September 30, 2006, net charges for environmental provisions of $29.4 million and $51.1 million ($22.3 million and $38.8 million after-tax), respectively, were recognized. (Refer to Note 6, Environmental, and Reclamation and Closure Matters, for further discussion of environmental matters.)

On February 10, 2006, Phelps Dodge completed the sale of substantially all its North American magnet wire assets to Rea. In connection with the transaction, we recognized charges of $5.1 million (before and after taxes) for the nine months ended September 30, 2006, which consisted of a loss on disposal of $1.0 million ($2.0 million after-tax) and

transaction and employee-related costs of $4.1 million ($3.1 million after-tax). (Refer to Note 3, Divestitures, for further discussion.)

On March 31, 2006, Phelps Dodge completed the sale of HPC to IWG. In connection with the transaction, we recognized charges of $3.9 million ($4.7 million after-tax) for the nine months ended September 30, 2006, which consisted of a loss on disposal of $1.0 million ($1.8 million after-tax) and transaction and employee-related costs of $2.9 million (before and after taxes). (Refer to Note 3, Divestitures, for further discussion.)

In the 2006 third quarter, Phelps Dodge International Corporation (PDIC) recognized asset impairment charges of $5.6 million (before and after taxes), which were determined through an assessment of fair market value based on projected cash flows.

In the 2006 third quarter, asset impairment charges of (i) $2.0 million ($1.5 million after-tax) were recognized for our El Paso, Texas, magnet wire facility, which ceased operations in the 2004 fourth quarter, and (ii) $0.8 million ($0.6 million after-tax) for our Laurinburg, North Carolina, magnet wire facility, which was permanently closed in the 2003 fourth quarter. These impairments were determined through an assessment of fair market value as determined by an independent appraisal.

In the 2006 third quarter, PDIC recognized a net charge of $1.2 million (before and after taxes) for the dissolution of a telephone cable operation in El Salvador.

For the nine months ended September 30, 2006, net gains of $6.6 million ($5.0 million after-tax) were recognized for legal matters. These gains included $7.0 million ($5.3 million after-tax) for settlement of an historical Cyprus Amax Minerals Company lawsuit in the 2006 third quarter.

The following table summarizes the pre-tax special items and provisions, net, included in operating income for the quarter and nine months ended September 30, 2005:

		2005 Third Quarter	Nine Months Ended September 30, 2005
PDMC			
Environmental provisions, net	$	(8.7)	(24.4)
Environmental insurance recoveries, net		(0.1)	(1.2)
Asset impairment charges			(419.1)
Historical legal matters		0.3	15.3
		(8.5)	(429.4)
PDI			
Environmental provisions, net		(0.1)	(0.1)
Asset impairment charges		(2.0)	(2.4)
Restructuring programs/closures		0.3	(0.8)
		(1.8)	(3.3)
Corporate and Other			
Environmental provisions, net		(34.4)	(54.1)
Environmental insurance recoveries, net		0.1	1.2
Historical legal matters		(0.4)	4.3
		(34.7)	(48.6)

$	(45.0)	(481.3)

In the 2005 second quarter, PDMC recorded special charges for asset impairments of $419.1 million ($320.9 million after-tax) at the Tyrone and Cobre mines, Chino smelter and Miami refinery. On June 1, 2005, the Company s board of directors approved expenditures of $210 million to construct a concentrate-leach, direct-electrowinning facility at the Morenci copper mine, and to restart its concentrator, which had been idle since 2001. The concentrate-leach facility will utilize Phelps Dodge s proprietary medium-temperature, pressure leaching and direct-electrowinning technology that has been demonstrated at our Bagdad, Arizona, copper mine. The concentrate-leach, direct-electrowinning facility is expected to be in operation by mid-2007, with copper production projected to be approximately 150 million pounds per year. Concentrate-leach technology, in conjunction with a conventional milling and flotation concentrator, allows copper in sulfide ores to be transformed into copper cathode through efficient pressure leaching and

electrowinning processes instead of smelting and refining. Historically, sulfide ores have been processed into copper anodes through a smelter. This decision had consequences for several of our other southwest U.S. copper operations, resulting in the impairment of certain assets.

With future Morenci copper concentrate production being fed into the concentrate-leach facility, the operating smelter in Miami, Arizona, will be sufficient to treat virtually all remaining concentrate expected to be produced by Phelps Dodge at our operations in the southwestern United States. Accordingly, the Chino smelter located near Hurley, New Mexico, which had been on care-and-maintenance status since 2002, was permanently closed and demolition initiated. With the closing of the Chino smelter, we had unnecessary refining capacity in the region. Because of its superior capacity and operating flexibility, our refinery in El Paso, Texas, continues to operate. The El Paso refinery is more than twice the size of our refinery in Miami, Arizona, and has sufficient capacity to refine all anodes expected to be produced from our operations in the southwestern United States given the changes brought by the above-mentioned Morenci project. Accordingly, the Miami refinery, which had been on care-and-maintenance status since 2002, was permanently closed. As a result of the decision to close the Chino smelter and the Miami refinery, we recorded asset impairment charges during the 2005 second quarter of $89.6 million ($68.6 million after-tax) and $59.1 million ($45.2 million after-tax), respectively, to reduce the related carrying values of these properties to their respective salvage values.

The steps being taken at Morenci also impacted our Tyrone and Cobre mines in New Mexico. The Tyrone mine had been partially curtailed since 2003, while activities at the Cobre mine were suspended in 1999, with the exception of limited mining activities. Future economics of these mines will be affected by significantly higher acid costs resulting from their inability to obtain low-cost acid from the Chino smelter. These factors caused Phelps Dodge to reassess the recoverability of the long-lived assets at both the Tyrone and Cobre mines. This reassessment, which was based on an analysis of cash flows associated with the related assets, indicated that the assets were not recoverable and that asset impairment charges were required.

Tyrone s impairment of $210.5 million ($161.2 million after-tax) primarily resulted from fundamental changes to its life-of-mine (LOM) cash flows mostly due to higher than expected acid costs and the decision to accelerate reclamation of portions of stockpiles around the mine perimeter. The impact of these assumptions increased costs and decreased Tyrone s copper ore reserves by approximately 155 million pounds, or 14 percent. The following table summarizes the reduction in reserves and higher cost of delivered acid for Tyrone included in the 2005 second quarter impairment analysis and the then-current LOM plan:

	2004	June 2005	Reduction
Leach ore (in million tons)	275	242	33
Grade	0.31%	0.31%	
Saleable copper (in million pounds)	1,073	918	155

	2004	2005	Increase
Delivered acid costs:			
Per ton*	$ 31	51	20
In millions	$ 61	90	29

* Represents the blended cost of internally sourced acid

and acid obtained from third-party sources.

Cobre s impairment of $59.9 million ($45.9 million after-tax) primarily resulted from projected higher acid, external smelting and freight costs. Previously, Cobre s operating plan was based on lower-cost acid from the Chino smelter. However, upon the decision to close the Chino smelter, the long-term operating plan reflected that Cobre would have to obtain acid from third-party sources (an increase from approximately $25 per ton to $60 per ton). Additionally, the closure of the Chino smelter would require Cobre to transport its concentrates longer distances to the Miami smelter at approximately $23 per ton and overseas to third parties at approximately $85 per ton for processing versus concentrate freight charges of approximately $15 per ton transported to the Chino smelter. In addition, as a result of the Chino smelter being permanently closed, the charges reflected estimated higher restart and operating costs of running the Cobre mill. Additionally, the cost for building a tailing pipeline from Cobre to the Chino mine increased based upon a detailed engineering evaluation recommending (i) extending the pipeline an additional nine miles, (ii) adding a new thickener and booster pump station and (iii) a larger pipe size. The higher estimated restart and operating costs associated with running the Cobre mill and the increased costs for building a tailing pipeline from Cobre to the Chino mine were used only for our analysis of projected cash flows and resulted in the Cobre millable reserves no longer being economical at our long-term copper price and costs forecasts. Accordingly, the current development plan does not include the operation of the Cobre mill.

For the quarter and nine months ended September 30, 2005, net charges for environmental provisions of $43.2 million and $78.6 million ($33.1 million and $60.0 million after-tax), respectively, were recognized.

For the nine months ended September 30, 2005, Phelps Dodge Magnet Wire recorded special, pre-tax charges of $2.4 million ($1.9 million after-tax) for asset impairments. This included an impairment charge of (i) $2.0 million ($1.6 million after-tax) recognized in the 2005 third quarter at our El Paso, Texas, magnet wire facility, which

ceased operations during the 2004 fourth quarter, and (ii) $0.4 million ($0.3 million after-tax) recognized in the 2005 second quarter at our Laurinburg, North Carolina, magnet wire facility, which was permanently closed in the 2003 fourth quarter. The amounts of these asset impairments were determined through an assessment of fair market value as determined by independent appraisals.

For the nine months ended September 30, 2005, net pre-tax charges of $0.8 million (net zero after-tax) were recognized for Phelps Dodge Magnet Wire s restructuring programs and facility closures. (Refer to the Company s Form 10-K for the year ended December 31, 2005, for additional discussion.)

For the nine months ended September 30, 2005, net pre-tax gains of $19.6 million ($15.7 million after-tax) were recognized for legal matters. These gains included $14.8 million ($11.2 million after-tax) of net settlements on historical legal matters, an adjustment of $3.6 million (before and after taxes) related to an historical Cyprus Amax Minerals Company lawsuit and a net settlement of $1.2 million ($0.9 million after-tax) reached with one of our insurance carriers associated with potential future legal matters.

5. New Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R), which requires recognition of a net liability or asset to report the funded status of defined benefit pension and other postretirement plans on the balance sheet and recognition (as a component of other comprehensive income) of changes in the funded status in the year in which the changes occur. Additionally, SFAS No. 158 requires measurement of a plan s assets and obligations as of the balance sheet date and additional annual disclosures in the notes to the financial statements. The recognition and disclosure provisions of SFAS No. 158 are effective for fiscal years ending after December 15, 2006, while the requirement to measure a plan s assets and obligations as of the balance sheet date is effective for fiscal years ending after December 15, 2008. We are currently evaluating the impact the adoption of SFAS No. 158 will have on our financial reporting and disclosures.

In September 2006, FASB issued SFAS No. 157, Fair Value Measurements, which provides enhanced guidance for using fair value to measure assets and liabilities. SFAS No. 157 establishes a common definition of fair value, provides a framework for measuring fair value under U.S. GAAP and expands disclosures requirements about fair value measurements. SFAS No. 157 is effective for financial statements issued in fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. We are currently evaluating the impact, if any, the adoption of SFAS No. 157 will have on our financial reporting and disclosures.

In June 2006, FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109 (FIN 48), which prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are currently evaluating the impact the adoption of FIN 48 will have on our financial reporting and disclosure requirements.

In February 2006, FASB issued SFAS No. 155, Accounting for Certain Hybrid Financial Instruments, an amendment of FASB Statements No. 133 and 140, which eliminates the exemption from applying SFAS No. 133, Accounting for Derivative Instruments and Hedging Activities, to interests on securitized financial assets so that similar instruments are accounted for similarly regardless of the form. This Statement also allows the election of fair value measurement at acquisition, at issuance or when a previously recognized financial instrument is subject to a remeasurement event, on an instrument-by-instrument basis, in cases in which a derivative would otherwise have to be bifurcated. SFAS No. 155 is effective for all financial instruments acquired or issued in an entity s first fiscal year beginning after September 15, 2006. The adoption of this Statement is not expected to have a material impact on our financial reporting and disclosures.

Effective January 1, 2006, the Company adopted Emerging Issues Task Force (EITF) Issue No. 04-6, Accounting for Stripping Costs Incurred During Production in the Mining Industry, which specifies that stripping costs incurred

during the production phase of a mine are considered variable production costs and included in the cost of inventory produced during the period that the stripping costs are incurred. Prior to adoption of EITF Issue No. 04-6, Phelps Dodge had historically charged stripping costs to maintain production at operating mines to operations as incurred. Additionally, stripping costs incurred at new mines or at operating mines outside existing pit limits that were expected to benefit future production were capitalized and amortized under the units-of-production method. This EITF requires capitalization of pre-stripping or mine development costs only to the extent that the production phase has not commenced, which is determined when salable minerals, excluding removal of *de minimis* material, are extracted from an ore body. Upon adoption in the 2006 first quarter, we recorded an increase to our work-in-process inventories of $46.0 million, a net decrease to our capitalized mine development of $19.3 million, a net increase to minority interests in consolidated subsidiaries of $1.3 million and a cumulative effect adjustment to increase beginning retained earnings by $19.8 million, net of deferred income taxes of $8.2 million.

Effective January 1, 2006, the Company adopted SFAS No. 123-R, which amends SFAS No. 123 and requires all share-based payments to employees, including employee stock options, be measured at fair value and expensed over the requisite period (generally the vesting period) for awards expected to vest. The Company has elected to use the modified prospective method for adoption, which requires compensation expense to be recognized for all unvested stock options and restricted stock beginning in the first quarter of adoption. (Refer to Note 2, Share-Based Compensation, for further discussion.)

Effective December 31, 2005, the Company adopted FIN 47, Accounting for Conditional Asset Retirement Obligations an interpretation of FASB Statement No. 143, which clarifies the term conditional asset retirement obligation as used in SFAS No. 143, Accounting for Asset Retirement Obligations. With the adoption of FIN 47, we recognize conditional asset retirement obligations as

liabilities when sufficient information exists to reasonably estimate the fair value. Any uncertainty about the amount and/or timing of future settlement of a conditional asset retirement obligation is factored into the measurement of the liability. Upon adoption in the 2005 fourth quarter, we recorded an increase to our closure and reclamation reserve of $17.9 million, a net increase in our mining properties assets of $4.4 million and a cumulative effect loss of $10.1 million, net of deferred income taxes of $3.4 million.

In November 2005, FASB issued FASB Staff Position (FSP) Nos. FAS 115-1 and FAS 124-1, The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments (FSP 115-1/124-1). FSP 115-1/124-1 provides guidance on determining when investments in certain debt and equity securities are considered impaired, whether that impairment is other-than-temporary and on measuring such impairment loss. FSP 115-1/124-1 also includes accounting considerations subsequent to the recognition of an other-than-temporary impairment and requires certain disclosures about unrealized losses that have not been recognized as other-than-temporary impairments. The adoption of FSP 115-1/124-1 in the 2006 first quarter did not have a material impact on our financial reporting and disclosures.

In September 2005, FASB ratified the consensus reached by the EITF on Issue No. 04-13, Accounting for Purchases and Sales of Inventory with the Same Counterparty. The consensus concluded that two or more legally separate exchange transactions with the same counterpart should be combined and considered as a single arrangement for accounting purposes, if they are entered into in contemplation of one another. The EITF also reached a consensus that nonmonetary exchanges of inventory within the same business should be recognized at fair value. The adoption of EITF Issue No. 04-13 in the 2006 second quarter did not have a material impact on our financial reporting and disclosures.

In May 2005, FASB issued SFAS No. 154, Accounting Changes and Error Corrections, a replacement of APB Opinion No. 20 and FASB Statement No. 3. SFAS No. 154 requires retrospective application to prior periods financial statements for changes in accounting principle, unless it is impracticable to determine either the period-specific effects or the cumulative effect of the change. This Statement applies to all voluntary changes in accounting principle as well as to changes required by an accounting pronouncement in the unusual instance that the pronouncement does not include specific transition provisions. SFAS No. 154 further requires a change in depreciation, amortization or depletion method for long-lived, non-financial assets to be accounted for as a change in accounting estimate effected by a change in accounting principle. Corrections of errors in the application of accounting principles will continue to be reported by retroactively restating the affected financial statements. The Company adopted the provisions of SFAS No. 154 on January 1, 2006.

In November 2004, FASB issued SFAS No. 151, Inventory Costs, an Amendment of ARB No. 43, Chapter 4. SFAS No. 151 clarifies that abnormal amounts of idle facility expense, freight, handling costs and wasted materials (spoilage) should be recognized as current period charges and requires the allocation of fixed production overhead to inventory based on the normal capacity of the production facilities. The adoption of SFAS No. 151 in the 2006 first quarter did not have a material impact on our financial reporting and disclosures.

6. Environmental, and Reclamation and Closure Matters

At September 30, 2006, and December 31, 2005, environmental reserves totaled $376.8 million and $367.9 million, respectively, for environmental liabilities attributed to Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) or analogous state programs and for estimated future costs associated with environmental matters at closed facilities and closed portions of certain operating facilities.

The following table summarizes our environmental reserve activities for the quarter and nine months ended September 30, 2006:

(Unaudited; $ in millions)

	2006	Nine Months Ended

		Third Quarter	September 30, 2006
Balance, beginning of period	$	366.8	367.9
Additions to reserves*		34.4	61.3
Reductions in reserve estimates		(1.6)	(1.6)
Spending against reserves		(22.8)	(50.8)
Balance, end of period	$	376.8	376.8

* The quarter and nine months ended September 30, 2006, included $3.3 million and $8.5 million, respectively, associated with a cash settlement to Phelps Dodge with potentially responsible parties that was not charged to expense.

The site currently considered to be most significant is the Pinal Creek site near Miami, Arizona, where $103.5 million remained in the environmental reserve at September 30, 2006. Phelps Dodge Miami, Inc. and the other Pinal Creek Group (PCG) members have been pursuing contribution litigation against three other parties involved with the site. Phelps Dodge Miami, Inc. dismissed its contribution claims against one defendant when another PCG member agreed to be responsible for any share attributable to that defendant. Phelps Dodge Miami, Inc. and the other PCG members settled their contribution claims against another defendant in April 2005, which resulted in cancellation of the Phase I trial. While the terms of the settlement are confidential, the proceeds of the settlement will be used to address remediation at the Pinal Creek site. The Phase II trial, which will allocate liability, has been postponed due to a discovery dispute and related orders and appeals and has not yet been rescheduled.

At September 30, 2006, the cost range for reasonably possible outcomes for all reservable remediation sites (including Pinal Creek s estimate of approximately $93 million to $206 million) was estimated to be from approximately $331 million to $630 million (of which $377 million has been reserved).

Phelps Dodge has a number of sites that are not the subject of an environmental reserve because it is not probable that a successful claim will be made against the Company for those sites, but for which there is a reasonably possible likelihood of an environmental remediation liability. At September 30, 2006, the cost range for reasonably possible outcomes for all such sites, for which an estimate can be made, was estimated to be from approximately $3

million to approximately $17 million. The liabilities arising from potential environmental obligations that have not been reserved at this time may be material to the operating results of any single quarter or year in the future. Management, however, believes the liability arising from potential environmental obligations is not likely to have a material adverse effect on the Company s liquidity or financial position as such obligations could be satisfied over a period of years.

We recognize asset retirement obligations (AROs) as liabilities when incurred, with initial measurement at fair value. In addition, with the adoption of FIN 47, we recognize conditional AROs as liabilities when sufficient information exists to reasonably estimate the fair value. These liabilities are accreted to full value over time through charges to income. In addition, asset retirement costs (ARCs) are capitalized as part of the related asset s carrying value and are depreciated primarily on a units-of-production basis over the asset s useful life. Reclamation costs for future disturbances are recognized as an ARO and as a related ARC in the period incurred. The Company s cost estimates are reflected on a third-party cost basis and comply with the Company s legal obligation to retire tangible, long-lived assets as defined by SFAS No. 143. These cost estimates may differ from financial assurance cost estimates due to a variety of factors, including obtaining updated cost estimates for reclamation activities, the timing of reclamation activities, changes in the scope of reclamation activities and the exclusion of certain costs not accounted for under SFAS No. 143.

The following tables summarize our asset retirement obligations and asset retirement cost activities for the quarter and nine months ended September 30, 2006:

Asset Retirement Obligations
(Unaudited; $ in millions)

	2006 Third Quarter	Nine Months Ended September 30, 2006
Balance, beginning of period	$ 386.7	398.4
New liabilities during the period	1.4	3.9
Accretion expense	6.5	19.6
Payments	(20.0)	(45.5)
Revisions in estimated cash flows		(1.8)
Balance, end of period	$ 374.6	374.6

Asset Retirement Costs
(Unaudited; $ in millions)

	2006 Third Quarter	Nine Months Ended September 30, 2006
Gross balance, beginning of period	$ 199.9	199.2
New assets during the period	1.4	3.9
Revisions in estimated cash flows		(1.8)

Gross balance, end of period		201.3	201.3
Less accumulated depreciation, depletion and amortization		97.0	97.0
Balance, end of period	$	104.3	104.3

We have estimated that our share of the total cost of AROs, including anticipated future disturbances and excluding cumulative payments, as of September 30, 2006, aggregated approximately $1.4 billion (unescalated, undiscounted and on a third-party cost basis), leaving approximately $1 billion remaining to be accreted over time. These aggregate costs may increase or decrease materially in the future as a result of changes in regulations, technology, permit modifications or updates, mine plans or other factors and as actual reclamation spending occurs. ARO activities and expenditures generally are made over an extended period of time commencing near the end of the mine life; however, certain reclamation activities could be accelerated if they are determined to be economically beneficial.

In December 2005, the Company established a trust dedicated to funding our global environmental reclamation and remediation activities and made an initial cash contribution of $100 million. In March 2006, the Company made an additional cash contribution of $300 million to the trust. The Company also has trust assets that are legally restricted to fund a portion of its AROs for Chino, Tyrone and Cobre as required for New Mexico financial assurance. At September 30, 2006, and December 31, 2005, the fair value of the trust assets was approximately $507 million and $191 million, respectively, of which approximately $96 million was legally restricted at September 30, 2006.

7. Contingencies

Significant New Mexico Environmental and Reclamation Programs

The Company s New Mexico operations, Chino, Tyrone, Cobre and Hidalgo, each are subject to regulation under the New Mexico Water Quality Act and the Water Quality Control Commission (WQCC) regulations adopted under that Act. The New Mexico Environment Department (NMED) has required each of these operations to submit closure plans for NMED s approval. The closure plans must describe the measures to be taken to prevent groundwater quality standards from being exceeded following closure of the discharging facilities and to abate any groundwater or surface water contamination.

Chino, Tyrone and Cobre also are subject to regulation under the New Mexico Mining Act (the Mining Act), which was enacted in 1993, and the Mining Act Rules, which are administered by the Mining and Minerals Division (MMD) of the New Mexico Energy, Minerals and Natural Resources Department. Under the Mining Act, Chino, Tyrone and Cobre are required to submit and obtain approval of closeout plans describing the reclamation to be performed following closure of the mines or portions of the mines.

Financial assurance is required to ensure that funding will be available to perform both the closure and the closeout plans if the operator is not able to perform the work required by the plans. The amount of the financial assurance is based upon the estimated cost for a third party to complete the work specified in the plans, including any long-term operation and maintenance, such as operation of water treatment systems. NMED and MMD calculate the required amount of financial assurance using a net present value (NPV) method, based upon approved discount and escalation rates, when the closure plan and/or closeout plan require performance over a long period of time.

In April 2005, the governor of New Mexico signed Senate Bill 986, effective June 17, 2005, which removes the requirement to provide financial assurance for the gross receipts tax levied on closure work.

Eliminating this requirement is expected to reduce our New Mexico financial assurance up to approximately $27 million (NPV basis).

The Company s cost estimates to perform the work itself (internal cost basis) generally are lower than the cost estimates used for financial assurance due to the Company s historical cost advantages, savings from the use of the Company s own personnel and equipment as opposed to third-party contractor costs, and opportunities to prepare the site for more efficient reclamation as mining progresses.

Chino, Tyrone and Cobre each have NMED-issued closure permits and MMD-approved closeout plans. Chino s closure permit was appealed to the WQCC by a third party. The appeal originally was dismissed by the WQCC on procedural grounds, but that decision was overturned by the New Mexico Court of Appeals. The WQCC has postponed the hearing on the Chino closure permit pending a report by the parties regarding settlement discussions. Tyrone appealed certain conditions in its closure permit to the WQCC, which upheld the permit conditions. Tyrone appealed the WQCC s decision to the Court of Appeals, and on June 15, 2006, the Court of Appeals overturned two conditions that Tyrone had challenged in its closure permit. The New Mexico Supreme Court denied Petitions for Certiorari filed by other parties. The case will be remanded by the Court of Appeals to the WQCC for further proceedings. Hidalgo has applied for renewal of its discharge permit, which includes a requirement for an updated closure plan. Hidalgo expects NMED to issue a new permit, including permit conditions regarding closure and financial assurance, within the next few months.

The terms of the NMED closure permits and MMD-approved closeout plans for Chino, Tyrone and Cobre require the facilities to conduct supplemental studies concerning closure and closeout, including feasibility studies to evaluate additional closure and reclamation alternatives. The feasibility study is due, along with amended closure plans, before the end of the five-year permit terms, which end in 2008 for Chino and Tyrone and in 2009 for Cobre. The terms of the NMED closure permits also require the facilities to prepare and submit abatement plans to address groundwater that exceeds New Mexico groundwater quality standards as well as potential sources of future groundwater contamination. Changes to the existing closure plans and additional requirements arising from the abatement plans could increase or decrease the cost of closure and closeout. Cobre also has submitted an application to MMD and NMED for a standby permit to defer implementation of closure and reclamation requirements while Cobre continues on care-and-maintenance status.

The terms of the permits also require Chino, Tyrone, Cobre and Hidalgo to provide and maintain financial assurance based upon the estimated cost to the state of New Mexico to implement the closure and closeout plans in the event of a default by the operators. The third-party cost estimates for financial assurance under the existing permits are $395 million for Chino, $439 million for Tyrone and $45 million for Cobre on an undiscounted and unescalated basis over the 100-year period of the closure and closeout plans. Hidalgo is updating its cost estimate as part of its pending closure permit renewal. These cost estimates are converted to an NPV basis to determine the amount of financial assurance required for each facility. The current financial assurance amounts are $192 million for Chino, $271 million for Tyrone and $29 million for Cobre. In addition, Hidalgo has provided financial assurance for approximately $11 million under the terms of its existing discharge permit.

Up to 70 percent of the financial assurance for Chino, Tyrone and Cobre is in the form of third-party guarantees provided by Phelps Dodge. The terms of the guarantees require Phelps Dodge to meet certain financial tests that, in part, require Phelps Dodge to maintain an investment-grade corporate credit rating. Phelps Dodge s senior unsecured debt currently carries an investment-grade credit rating. In the event of a ratings downgrade below investment-grade, some additional portion of the financial assurance would have to be provided in a different form. The balance of the financial assurance (approximately 30 percent) is provided in the form of trust funds, real estate collateral, surety bonds and letters of credit.

The Company estimates its total cost, on an internal cost basis, to perform the requirements of the approved closure and closeout permits to be approximately $287 million for Chino, $354 million for Tyrone and $41 million for Cobre (undiscounted and unescalated) over the 100-year period of the closure and closeout plans. The above cost estimates do not include cumulative payments through September 30, 2006. These estimates are lower than the

estimated costs used as the basis for financial assurance amounts due to the factors discussed above, and reflect our internal cost estimate. Our cost estimates, on a third-party cost basis used to determine the fair value of our closure and closeout accrual for SFAS No. 143, totaled approximately $395 million for Chino, $460 million for Tyrone and $47 million for Cobre (undiscounted and unescalated). Tyrone s cost estimate includes approximately $21 million of net costs in addition to the financial assurance cost estimate that primarily relates to an increased scope of work for the tailing, stockpiles and other projects, and updated estimates for actual closure expenditures incurred. Cobre s cost estimate includes approximately $2 million of costs in addition to the financial assurance cost estimate primarily for increased scope of work for stockpiles and characterization studies. At September 30, 2006, we had accrued approximately $68 million for Chino, $163 million for Tyrone, $5 million for Cobre and $5 million for Hidalgo. By comparison, at December 31, 2005, we had accrued approximately $65 million for Chino, $186 million for Tyrone, $8 million for Cobre and $4 million for Hidalgo.

During 2006, Tyrone continued certain closure activities, including completion of a project to remove a portion of the 1C stockpile and initiating reclamation of the adjacent stockpile area. Additionally, Tyrone continued accelerated reclamation of tailing impoundments located in Mangas Valley, including completion of reclamation of one tailing impoundment. Through September 30, 2006, approximately $67 million has been spent on these actions, including approximately $21 million on the 1C stockpile. In 2005, Tyrone submitted an application to reduce the required amount of financial assurance by $32 million to reflect the completion of the 1C stockpile removal project and 2005 legislation that eliminated a requirement to include New Mexico gross receipts tax in the cost estimates used for financial assurance. On December 12, 2005, the state concurred with the reduction and Tyrone is currently negotiating changes in financial assurance with the state.

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In December 1994, Chino entered into an Administrative Order on Consent (AOC) with NMED. The AOC requires Chino to perform a CERCLA quality investigation of environmental impacts and potential risks to human health and the environment associated with portions of the Chino property affected by historical mining operations. The remedial investigations began in 1995 and are still under way, although substantial portions of the remedial investigations are near completion. The Company expects that some remediation will be required and is considering interim remediation proposals, although no feasibility studies have yet been completed. Chino has begun remediating residential yards in the town of Hurley after agreement was reached with NMED on cleanup levels. NMED has not yet issued a record of decision regarding any additional remediation that may be required under the AOC. As of September 30, 2006, the Company s estimated cost for all aspects of the AOC is approximately $23 million. In addition to work under the AOC, Chino has implemented projects to control blowing dust from tailing impoundments. Chino continues work on excavating and removing copper-bearing material from an area known as Lake One for copper recovery in existing leach stockpiles at the mine. As of September 30, 2006, the Company s estimated cost for the remaining work at Lake One is approximately $5 million. The Company s aggregate environmental reserve for liability under the Chino AOC, the interim work on the tailing impoundments and Lake One, as described above, is approximately $33 million at September 30, 2006.

Significant Changes in International Closure and Reclamation Programs

Sociedad Minera Cerro Verde S.A.A.

On August 15, 2005, the Peruvian Ministry of Energy and Mines published the final regulation associated with the Mine Closure Law. The regulation required companies to submit closure plans for existing projects within one year after August 15, 2005, and for new projects within one year after approval of the Environment Impact Statement. Additionally, the regulation sets forth the financial assurance requirements, including guidance for calculating the estimated cost and the types of financial assurance instruments that can be utilized.

In accordance with the new regulation, Cerro Verde submitted its closure plan on August 14, 2006. Cerro Verde is also in the process of determining its financial assurance obligations associated with the new regulation. Based on the submitted closure plan s scope of work, the revised site-wide cost estimate is approximately $80 million (undiscounted, unescalated and on a third-party cost basis). At both September 30, 2006, and December 31, 2005, Cerro Verde had accrued closure costs of approximately $5 million.

Other

On February 7, 2004, the Chilean Ministry of Mining published and passed a modification to its mining safety regulations. The current published regulation requires a company to submit a reclamation plan within five years of the published regulation. In the 2005 fourth quarter, El Abra and Candelaria completed their comprehensive review of the revised cost estimates based on existing regulations, which resulted in a revision to the ARO estimates. ARO estimates may require further revision if new interpretations or additional technical guidance are published to further clarify the regulation. Final closure plans and related financial assurance requirements will be filed with the Ministry before February 2009. At September 30, 2006, and December 31, 2005, we had accrued closure costs of approximately $23 million and $20 million, respectively, for our Chilean operations.

8. Earnings Per Share

Basic earnings per common share are computed by dividing income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted earnings per common share are computed similarly to basic earnings per common share except that the denominator is increased to include the number of additional common shares that would have been outstanding if the potentially dilutive common shares had been issued, and the numerator excludes preferred stock dividends, unless anti-dilutive. Unvested restricted stock is included in the computation of diluted earnings per common share as the issuance of such shares is contingent upon vesting.

(Unaudited; $ in millions except per share amounts)

	Third Quarter	
	2006	2005
Basic Earnings Per Common Share Computation		
Numerator:		
Income from continuing operations	$ 889.1	360.1
Income (loss) from discontinued operations	(1.1)	6.0
Net income applicable to common shares	$ 888.0	366.1
Denominator:		
Weighted average common shares outstanding*	202.5	197.2
Basic earnings per common share:*		
Income from continuing operations	$ 4.39	1.83
Income (loss) from discontinued operations	(0.01)	0.03
Basic earnings per common share	$ 4.38	1.86
Diluted Earnings Per Common Share Computation		
Numerator:		
Income from continuing operations	$ 889.1	360.1
Income (loss) from discontinued operations	(1.1)	6.0
Net income applicable to common shares	$ 888.0	366.1
Denominator:		
Weighted average common shares outstanding*	202.5	197.2
Weighted average employee stock options*	0.2	0.6
Weighted average restricted stock issued to employees*	0.8	0.8
Weighted average mandatory convertible preferred shares*		4.1
Total weighted average common shares outstanding*	203.5	202.7
Diluted earnings per common share:*		
Income from continuing operations	$ 4.37	1.78
Income (loss) from discontinued operations	(0.01)	0.03
Diluted earnings per common share	$ 4.36	1.81

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(Unaudited; $ in millions except per share amounts)

	Nine Months Ended September 30,	
	2006	2005
Basic Earnings Per Common Share Computation		
Numerator:		
Income from continuing operations	$ 1,711.2	1,412.6
Income (loss) from discontinued operations	(17.7)	22.5
Net income	1,693.5	1,435.1
Preferred stock dividends		(6.8)
Net income applicable to common shares	$ 1,693.5	1,428.3
Denominator:		
Weighted average common shares outstanding*	202.3	193.7
Basic earnings per common share:*		
Income from continuing operations	$ 8.46	7.26
Income (loss) from discontinued operations	(0.09)	0.11
Basic earnings per common share	$ 8.37	7.37
Diluted Earnings Per Common Share Computation		
Numerator:		
Income from continuing operations	$ 1,711.2	1,412.6
Income (loss) from discontinued operations	(17.7)	22.5
Net income applicable to common shares	$ 1,693.5	1,435.1
Denominator:		
Weighted average common shares outstanding*	202.3	193.7
Weighted average employee stock options*	0.2	0.8
Weighted average restricted stock issued to employees*	0.9	0.8
Weighted average mandatory convertible preferred shares*		6.9
Total weighted average common shares outstanding*	203.4	202.2
Diluted earnings per common share:*		
Income from continuing operations	$ 8.42	6.99

Income (loss) from discontinued operations	(0.09)	0.11
Diluted earnings per common share	$ 8.33	7.10

* Weighted average shares outstanding and earnings per common share for the quarter and nine months ended September 30, 2005, have been adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15, Shareholders Equity, for further discussion.)

9. Provision for Taxes on Income

The Company s income tax provision from continuing operations for the 2006 third quarter resulted from taxes on earnings at international operations ($194.9 million) and U.S. operations ($180.4 million), including benefits from the release of valuation allowances ($0.5 million).

The Company s income tax provision from continuing operations for the nine months ended September 30, 2006, resulted from taxes on earnings at international operations ($569.5 million) and U.S. operations ($254.3 million), including benefits from the release of valuation allowances ($7.4 million).

The release in our domestic valuation allowances for the quarter and nine months ended September 30, 2006, was attributable to a portion of our U.S. federal minimum tax credits, as well as our state net operating loss carryforwards.

Phelps Dodge provides reserves for various unresolved tax issues. During the 2006 first quarter, certain of these issues were favorably resolved, resulting in a reduction of the Company s income tax provision from continuing operations of approximately $10 million.

In addition, during January 2006, a change in Arizona tax law impacting the apportionment of income became effective resulting in a reduction of the Company s income tax provision from continuing operations of approximately $6 million.

The difference between our effective income tax rate of approximately 27 percent for the nine months ended September 30, 2006, and the U.S. federal statutory rate of 35 percent primarily was due to percentage depletion deductions for regular tax purposes in the United States and Peruvian reinvestment deductions associated with the Cerro Verde mine expansion.

The Company s income tax provision from continuing operations for the 2005 third quarter resulted from taxes on earnings at U.S. operations ($57.0 million), including recognition of valuation allowances ($34.1 million), and taxes on earnings at international operations ($47.3 million), including benefits from the release of valuation allowances ($0.9 million).

The Company s income tax provision from continuing operations for the nine months ended September 30, 2005, resulted from taxes on earnings at U.S. operations ($179.2 million), including recognition of valuation allowances ($2.2 million), and taxes on earnings at international operations ($121.2 million), including recognition of valuation allowances ($0.6 million).

The difference between our effective income tax rate of approximately 16 percent for the nine months ended September 30, 2005, and the U.S. federal statutory rate of 35 percent primarily was due to (i) percentage depletion deductions for regular tax purposes in the United States, (ii) a portion of the gain on the sale of our Southern Peru Copper Corporation (SPCC) investment being offset by previously unrecognized capital loss carryovers, (iii) the extraterritorial income exclusion associated with foreign molybdenum sales, (iv) Peruvian reinvestment benefits resulting from the Cerro Verde mine expansion and (v) deferred income taxes not being provided on the change in interest gain from the Cerro Verde stock issuance, as we expected to permanently reinvest our portion of the proceeds in that entity.

Cerro Verde s Mining Stability Agreement, which was executed in 1998, contains a provision that allows it to exclude from taxable income qualifying profits that are reinvested in an investment program filed with and approved by the Ministry of Energy and Mines (the Mining Authority). On December 9, 2004, Cerro Verde received confirmation from the Mining Authority that approximately $800 million of its sulfide expansion project qualified for the taxable exclusion. The total reinvestment benefit is limited to 30 percent of the qualifying investment or up to $240 million. In order to obtain the tax benefit, Cerro Verde is required to reinvest its qualifying profits of up to $800 million during the four-year period from 2004 through 2007, which could be extended at the discretion of the Mining Authority for up to three years through 2010. Qualifying profits for each year are limited to 80 percent of the lesser of after-tax book income or undistributed earnings. Based on qualified earnings for the first nine months of 2006, Cerro Verde recorded a current reinvestment benefit of approximately $72 million and a deferred tax benefit of approximately $21 million. At September 30, 2006, Cerro

Verde had a total deferred tax asset of approximately $63 million associated with its sulfide expansion project.

10. Accounting for Derivative Instruments and Hedging Activities

We do not purchase, hold or sell derivative financial instruments unless we have an existing asset or obligation or we anticipate a future activity that is likely to occur and will result in exposing us to market risk. We do not enter into any instruments for speculative purposes. We use various strategies to manage our market risk, including the use of derivative instruments to limit, offset or reduce our market exposure. Derivative financial instruments are used to manage well-defined commodity price, energy, foreign exchange, and interest rate risks from our primary business activities. The fair values of our derivative instruments are based on valuations provided by third parties, purchased derivative pricing models or widely published market closing prices at period end. Refer to Management s Discussion and Analysis of Financial Condition and Results of Operations and Note 22, Derivative Financial Instruments and Fair Value of Financial Instruments, to the Consolidated Financial Statements included in the Company s Form 10-K for the year ended December 31, 2005, for further discussion of our derivative instruments.

Phelps Dodge entered into programs to protect a portion of its expected copper production by purchasing zero-premium copper collars (consisting of put options and call options) and copper put options. The copper collars and copper put options are settled on an average London Metal Exchange (LME) pricing basis for their respective hedge periods. The copper collar put options and purchased copper put options are settled monthly for 2006 and annually for 2007; all of the copper collar call options are settled annually. Phelps Dodge entered into the programs as insurance to help ameliorate the effects of unanticipated copper price decreases.

The following table provides a summary of PDMC s zero-premium copper collar and copper put option programs for 2006 and 2007:

(Unaudited)

	2006	2007
Copper Collars:		
Pounds of zero-premium copper collars purchased (in millions)	564	486
Average LME put strike price (floor) per pound	$ 0.954	0.950
Annual average LME call strike price (ceiling) per pound	$ 1.632	2.002
Associated pre-tax gains (charges) for the 2006 third quarter (A):		
Intrinsic value component (in millions)	$ (52)	(120)
Time value component (in millions)	$	27
Associated pre-tax gains (charges) for the nine months ended September 30, 2006 (A):		
Intrinsic value component (in millions)	$ (669)	(584)
Time value component (in millions)	$ 13	28
Copper Put Options:		
Pounds of copper put options purchased (in millions)	564	730
Average LME put strike price per pound	$ 0.950	0.950
Premium cost per pound	$ 0.020	0.023
Associated pre-tax charges for the 2006 third quarter (A):		
Intrinsic value component (in millions)	$	
Time value component (in millions)	$	
Associated pre-tax charges for the nine months ended September 30, 2006 (A):		
Intrinsic value component (in millions)	$	
Time value component (in millions)	$	(3)

(A) The 2006 unrealized pre-tax charges resulted from the 2006 LME price average of $3.105 per pound exceeding the $1.632 per pound ceiling of our 2006 zero-premium copper collars. The cumulative pre-tax charges for our 2006 copper collars and copper put options, including amounts recognized in 2005, were approximately $831 million, primarily reflecting intrinsic value charges and put option premiums. The 2007 unrealized pre-tax charges resulted from the 2007 LME price average of $3.285 per pound exceeding the $2.002 per pound ceiling of our 2007 zero-premium copper collars. The cumulative pre-tax charges for our 2007 copper collars and copper put options,

including amounts recognized in 2005, were approximately $608 million, consisting of approximately $584 million for the intrinsic value component and approximately $7 million for the time value component, with the remainder for put option premiums.

Transactions under these copper price protection programs do not qualify for hedge accounting treatment under SFAS No. 133 and are adjusted to fair market value based on the forward curve price and implied volatility as of the last day of the respective reporting period, with the gain or loss recorded in revenues. The actual impact of our 2006 and 2007 zero-premium copper collar price protection programs will not be fully determinable until the maturity of the copper collars at each respective year end, with final adjustments based on the average annual price.

During the 2006 first quarter, approximately $187 million was paid to the respective counterparts for the PDMC and El Abra 2005 zero-premium copper collar programs.

During the quarter and nine months ended September 30, 2006, we reclassified approximately $1.1 million and $9.7 million, respectively, from other comprehensive income to the Consolidated Statement of Income primarily as a result of our international metal swap contracts.

During the quarter and nine months ended September 30, 2005, we reclassified approximately $5.0 million and $6.6 million, respectively, of other comprehensive income to the Consolidated

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Statement of Income primarily as a result of our domestic energy (diesel fuel and natural gas) price protection contracts.

11. Pension and Postretirement Benefits

The following tables present the components of net periodic benefit cost for pension benefits and postretirement benefits for the quarters and nine months ended September 30, 2006 and 2005:

Pension Benefits
(Unaudited; $ in millions)

	Third Quarter	
	2006	2005
Service cost benefits earned during the period	$ 5.6	7.1
Interest cost on benefit obligation	17.5	18.6
Expected return on plan assets	(25.9)	(21.6)
Amortization of prior service cost	0.7	0.9
Amortization of actuarial loss	4.4	3.5
Curtailment and special retirement benefits		0.1
Net periodic benefit cost	$ 2.3	8.6

	Nine Months Ended September 30,	
	2006	2005
Service cost benefits earned during the period	$ 16.7	21.1
Interest cost on benefit obligation	52.6	55.9
Expected return on plan assets	(77.8)	(64.7)
Amortization of prior service cost	2.0	2.5
Amortization of net actuarial loss	13.4	10.6
Curtailment and special retirement benefits	0.5	0.1
Net periodic benefit cost	$ 7.4	25.5

Postretirement Benefits
(Unaudited; $ in millions)

	Third Quarter	
	2006	2005
Service cost benefits earned during the period	$ 0.3	1.1
Interest cost on benefit obligation	3.6	5.1
Expected return on plan assets	(1.7)	
Amortization of prior service (benefit) cost	(0.7)	0.1
Recognized net actuarial (gain) loss	(0.2)	0.3

Net periodic benefit cost	$ 1.3	6.6

	Nine Months Ended September 30,	
	2006	2005
Service cost benefits earned during the period	$ 0.9	3.3
Interest cost on benefit obligation	10.8	14.7
Expected return on plan assets	(5.2)	(0.1)
Amortization of prior service (benefit) cost	(1.9)	0.2
Recognized net actuarial (gain) loss	(0.6)	0.3
Special retirement benefits	(0.3)	
Net periodic benefit cost	$ 3.7	18.4

On July 13, 2005, Phelps Dodge made a cash contribution of $250 million to certain U.S. pension plans.

Our pension expense in the 2006 third quarter was $2.3 million, compared with $8.6 million in the 2005 third quarter. The decrease of $6.3 million was primarily due to (i) an increase in the expected return on plan assets ($4.3 million) associated with the July 2005 contribution, (ii) a decrease in service costs ($1.5 million) resulting from updated actuarial assumptions and (iii) a decrease in interest costs ($1.1 million) resulting mostly from the sale of Columbian Chemicals; partially offset by higher amortization of actuarial losses ($0.9 million) resulting from a decrease in the expected future working lifetime of employees due to updated withdrawal assumptions.

Our pension expense for the nine months ended September 30, 2006, was $7.4 million, compared with $25.5 million in the corresponding 2005 period. The decrease of $18.1 million was primarily due to (i) an increase in the expected return on plan assets ($13.1 million) associated with the July 2005 contribution, (ii) a decrease in service costs ($4.4 million) resulting from updated actuarial assumptions and (iii) a decrease in interest costs ($3.3 million) resulting mostly from the sale of Columbian Chemicals; partially offset by higher amortization of actuarial losses ($2.8 million) resulting from a decrease in the expected future working lifetime of employees due to updated withdrawal assumptions.

In December 2005, Phelps Dodge established and funded two trusts, one dedicated to funding postretirement medical obligations and the other dedicated to funding postretirement life insurance obligations, for eligible U.S. retirees. These trusts were established in connection with certain employee benefit plans sponsored by Phelps Dodge and are intended to constitute Voluntary Employees Beneficiary Association (VEBA) trusts under section 501(c)(9) of the Internal Revenue Code. The trusts will help provide assurance to participants in these plans that Phelps Dodge will continue to have funds available to meet its obligations under the covered retiree medical and life insurance programs. However, the trusts will not reduce retiree contribution obligations that help fund these benefits and will not guarantee that retiree contribution obligations will not increase in the future. In December 2005, the Company contributed a total of $200 million to these trusts, consisting of $175 million for postretirement medical obligations and $25 million for postretirement life insurance obligations. At the end of the 2006 second quarter, each VEBA trust commenced making payments in support of the benefit obligations funded by the respective trust.

Our postretirement expense in the 2006 third quarter was $1.3 million, compared with $6.6 million in the 2005 third quarter. The decrease of $5.3 million was primarily due to (i) an increase in the expected return on plan assets ($1.7 million) associated with the December 2005 contribution, (ii) lower interest costs ($1.5 million) and service costs ($0.8 million) resulting from updated actuarial assumptions and the sale of Columbian Chemicals and HPC and (iii) amortization of prior service cost ($0.8 million) resulting from a plan amendment.

Our postretirement expense for the nine months ended September 30, 2006, was $3.7 million, compared with $18.4 million in the corresponding 2005 period. The decrease of $14.7 million was primarily due to (i) an increase in expected return on plan assets ($5.1 million) associated with the December 2005 contribution, (ii) lower interest costs ($3.9 million) and service costs ($2.4 million) resulting from updated actuarial assumptions and the sale of

Columbian Chemicals and HPC and (iii) amortization of prior service cost ($2.1 million) resulting from a plan amendment.

12. Debt and Other Financing

On April 1, 2005, the Company amended the agreement for its $1.1 billion revolving credit facility, extending its maturity to April 20, 2010, and slightly modifying its fee structure. The facility is to be used for general corporate purposes. The agreement requires the Company to maintain a minimum earnings before interest, taxes, depreciation and amortization (EBITDA as defined in the agreement) to interest ratio of 2.25 on a rolling four-quarter basis, and limits consolidated indebtedness to 55 percent of total consolidated capitalization. At September 30, 2006, there was a total of approximately $73 million of letters of credit issued under the revolver. Total availability under the revolving credit facility at September 30, 2006, amounted to approximately $1.0 billion, of which approximately $227 million could be used for additional letters of credit.

On September 30, 2005, the Company entered into a number of agreements in connection with obtaining debt-financing facilities in an overall amount of $450 million, subject to certain conditions, for the expansion of the Cerro Verde copper mine. At September 30, 2006, and December 31, 2005, our Cerro Verde copper mine, in which we own a 53.6 percent equity interest, had outstanding project-financed debt under these facilities of $112.0 million and $20.0 million, respectively. (Refer to Note 14, Debt and Other Financing, to the Company s Consolidated Financial Statements included in the Company s Form 10-K for the year ended December 31, 2005, for additional information on the Cerro Verde debt-financing facilities.)

On April 17, 2006, the National Supervisory Commission of Companies and Securities of the Republic of Peru authorized the registration of a series of bonds to be issued through one or more offerings by Cerro Verde in an aggregate principal amount of up to $250 million, with the issuance of the first series of bonds in the aggregate principal amount of up to $90 million. On April 27, 2006, the first series of bonds was issued for total proceeds of $90.0 million, which was used to fund the Cerro Verde expansion project. The issuance of these bonds reduced, dollar-for-dollar, the $90 million stand-by facility included in the $450 million debt-financing facilities. Any further issuance of bonds would require the consent of the Senior Facility Lenders in accordance with the Master Participation Agreement.

In September 2006, Cerro Verde notified the Senior Facility Lenders that it would reduce loan commitments by $138 million so that total borrowings would not exceed $312 million, including the $90.0 million of local bonds issued in April 2006 and $112.0 million of outstanding project-financed debt at September 30, 2006. The reduction in loan commitments became effective on October 11, 2006.

In July 2005, the Company completed a tender offer for its 8.75 percent Notes due in 2011, which resulted in the retirement of long-term debt with a book value of approximately $280 million (representing approximately 72 percent of the outstanding notes). This resulted in a 2005 third quarter pre-tax charge of $54.0 million ($41.3 million after-tax), including purchase premiums, for early debt extinguishment costs.

13. Gain on Sale of Cost-Basis Investment

On June 9, 2005, the Company entered into an Underwriting Agreement with Citigroup Global Markets, Inc., UBS Securities LLC, SPCC Cerro Trading Company, Inc. and SPC Investors, LLC. On June 15, 2005, pursuant to the Underwriting Agreement, the Company sold all of its SPCC common shares to the underwriters for a net price of $40.635 per share (based on a market price of $42.00 per share less underwriting fees). This transaction resulted in a 2005 second quarter pre-tax gain of $438.4 million ($388.0 million after-tax).

14. Change in Interest Gain

In the 2005 second quarter, our Cerro Verde copper mine in Peru completed a general capital increase transaction. The transaction resulted in SMM Cerro Verde Netherlands B.V. acquiring an equity position in Cerro Verde totaling 21.0 percent. In addition, Compañía de Minas Buenaventura S.A.A. (Buenaventura) increased its ownership position in Cerro Verde to 18.2 percent. The remaining minority shareholders own 7.2 percent of Cerro Verde through shares publicly traded on the Lima Stock Exchange. As a result of the transaction, Phelps Dodge s interest in Cerro Verde was reduced to 53.6 percent from 82.5 percent.

In connection with the transaction, Cerro Verde issued 122.7 million of its common shares at $3.6074 per share to SMM Cerro Verde Netherlands B.V., Buenaventura and the remaining minority shareholders, and received $441.8 million in cash (net of $1.0 million of expenses). The stock issuance transactions resulted in a 2005 second quarter pre-tax gain of $159.5 million ($172.9 million after-tax) associated with our change of interest. The $13.4 million tax benefit related to this transaction included a reduction in deferred tax liabilities ($16.1 million) resulting from the recognition of certain book adjustments to reflect dilution of our ownership interest, partially offset by taxes charged ($2.7 million) on the transfer of stock subscription rights to Buenaventura and SMM Cerro Verde Netherlands B.V. The inflow of capital from Buenaventura and SMM Cerro Verde Netherlands B.V. is being used to partially finance the approximate $850 million expansion to mine a primary sulfide ore body beneath the leachable ore body currently in production at Cerro Verde.

15. Shareholders Equity

Stock Split

On February 1, 2006, the Company s board of directors approved a two-for-one split of the Company s outstanding common stock in the form of a 100 percent stock dividend. Common shareholders of record at the close of business on February 17, 2006, received one additional share of common stock for every share they owned as of that date. The additional shares were distributed on March 10, 2006, and increased the number of shares outstanding to approximately 203.7 million from approximately 101.9 million. The par value of Phelps Dodge s common stock remains at $6.25 per share. All references to shares of common stock and per common share amounts for the quarter and nine months ended September 30, 2005, have been retroactively adjusted to reflect the two-for-one stock split, except for the Consolidated Statement of Shareholders Equity that reflects the stock split by reclassifying from Capital in Excess of Par Value to Common Shares an amount equal to the par

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value of the additional shares issued to effect the stock split. The Company s common stock began trading at its post-split price at the beginning of trading on March 13, 2006.

16. Inco Termination Fee

On June 25, 2006, Phelps Dodge, Inco Ltd. (Inco) and Falconbridge Ltd. (Falconbridge) entered into a Combination Agreement (the Agreement). On July 28, 2006, as the minimum tender condition of 50.01 percent of Falconbridge common shares had not been satisfied, Inco elected to terminate its offer for Falconbridge, and on September 5, 2006, Phelps Dodge and Inco agreed to terminate the Agreement.

In connection with terminating the Agreement, Phelps Dodge received a gross termination fee of $125 million in cash ($82.3 million net of expenses). This transaction resulted in a 2006 third quarter net gain of $82.3 million ($62.5 million after-tax), which is included as miscellaneous income and expense, net, in the Consolidated Statement of Income. Inco has agreed to pay an additional $350 million if it consummates a change-of-control transaction on or prior to September 7, 2007.

REVIEW BY INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

The financial information as of September 30, 2006, and for the three-month and nine-month periods ended September 30, 2006 and 2005, included in Part I pursuant to Rule 10-01 of Regulation S-X has been reviewed by PricewaterhouseCoopers LLP (PricewaterhouseCoopers), the Company s independent registered public accounting firm, in accordance with the standards of the Public Company Accounting Oversight Board (United States). PricewaterhouseCoopers report is included below.

PricewaterhouseCoopers does not carry out any significant or additional procedures beyond those that would have been necessary if its report had not been included in this quarterly report. Accordingly, such report is not a report or part of a registration statement within the meaning of Sections 7 and 11 of the Securities Act of 1933 and the liability provisions of Section 11 of such Act do not apply.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of Phelps Dodge Corporation:

We have reviewed the accompanying consolidated balance sheet of Phelps Dodge Corporation and its subsidiaries as of September 30, 2006, and the related consolidated statement of income for each of the three-month and nine-month periods ended September 30, 2006 and 2005, the consolidated statement of cash flows for the nine-month periods ended September 30, 2006 and 2005, and the consolidated statement of shareholders equity for the nine-month period ended September 30, 2006. This interim financial information is the responsibility of the Company s management.

We conducted our review in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our review, we are not aware of any material modifications that should be made to the accompanying consolidated interim financial information for it to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2005, and the related consolidated statements of income, of cash flows, and of shareholders equity for the year then ended, management s assessment of the effectiveness of the Company s internal control over financial reporting as of December 31, 2005, and the effectiveness of the Company s internal control over financial reporting as of December 31, 2005; and in our report dated February 24, 2006, we expressed unqualified opinions thereon. The consolidated financial statements and management s assessment of the effectiveness of internal control over financial reporting referred to above are not presented herein. In our opinion, the information set forth in the accompanying consolidated balance sheet information as of December 31, 2005, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP
Phoenix, Arizona
October 23, 2006

ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The U.S. securities laws provide a safe harbor for certain forward-looking statements. This quarterly report contains forward-looking statements that express expectations of future events or results. All statements based on future expectations rather than historical facts are forward-looking statements that involve a number of risks and uncertainties, and Phelps Dodge Corporation (the Company, which may be referred to as Phelps Dodge, PD, we, us or our) cannot give assurance that such statements will prove to be correct.

Factors that could cause actual results to differ materially include, among other risks: risks and uncertainties relating to general U.S. and international economic and political conditions; the cyclical and volatile price of copper, molybdenum and other commodities; volatility in our financial performance caused by our copper price protection programs; volatility in energy prices, including the price of electricity, diesel fuel and natural gas; pressure on our copper production costs; the cost of environmental and regulatory compliance; the cost of mine closure regulations, including the ability to obtain surety bonds or other financial assurance for reclamation obligations; uncertainty relating to levels of ore reserves and mill and leach stockpiles; the ability to replenish our copper and molybdenum ore reserves; political and economic risks associated with foreign operations; and operational risks, including: unanticipated ground and water conditions and adverse claims to water rights; geological problems; metallurgical and other processing problems; the occurrence of unusual weather or operating conditions and other force majeure events; lower than expected ore grades and recovery rates; accidents; delays in the receipt of or failure to receive necessary government permits; the results of appeals of agency decisions or other litigation; uncertainty of exploration and development; delays in transportation; labor disputes; inability to obtain satisfactory insurance coverage; unavailability of materials and equipment; the failure of equipment or processes to operate in accordance with specifications or expectations; unanticipated difficulties consolidating acquired operations and obtaining expected synergies; and the results of financing efforts and financial market conditions. Refer to Item 1A, Risk Factors, Management s Discussion and Analysis of Financial Condition and Results of Operations and to Quantitative and Qualitative Disclosures About Market Risk in the Company s report on Form 10-K for the year ended December 31, 2005, for a further discussion of such risks and uncertainties, our operations, and our critical accounting policies.

Refer to Note 1, General Information, to our unaudited September 30, 2006, Consolidated Financial Information for a discussion of our consolidation policy.

RESULTS OF OPERATIONS

Consolidated Financial Results

As discussed in Note 3, Divestitures, to our unaudited September 30, 2006, Consolidated Financial Information, on November 15, 2005, the Company entered into an agreement to sell Columbian Chemicals Company and its subsidiaries (Columbian Chemicals or Columbian). The transaction was completed on March 16, 2006. As a result of this transaction, the operating results of Columbian have been reported separately from continuing operations and shown as discontinued operations in the Consolidated Statement of Income for all periods presented. Note that the results of discontinued operations are not necessarily indicative of the results of Columbian on a stand-alone basis. Except as otherwise indicated, all discussions and presentations of financial results are based on results from continuing operations.

All per share amounts for the quarter and nine months ended September 30, 2005, have been adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15, Shareholders Equity, to our unaudited September 30, 2006, Consolidated Financial Information for further discussion.)

All references to earnings or losses per common share are based on diluted earnings or losses per common share.
(Unaudited; $ in millions except per share amounts)

	Third Quarter	
	2006	2005
Sales and other operating revenues	$ 3,458.3	2,179.0

Operating income	$ 1,334.0	560.3
Minority interests in consolidated subsidiaries	$ (206.0)	(51.6)
Income from continuing operations	$ 889.1	360.1
Income (loss) from discontinued operations	$ (1.1)	6.0
Net income	$ 888.0	366.1
Basic earnings per common share:*		
Income from continuing operations	$ 4.39	1.83
Income from discontinued operations	(0.01)	0.03
Basic earnings per common share	$ 4.38	1.86
Diluted earnings per common share:*		
Income from continuing operations	$ 4.37	1.78
Income from discontinued operations	(0.01)	0.03
Diluted earnings per common share	$ 4.36	1.81

* Earnings per common share for the 2005 third quarter have been adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15, Shareholders Equity, to our unaudited September 30, 2006, Consolidated Financial Information for further discussion.)

The Company had consolidated net income for the 2006 third quarter of $888.0 million, or $4.36 per common share, including an after-tax charge of $110.5 million, or 54 cents per common share, for mark-to-market accounting adjustments on our 2006 and 2007 copper collars and copper put options. Also included in 2006 third quarter consolidated net income were special, net gains of $34.8 million, or 17 cents per common share, after taxes. In the 2005 third quarter, consolidated net income was $366.1 million, or $1.81 per common share, including special, net losses from continuing operations of $75.8 million, or 37 cents per common share, after taxes. Included in 2005 third quarter consolidated net income was

income from discontinued operations of $6.0 million, or 3 cents per common share.

The $529.0 million increase in income from continuing operations in the 2006 third quarter, compared with the 2005 third quarter primarily was due to (i) the effects of higher average copper prices (approximately $1.1 billion), (ii) the net gain recognized from the Inco termination fee ($82.3 million) and (iii) the absence of 2005 third quarter early debt extinguishment costs ($54.0 million). These were partially offset by (i) a higher tax provision ($271.0 million) primarily due to higher international earnings, (ii) higher minority interests in consolidated subsidiaries ($154.4 million) mostly resulting from increased earnings at our South American mining operations and the reduction of our ownership interest in Ojos del Salado, (iii) higher copper production costs (approximately $142 million), (iv) the negative impact of higher net copper pricing adjustments for our copper collars and copper put options (approximately $70 million) and (v) lower molybdenum by-product revenues (approximately $65 million).

(Unaudited; $ in millions except per share amounts)

	Nine Months Ended September 30,	
	2006	2005
Sales and other operating revenues	$ 8,675.1	6,031.5
Operating income	$ 2,871.5	1,260.9
Minority interests in consolidated subsidiaries	$ (525.3)	(116.5)
Income from continuing operations	$ 1,711.2	1,412.6
Income (loss) from discontinued operations	$ (17.7)	22.5
Net income	$ 1,693.5	1,435.1
Basic earnings per common share:*		
Income from continuing operations	$ 8.46	7.26
Income (loss) from discontinued operations	(0.09)	0.11
Basic earnings per common share	$ 8.37	7.37
Diluted earnings per common share:*		
Income from continuing operations	$ 8.42	6.99
Income (loss) from discontinued operations	(0.09)	0.11
Diluted earnings per common share	$ 8.33	7.10

* Earnings per common share for the nine months ended September 30, 2005, have been adjusted to reflect the March 10, 2006, stock split.

(Refer to Note 15, Shareholders Equity, to our unaudited September 30, 2006, Consolidated Financial Information for further discussion.)

The Company had consolidated net income for the nine months ended September 30, 2006, of $1.7 billion, or $8.33 per common share, including an after-tax charge of $923.5 million, or $4.54 per common share, for mark-to-market accounting adjustments on our 2006 and 2007 copper collars and copper put options. Also included in consolidated net income for the first nine months of 2006 were (i) special, net gains from continuing operations of $10.4 million, or 5 cents per common share, after taxes (consisting of a special gain of $62.5 million to miscellaneous income and expense, net; partially offset by special, net charges to operating income of $52.1 million) and (ii) a loss from discontinued operations of $17.7 million, or 9 cents per common share, including special, net charges of $30.3 million, or 15 cents per common share, after taxes. For the nine months ended September 30, 2005, consolidated net income was $1.4 billion, or $7.10 per common share, including special, net gains from continuing operations of $150.1 million, or 74 cents per common share, after taxes. Also included in consolidated net income for the first nine months of 2005 was income from discontinued operations of $22.5 million, or 11 cents per common share.

The $298.6 million increase in income from continuing operations for the nine months ended September 30, 2006, compared with the corresponding 2005 period primarily was due to the effects of (i) higher average copper prices (approximately $2.7 billion) and other net pricing adjustments (approximately $61 million) primarily for provisionally priced copper contracts at September 30, 2006, (ii) the absence of 2005 second quarter asset impairment charges recorded at PDMC ($419.1 million), (iii) the net gain recognized from the Inco termination fee ($82.3 million) and (iv) the absence of 2005 third quarter early debt extinguishment costs ($54.0 million). These were partially offset by (i) the negative impact of higher net copper pricing adjustments for our copper collars and copper put options (approximately $ 1.1 billion), (ii) a higher tax provision ($523.4 million) primarily due to higher international earnings, (iii) the absence of the 2005 gain recognized on the sale of our Southern Peru Copper Corporation (SPCC) investment ($438.4 million), (iv) higher minority interests in consolidated subsidiaries ($408.8 million) mostly resulting from increased earnings at our South American mining operations and the reduction of our ownership interests in Cerro Verde and Ojos del Salado, (v) higher copper production costs (approximately $295 million), (vi) the absence of the 2005 second quarter change in interest gain associated with the Cerro Verde stock issuance ($159.5 million) and (vii) lower molybdenum by-product revenues (approximately $160 million).

Special Items, Net of Taxes (Includes Special Items and Provisions, Net, in Operating Income and Other Non-Operating Significant Items Affecting Comparability of Results)

Throughout Management s Discussion and Analysis of Financial Condition and Results of Operations there is disclosure and discussion of what management believes to be special items. Special items include those operating and non-operating items that management believes should be separately disclosed to assist in the understanding of the financial performance of the Company and the comparability of its results. Such special items and provisions are primarily unpredictable and atypical of the Company s operations in a given period. In certain instances, certain transactions such as restructuring costs, asset impairment charges, certain asset disposals, certain legal matters, early debt extinguishment costs or certain tax items are reflected as special items or other non-operating significant items as they are not considered to be representative of the normal course of business. Additionally, environmental provisions and recoveries are included due to their nature and the impact of these amounts on comparison between periods. We believe consistent identification, disclosure and discussion of such items, both favorable and unfavorable, provide additional information to assess the quality of our performance and our earnings or losses. In addition, management

measures the performance of its reportable segments excluding special items. This supplemental information is not a substitute for any U.S. generally accepted accounting principles (GAAP) measure and should be evaluated within the context of our U.S. GAAP results. The tax impacts of the special items were determined at the marginal effective tax rate of the appropriate taxing jurisdictions, including provision for valuation allowance, if warranted.

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Any supplemental information references to earnings, losses or results excluding special items or before special items is a non-GAAP measure that may not be comparable to similarly titled measures reported by other companies.

Note: Supplemental Data

The following table summarizes consolidated net income, special items, and the resultant net income excluding these special items, net of taxes for the quarters and nine months ended September 30, 2006 and 2005:

(Unaudited; $ in millions)

	Third Quarter		Nine Months Ended September 30,	
	2006	2005	2006	2005
Net income	$ 888.0	366.1	1,693.5	1,435.1
Special items, net of taxes	34.8	(75.8)	(19.9)	150.1
Net income excluding special items (after taxes)	$ 853.2	441.9	1,713.4	1,285.0

Note: Supplemental Data

The following tables summarize the special items for the quarters and nine months ended September 30, 2006 and 2005 (refer to Note 4, Special Items and Provisions, Net, to our unaudited September 30, 2006, Consolidated Financial Information, for further discussion of special items and provisions, net, included in operating income):

(Unaudited; $ in millions except per share amounts)

	2006 Third Quarter			Nine Months Ended September 30, 2006		
Consolidated Statement of Income Line Item	Pre-tax	After-tax	$/Share After-tax	Pre-tax	After-tax	$/Share After-tax
Special items and provisions, net (included in operating income):						
PDMC (see Business Segment disclosure)	$ (3.0)	(2.2)	(0.01)	(22.9)	(17.4)	(0.08)
PDI (see Business Segment disclosure)	(7.1)	(7.0)	(0.04)	(15.8)	(16.6)	(0.09)
Corporate and Other						
Environmental provisions, net	(19.5)	(14.8)	(0.07)	(21.6)	(16.4)	(0.08)
Environmental insurance recoveries, net	0.1	0.1		0.2	0.2	
Asset impairment charges	(2.8)	(2.1)	(0.01)	(2.8)	(2.1)	(0.01)
Historical legal matters	(0.2)	(0.2)		(0.2)	(0.2)	
Sale of non-core real estate				0.5	0.4	
	(22.4)	(17.0)	(0.08)	(23.9)	(18.1)	(0.09)
Special items and provisions, net (included in operating income)	(32.5)	(26.2)	(0.13)	(62.6)	(52.1)	(0.26)

Other non-operating significant items affecting comparability of results:						
Miscellaneous income and expense, net (A):						
Inco termination fee, net of expenses	82.3	62.5	0.31	82.3	62.5	0.31
Discontinued operations (B):						
Loss on disposal of Columbian Chemicals	(0.6)	(1.9)	(0.01)	(15.4)	(16.0)	(0.08)
Transaction and employee-related costs	0.4	0.4		(14.3)	(14.3)	(0.07)
	(0.2)	(1.5)	(0.01)	(29.7)	(30.3)	(0.15)
	$ 49.6	34.8	0.17	(10.0)	(19.9)	(0.10)

(A) Miscellaneous income and expense, net, of $136.3 million and $196.9 million, as reflected in the Consolidated Statement of Income for the quarter and nine months ended September 30, 2006, respectively, included other amounts that have not been separately disclosed as special items, as these amounts are typical and representative of the normal course of the Company s business in a given period.

(B) Loss from discontinued operations of $1.1 million and $17.7 million,

as reflected in the Consolidated Statement of Income for the quarter and nine months ended September 30, 2006, respectively, included the operating results of Columbian Chemicals of $0.4 million and $12.6 million, respectively, which have not been separately disclosed as special items. Refer to Note 3, Divestitures, to our unaudited September 30, 2006, Consolidated Financial Information for further discussion of special items recorded in discontinued operations for the nine months ended September 30, 2006.

Inco termination fee. On September 5, 2006, Phelps Dodge and Inco Ltd. (Inco) agreed to terminate the Combination Agreement (the Agreement) entered into on June 25, 2006. In connection with terminating the Agreement, Phelps Dodge received a gross termination fee of $125 million in cash ($82.3 million net of expenses). This transaction resulted in a 2006 third quarter net gain of $82.3 million ($62.5 million after-tax).

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(Unaudited; $ in millions except per share amounts)

	2005 Third Quarter			Nine Months Ended September 30, 2005		
Consolidated Statement of Income Line Item	Pre-tax	After-tax	$/Share After-tax*	Pre-tax	After-tax	$/Share After-tax*
Special items and provisions, net (included in operating income):						
PDMC (see Business Segment disclosure)	$ (8.5)	(6.5)	(0.03)	(429.4)	(328.8)	(1.63)
PDI (see Business Segment disclosure)	(1.8)	(1.4)	(0.01)	(3.3)	(2.0)	(0.01)
Corporate and Other						
Environmental provisions, net	(34.4)	(26.3)	(0.13)	(54.1)	(41.3)	(0.21)
Environmental insurance recoveries, net	0.1			1.2	0.9	0.01
Historical legal matters	(0.4)	(0.3)		4.3	4.1	0.02
	(34.7)	(26.6)	(0.13)	(48.6)	(36.3)	(0.18)
Special items and provisions, net (included in operating income)	(45.0)	(34.5)	(0.17)	(481.3)	(367.1)	(1.82)
Other non-operating significant items affecting comparability of results:						
Early debt extinguishment costs	(54.0)	(41.3)	(0.20)	(54.0)	(41.3)	(0.21)
Gain on sale of cost-basis investment				438.4	388.0	1.92
Change in interest gain				159.5	172.9	0.86
Provision for taxes on income (A):						
Foreign dividend taxes					(2.4)	(0.01)
	$ (99.0)	(75.8)	(0.37)	62.6	150.1	0.74

* After-tax per common share amounts have been adjusted to reflect the March 10, 2006, stock split. (Refer to Note 15,

Shareholders Equity, to our unaudited September 30, 2006, Consolidated Financial Information for further discussion.)

(A) Provision for taxes on income of $300.4 million, as reflected in the Consolidated Statement of Income for the nine months ended September 30, 2005, included other amounts that have not been separately disclosed as special items, as these amounts are typical and representative of the normal course of the Company s business in a given period.

Early debt extinguishment costs. In July 2005, the Company completed a tender offer for its 8.75 percent Notes due in 2011, which resulted in the retirement of long-term debt with a book value of approximately $280 million (representing approximately 72 percent of the outstanding notes). This resulted in a 2005 third quarter pre-tax charge of $54.0 million ($41.3 million after-tax), including purchase premiums, for early debt extinguishment costs.

Gain on sale of cost-basis investment. In the 2005 second quarter, a pre-tax gain of $438.4 million ($388.0 million after-tax) was recognized from the sale of our common shares of SPCC. On June 9, 2005, the Company entered into an Underwriting Agreement with Citigroup Global Markets, Inc., UBS Securities LLC, SPCC, Cerro Trading Company, Inc. and SPC Investors, LLC. On June 15, 2005, pursuant to the Underwriting Agreement, the Company sold all of its SPCC common shares to the underwriters for a net purchase price of $40.635 per share (based on a market purchase price of $42.00 per share less underwriting fees).

Change in interest gain. In the 2005 second quarter, our Cerro Verde copper mine in Peru completed a general capital increase transaction. The transaction resulted in SMM Cerro Verde Netherlands B.V. acquiring an equity position in Cerro Verde totaling 21.0 percent. In addition, Compañía de Minas Buenaventura S.A.A. (Buenaventura) increased its ownership position in Cerro Verde to 18.2 percent. The remaining minority shareholders own 7.2 percent

of Cerro Verde through shares publicly traded on the Lima Stock Exchange. As a result of the transaction, Phelps Dodge s interest in Cerro Verde was reduced to 53.6 percent from 82.5 percent.

In connection with the transaction, Cerro Verde issued 122.7 million of its common shares at $3.6074 per share to SMM Cerro Verde Netherlands B.V., Buenaventura and the remaining minority shareholders, and received $441.8 million in cash (net of $1.0 million of expenses). This stock issuance transaction resulted in a pre-tax gain of $159.5 million ($172.9 million after-tax) associated with our change of interest. The $13.4 million tax benefit related to this transaction included a reduction in deferred tax liabilities ($16.1 million) resulting from the recognition of certain book adjustments to reflect the dilution of our ownership interest, partially offset by taxes charged ($2.7 million) on the transfer of stock subscription rights to Buenaventura and SMM Cerro Verde Netherlands B.V. The inflow of capital from Buenaventura and SMM Cerro Verde Netherlands B.V. is being used as partial financing for an approximate $850 million expansion project to mine a primary sulfide ore body beneath the leachable ore body currently in production.

Provision for taxes on income. For the nine months ended September 30, 2005, tax expense of $2.4 million was recognized for U.S. taxes incurred with respect to dividends received from Cerro Verde in 2005.

Business Divisions

Results for 2006 and 2005 can be meaningfully compared by separate reference to our business divisions, Phelps Dodge Mining Company (PDMC) and Phelps Dodge Industries (PDI).

On November 15, 2005, the Company entered into an agreement to sell Columbian Chemicals to a company owned jointly by One Equity Partners LLC, a private equity affiliate of JPMorgan Chase & Co., and South Korea-based DC Chemical Co., Ltd. The transaction was completed on March 16, 2006. As a result of this transaction, the operating results of Columbian, which were previously reported as a

segment of PDI, have been reported separately from continuing operations and shown as discontinued operations in the Consolidated Statement of Income for all periods presented.

In addition, on November 15, 2005, the Company entered into an agreement to sell substantially all of its North American magnet wire assets, previously reported as part of the Wire and Cable segment in the PDI division, to Rea Magnet Wire Company, Inc. (Rea). This transaction was completed on February 10, 2006. On March 4, 2006, Phelps Dodge entered into an agreement to sell High Performance Conductors of SC & GA, Inc. (HPC), previously reported as part of the Wire and Cable segment in the PDI division, to International Wire Group, Inc. (IWG). This transaction was completed on March 31, 2006.

(Refer to Note 3, Divestitures, to our unaudited September 30, 2006, Consolidated Financial Information, for further discussion of these transactions.)

Significant events and transactions have occurred within the reportable segments of each business division that, as indicated in the separate discussions presented below, are material to an understanding of the particular period s results and to a comparison with results of the other periods.

RESULTS OF PHELPS DODGE MINING COMPANY

PDMC is our international business division comprising our vertically integrated copper operations from mining through rod production, molybdenum operations from mining through conversion to chemical and metallurgical products, marketing and sales; and worldwide mineral exploration, technology and project development programs. PDMC includes 11 reportable segments and other mining activities.

In the 2005 fourth quarter, the Company reassessed its reportable segments considering the increase in copper and molybdenum prices. Based upon our assessment, we are no longer separately disclosing Miami/Bisbee as an individual reportable segment, but rather have included it in PDMC Other. In accordance with Statement of Financial Accounting Standards (SFAS) No. 131, Disclosures about Segments of an Enterprise and Related Information, segment information for 2005 has been revised to conform to the 2006 presentation.

PDMC has five reportable copper production segments in the United States (Morenci, Bagdad, Sierrita, Chino/Cobre and Tyrone) and three reportable copper production segments in South America (Candelaria/Ojos del Salado, Cerro Verde and El Abra). These segments include open-pit mining, underground mining, sulfide ore concentrating, leaching, solution extraction and electrowinning. In addition, the Candelaria/Ojos del Salado, Morenci, Bagdad, Sierrita and Chino/Cobre segments also produce gold and silver, and the Bagdad, Sierrita and Chino mines produce molybdenum and rhenium as by-products.

The Manufacturing segment consists of conversion facilities, including our smelter, refinery, rod mills and specialty copper products facility. The Manufacturing segment processes copper produced at our mining operations and copper purchased from others into copper anode, cathode, rod and custom copper shapes. In addition, at times it smelts and refines copper and produces copper rod and shapes for customers on a toll basis. Toll arrangements require the tolling customer to deliver appropriate copper-bearing material to our facilities, which we then process into a product that is returned to the customer. The customer pays PDMC for processing its material into the specified products.

The Sales segment functions as an agent to sell copper from our U.S. mines and Manufacturing segment. The Sales segment also purchases and sells any copper not sold by the South American Mines to third parties. Copper is sold to others primarily as rod, cathode or concentrate. Copper rod historically was sold to the HPC and Magnet Wire North American operations of PDI s Wire and Cable segment. Since the disposition of these businesses, we have continued to sell them copper rod and certain copper alloys.

The Primary Molybdenum segment consists of the Henderson and Climax mines, related conversion facilities and a technology center. This segment is an integrated producer of molybdenum, with mining, roasting and processing facilities that produce high-purity, molybdenum-based chemicals, molybdenum metal powder and metallurgical products, which are sold to customers around the world. In addition, at times this segment roasts and/or processes material on a toll basis. Toll arrangements require the tolling customer to deliver appropriate molybdenum-bearing material to our facilities, which we then process into a product that is returned to the customer. The customer pays

PDMC for processing its material into the specified products. This segment also includes a technology center whose primary activity is developing, marketing and selling new engineered products and applications.

PDMC Other includes our worldwide mineral exploration and development programs, a process technology center whose primary activities are improving existing processes and developing new cost-competitive technologies, other ancillary operations, including our Miami/Bisbee operations, and eliminations within PDMC.

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Major operating and financial results of PDMC for the quarters and nine months ended September 30, 2006 and 2005, are summarized in the following tables:
(Unaudited; $ in millions except per pound amounts)

	Third Quarter	
	2006	2005
Sales and other operating revenues to unaffiliated customers	$ 3,143.0	1,859.7
Operating income	$ 1,376.0	618.4
Operating income before special items and provisions, net	$ 1,379.0	626.9
Minority interests in consolidated subsidiaries (A)	$ (203.5)	(49.8)
Copper production (thousand short tons):		
Total copper production	317.4	319.5
Less undivided interest (B)	15.6	15.3
Copper production on a consolidated basis	301.8	304.2
Less minority participants shares (A)	53.0	48.0
Copper production on a pro rata basis	248.8	256.2
Copper sales (thousand short tons):		
Total copper sales from own mines	314.1	318.7
Less undivided interest (B)	15.3	15.3
Copper sales from own mines on a consolidated basis	298.8	303.4
Less minority participants shares (A)	55.6	48.3
Copper sales from own mines on a pro rata basis	243.2	255.1
Purchased copper	97.6	123.8
Total copper sales on a consolidated basis	396.4	427.2
LME average spot copper price per pound cathodes	$ 3.479	1.704
COMEX average spot copper price per pound cathodes	$ 3.539	1.701
Molybdenum production (million pounds)	16.5	16.4
Molybdenum sales (million pounds):		
Net Phelps Dodge share from own mines	16.6	14.8
Purchased molybdenum	2.3	2.9
Total molybdenum sales	18.9	17.7

Metals Week:		
Molybdenum Dealer Oxide mean price per pound	$ 26.22	30.74
M-1 price per pound		