

MARTIN MARIETTA MATERIALS INC

Form 10-Q

August 01, 2006

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

(Mark One)

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

For the quarterly period ended June 30, 2006

OR

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

For the transition period from

to

Commission File Number 1-12744

MARTIN MARIETTA MATERIALS, INC.

(Exact name of registrant as specified in its charter)

North Carolina

56-1848578

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification Number)

2710 Wycliff Road, Raleigh, NC

27607-3033

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code 919-781-4550

Former name: None

Former name, former address and former fiscal year, if changes 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  No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

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

Yes  No

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

Class

Outstanding as of July 28, 2006

Common Stock, \$0.01 par value

45,333,799



MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
FORM 10-Q  
For the Quarter Ended June 30, 2006

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## MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES

## Item 1. Financial Statements

## MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

|   | June 30,<br>2006<br><i>(Unaudited)</i>               | December<br>31,<br>2005<br><i>(Audited)</i> | June 30,<br>2005<br><i>(Unaudited)</i> |
|---|--|---|--|
|   | <i>(Dollars in Thousands, Except Per Share Data)</i> |   |  |
| <b>ASSETS</b>   |  |   |  |
| Current Assets:   |  |   |  |
| Cash and cash equivalents                                 | \$ 20,386  | \$ 76,745                                   | \$ 81,410                              |
| Investments   |  | 25,000                                      | 10,000                                 |
| Accounts receivable, net                                  | 292,559  | 225,012                                     | 282,844                                |
| Inventories, net  | 243,714  | 222,728                                     | 217,003                                |
| Current portion of notes receivable                       | 2,494  | 5,081                                       | 3,844                                  |
| Current deferred income tax benefits                      | 16,906   | 14,989                                      | 6,112                                  |
| Other current assets                                      | 31,708   | 32,486                                      | 23,052                                 |
| <b>Total Current Assets</b>                               | <b>607,767</b>                                       | <b>602,041</b>                              | <b>624,265</b>                         |
| <br>  |  |   |  |
| Property, plant and equipment                             | 2,641,697  | 2,501,774                                   | 2,408,816                              |
| Allowances for depreciation and depletion                 | (1,385,697)  | (1,335,423)                                 | (1,285,309)                            |
| <b>Net property, plant and equipment</b>                  | <b>1,256,000</b>                                     | <b>1,166,351</b>                            | <b>1,123,507</b>                       |
| <br>  |  |   |  |
| Goodwill  | 570,336  | 569,263                                     | 569,294                                |
| Other intangibles, net                                    | 16,846   | 18,744                                      | 20,369                                 |
| Noncurrent notes receivable                               | 10,836   | 27,883                                      | 24,917                                 |
| Other noncurrent assets                                   | 40,231   | 49,034                                      | 43,915                                 |
| <br>  |  |   |  |
| <b>Total Assets</b>                                       | <b>\$ 2,502,016</b>                                  | <b>\$ 2,433,316</b>                         | <b>\$ 2,406,267</b>                    |
| <br>  |  |   |  |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b>                |  |   |  |
| Current Liabilities:                                      |  |   |  |
| Bank overdraft  | \$ 15,324  | \$ 7,290                                    | \$ 5,200                               |
| Accounts payable  | 99,526   | 93,445                                      | 103,566                                |
| Accrued salaries, benefits and payroll taxes              | 20,664   | 24,199                                      | 22,648                                 |
| Pension and postretirement benefits                       | 6,268  | 4,200                                       | 4,413                                  |
| Accrued insurance and other taxes                         | 43,442   | 39,582                                      | 43,351                                 |
| Income taxes  | 24,088   | 1,336                                       | 23,785                                 |
| Current maturities of long-term debt and commercial paper | 13,989   | 863   | 915                                    |
| Other current liabilities                                 | 27,275   | 29,207                                      | 25,578                                 |
| <b>Total Current Liabilities</b>                          | <b>250,576</b>                                       | <b>200,122</b>                              | <b>229,456</b>                         |

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|   |                     |                     |                     |
|---|---------------------|---------------------|---------------------|
| Long-term debt and commercial paper                 | 705,359             | 709,159             | 711,491             |
| Pension, postretirement and postemployment benefits | 97,056              | 98,714              | 87,924              |
| Noncurrent deferred income taxes                    | 143,678             | 149,972             | 138,469             |
| Other noncurrent liabilities                        | 86,062              | 101,664             | 100,447             |
| <b>Total Liabilities</b>                            | <b>1,282,731</b>    | <b>1,259,631</b>    | <b>1,267,787</b>    |
| Shareholders' Equity:                               |                     |                     |                     |
| Common stock, par value \$0.01 per share            | 453                 | 457                 | 462                 |
| Preferred stock, par value \$0.01 per share         |                     |                     |                     |
| Additional paid-in capital                          | 205,529             | 240,541             | 301,836             |
| Accumulated other comprehensive loss                | (15,325)            | (15,325)            | (8,970)             |
| Retained earnings                                   | 1,028,628           | 948,012             | 845,152             |
| <b>Total Shareholders' Equity</b>                   | <b>1,219,285</b>    | <b>1,173,685</b>    | <b>1,138,480</b>    |
| <b>Total Liabilities and Shareholders' Equity</b>   | <b>\$ 2,502,016</b> | <b>\$ 2,433,316</b> | <b>\$ 2,406,267</b> |

See accompanying condensed notes to consolidated financial statements.

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MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF EARNINGS

|   | Three Months Ended<br>June 30,               |                  | Six Months Ended<br>June 30, |                  |
|---|--|------------------|------------------------------|------------------|
|   | 2006   | 2005             | 2006                         | 2005             |
|   | <i>(In Thousands, Except Per Share Data)</i> |                  |                              |                  |
|   | <i>(Unaudited)</i>                           |                  |                              |                  |
| Net Sales   | \$ 518,271                                   | \$ 477,259       | \$ 942,682                   | \$ 815,476       |
| Freight and delivery revenues   | 70,370                                       | 66,582           | 129,923                      | 118,093          |
| <b>Total revenues</b>   | <b>588,641</b>                               | <b>543,841</b>   | <b>1,072,605</b>             | <b>933,569</b>   |
| <br>  |  |                  |                              |                  |
| Cost of sales   | 365,006                                      | 347,634          | 705,454                      | 636,182          |
| Freight and delivery costs  | 70,370                                       | 66,582           | 129,923                      | 118,093          |
| <b>Total cost of revenues</b>   | <b>435,376</b>                               | <b>414,216</b>   | <b>835,377</b>               | <b>754,275</b>   |
| <br>  |  |                  |                              |                  |
| <b>Gross Profit</b>   | <b>153,265</b>                               | <b>129,625</b>   | <b>237,228</b>               | <b>179,294</b>   |
| <br>  |  |                  |                              |                  |
| Selling, general & administrative expenses  | 37,148                                       | 31,801           | 73,309                       | 63,629           |
| Research and development  | 140  | 193              | 304                          | 341              |
| Other operating (income) and expenses, net  | (3,643)                                      | (2,225)          | (7,290)                      | (3,983)          |
| <b>Earnings from Operations</b>   | <b>119,620</b>                               | <b>99,856</b>    | <b>170,905</b>               | <b>119,307</b>   |
| <br>  |  |                  |                              |                  |
| Interest expense  | 9,708  | 10,662           | 19,684                       | 21,452           |
| Other nonoperating (income) and expenses, net   | (306)  | 964              | (2,400)                      | (1,271)          |
| <br>  |  |                  |                              |                  |
| <b>Earnings from continuing operations before income tax expense</b>  | <b>110,218</b>                               | <b>88,230</b>    | <b>153,621</b>               | <b>99,126</b>    |
| Income tax expense  | 34,234                                       | 25,449           | 47,976                       | 27,735           |
| <br>  |  |                  |                              |                  |
| <b>Earnings from continuing operations</b>  | <b>75,984</b>                                | <b>62,781</b>    | <b>105,645</b>               | <b>71,391</b>    |
| (Loss) Gain on discontinued operations, net of related tax expense (benefit) of \$46, \$(597), \$670 and \$(1,254) respectively | (194)  | (1,309)          | 1,151                        | (2,842)          |
| <br>  |  |                  |                              |                  |
| <b>Net Earnings</b>   | <b>\$ 75,790</b>                             | <b>\$ 61,472</b> | <b>\$ 106,796</b>            | <b>\$ 68,549</b> |
| <br>  |  |                  |                              |                  |
| <b>Net Earnings (Loss) Per Common Share:</b>  |  |                  |                              |                  |
| Basic from continuing operations  | \$ 1.66                                      | \$ 1.35          | \$ 2.31                      | \$ 1.52          |
| Discontinued operations   |  | (0.03)           | 0.03                         | (0.06)           |
|   | <b>\$ 1.66</b>                               | <b>\$ 1.32</b>   | <b>\$ 2.34</b>               | <b>\$ 1.46</b>   |

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|   |         |         |         |         |
|---|---------|---------|---------|---------|
| Diluted from continuing operations          | \$ 1.63 | \$ 1.33 | \$ 2.26 | \$ 1.50 |
| Discontinued operations                     |         | (0.03)  | 0.03    | (0.06)  |
|   | \$ 1.63 | \$ 1.30 | \$ 2.29 | \$ 1.44 |
| Cash Dividends Per Common Share             | \$ 0.23 | \$ 0.20 | \$ 0.46 | \$ 0.40 |
| Weighted Average Common Shares Outstanding: |         |         |         |         |
| Basic                                       | 45,663  | 46,569  | 45,706  | 46,814  |
| Diluted                                     | 46,623  | 47,174  | 46,704  | 47,454  |

See accompanying condensed notes to consolidated financial statements.

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MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS

|   | Six Months Ended<br>June 30,  |              |
|---|-------------------------------|--------------|
|   | 2006                          | 2005         |
|   | <i>(Dollars in Thousands)</i> |              |
|   | <i>(Unaudited)</i>            |              |
| Net earnings  | \$ 106,796                    | \$ 68,549    |
| Adjustments to reconcile net earnings to cash provided by operating activities:               |                               |              |
| Depreciation, depletion and amortization  | 66,622                        | 67,730       |
| Stock-based compensation expense  | 6,065                         | 1,527        |
| Gains on divestitures and sales of assets   | (5,142)                       | (483)        |
| Deferred income taxes   | (4,994)                       | (1,072)      |
| Excess tax benefits from stock-based compensation transactions                                | (9,375)                       | 2,713        |
| Other items, net  | (2,649)                       | (2,717)      |
| Changes in operating assets and liabilities, net of effects of acquisitions and divestitures: |                               |              |
| Accounts receivable, net  | (67,547)                      | (63,255)     |
| Inventories, net  | (21,065)                      | (5,517)      |
| Accounts payable  | 6,080                         | 13,741       |
| Other assets and liabilities, net   | 39,088                        | 27,434       |
| <br>Net cash provided by operating activities   | <br>113,879                   | <br>108,650  |
| <br>Investing activities:   |                               |              |
| Additions to property, plant and equipment  | (157,699)                     | (101,284)    |
| Acquisitions, net   | (2,939)                       | (4,138)      |
| Proceeds from divestitures and sales of assets  | 22,613                        | 20,922       |
| Purchases of investments  |                               | (10,000)     |
| Proceeds from sale of investments   | 25,000                        |              |
| Railcar construction advances   | (32,077)                      |              |
| Repayments of railcar construction advances   | 32,077                        |              |
| <br>Net cash used for investing activities  | <br>(113,025)                 | <br>(94,500) |
| <br>Financing activities:   |                               |              |
| Repayments of long-term debt  | (415)                         | (438)        |
| Borrowings on line of credit and commercial paper   | 13,539                        |              |
| Change in bank overdraft  | 8,034                         | (4,326)      |
| Payments on capital lease obligations   | (69)                          |              |
| Dividends paid  | (21,251)                      | (18,697)     |
| Repurchases of common stock   | (83,180)                      | (81,130)     |
| Issuances of common stock   | 16,754                        | 10,231       |
| Excess tax benefits from stock-based compensation transactions                                | 9,375                         |              |

|  |           |           |
|--|-----------|-----------|
| Net cash used for financing activities                                 | (57,213)  | (94,360)  |
| Net decrease in cash and cash equivalents                              | (56,359)  | (80,210)  |
| Cash and cash equivalents, beginning of period                         | 76,745    | 161,620   |
| Cash and cash equivalents, end of period                               | \$ 20,386 | \$ 81,410 |
| Supplemental disclosures of cash flow information:                     |           |           |
| Cash paid for interest   | \$ 23,596 | \$ 23,270 |
| Cash payments for income taxes   | \$ 12,233 | \$ 11,093 |
| See accompanying condensed notes to consolidated financial statements. |           |           |

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MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
 CONSOLIDATED STATEMENT OF SHAREHOLDERS EQUITY  
 (Unaudited)

| <i>(in thousands)</i>   | Shares<br>of<br>Common |                 | Common<br>Stock | Additional<br>Paid-in<br>Capital | Accumulated                    |                      | Total<br>Shareholders<br>Equity |
|---|------------------------|-----------------|-----------------|----------------------------------|--------------------------------|----------------------|---------------------------------|
|   | Common<br>Stock        | Common<br>Stock |                 |                                  | Other<br>Comprehensive<br>Loss | Retained<br>Earnings |                                 |
| Balance at December 31, 2005  | 45,727                 | \$ 457          | \$ 240,541      | \$ (15,325)                      | \$ 948,012                     | \$ 1,173,685         |                                 |
| Writeoff of capitalized stripping costs, net  |                        |                 |                 |                                  | (4,929)                        | (4,929)              |                                 |
| Reclassification of stock-based compensation liabilities to shareholders equity for FAS 123(R) adoption |                        |                 | 12,339          |                                  |                                | 12,339               |                                 |
| Net earnings  |                        |                 |                 |                                  | 106,796                        | 106,796              |                                 |
| Dividends declared  |                        |                 |                 |                                  | (21,251)                       | (21,251)             |                                 |
| Issuances of common stock for stock award plans   | 520                    | 5               | 29,755          |                                  |                                | 29,760               |                                 |
| Repurchases of common stock   | (914)                  | (9)             | (83,171)        |                                  |                                | (83,180)             |                                 |
| Stock-based compensation expense  |                        |                 | 6,065           |                                  |                                | 6,065                |                                 |
| Balance at June 30, 2006  | 45,333                 | \$ 453          | \$ 205,529      | \$ (15,325)                      | \$ 1,028,628                   | \$ 1,219,285         |                                 |

See accompanying condensed notes to consolidated financial statements.

MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
FORM 10-Q

For the Quarter Ended June 30, 2006

CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

**1. Significant Accounting Policies**

**Basis of Presentation**

The accompanying unaudited consolidated financial statements of Martin Marietta Materials, Inc. (the Corporation ) have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to the Quarterly Report on Form 10-Q and to Article 10 of Regulation S-X. The Corporation has continued to follow the accounting policies set forth in the audited consolidated financial statements and related notes thereto included in the Corporation s Annual Report on Form 10-K for the year ended December 31, 2005, filed with the Securities and Exchange Commission on February 27, 2006. In the opinion of management, the interim financial information provided herein reflects all adjustments, consisting of normal recurring accruals, necessary for a fair presentation of the results of operations for the interim periods. The results of operations for the six months ended June 30, 2006 are not indicative of the results to be expected for the full year.

**Reclassifications**

Certain 2005 amounts have been reclassified to conform to the 2006 presentation. The reclassifications had no impact on previously reported net earnings or financial position.

**Sales Taxes**

Sales taxes collected from customers are recorded as liabilities until remitted to taxing authorities and therefore are not reflected in the consolidated statements of earnings.

**Stripping Costs**

Effective January 1, 2006, the Corporation adopted Emerging Issues Task Force Issue 04-06, *Accounting for Stripping Costs in the Mining Industry* ( EITF 04-06 ). EITF 04-06 clarifies that post-production stripping costs, which represent costs of removing overburden and waste materials to access mineral deposits, should be considered costs of the extracted minerals under a full absorption costing system and recorded as a component of inventory to be recognized in costs of sales in the same period as the revenue from the sale of the inventory. Prior to the adoption of EITF 04-06, the Corporation capitalized certain post-production stripping costs and amortized these costs over the lesser of half of the life of the uncovered reserves or 5 years.

In connection with the adoption of EITF 04-06, the Corporation wrote off \$8,148,000 of capitalized post-production stripping costs previously reported as other noncurrent assets and a related deferred tax liability of \$3,219,000, thereby reducing retained earnings by \$4,929,000 at January 1, 2006.

MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
FORM 10-Q  
For the Quarter Ended June 30, 2006  
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Continued)

**1. Significant Accounting Policies (continued)**

**Stock-Based Compensation**

The Corporation has stock-based compensation plans for employees and directors as more fully described in Note 9. Effective January 1, 2006, the Corporation adopted Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* ( FAS 123(R) ) to account for these plans. FAS 123(R) requires all forms of share-based payments to employees, including stock options, to be recognized as compensation expense. The compensation expense is the fair value of the awards at the measurement date. Further, FAS 123(R) requires compensation cost to be recognized over the requisite service period for all awards granted subsequent to adoption. As required by FAS 123(R), the Corporation will continue to recognize compensation cost over the explicit vesting period for all unvested awards as of January 1, 2006, with acceleration for any remaining unrecognized compensation cost if an employee retires prior to the end of the vesting period.

The Corporation adopted the provisions of FAS 123(R) using the modified prospective transition method, which recognizes stock option awards as compensation expense for unvested awards as of January 1, 2006 and awards granted or modified subsequent to that date. In accordance with the modified prospective transition method, the Corporation's consolidated statements of earnings for the three and six months ended June 30, 2005 and its consolidated statement of cash flows for the six months ended June 30, 2005 have not been restated and do not include the impact of FAS 123(R).

Under FAS 123(R), an entity may elect either the accelerated expense recognition method or a straight-line recognition method for awards subject to graded vesting based on a service condition. The Corporation elected to use the accelerated expense recognition method for stock options issued to employees. The accelerated recognition method requires stock options that vest ratably to be divided into tranches. The expense for each tranche is allocated to its particular vesting period.

The adoption of FAS 123(R) did not change the Corporation's accounting for stock-based compensation related to restricted stock awards, incentive compensation awards and nonemployee directors' awards. The Corporation continues to expense the fair value of these awards based on the closing price of the Corporation's common stock on the awards' respective measurement dates.

MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
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 For the Quarter Ended June 30, 2006  
 CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 (Continued)

**1. Significant Accounting Policies (continued)**

**Stock-Based Compensation (continued)**

The adoption of FAS 123(R) resulted in the recognition of compensation expense for stock options granted by the Corporation. During the three months ended June 30, 2006, the Corporation recognized \$1,302,000 of compensation expense for the May 2006 grant of 168,393 stock options (141,393 to employees and 27,000 to directors). Of this amount, \$885,000 relates to directors' options that were expensed at the grant date as the options vested immediately. The remaining options are being expensed over their requisite service periods. With the current forfeiture rate assumptions, total stock-based compensation expense to be recognized for the May 2006 option grant is \$5,530,000. No stock options were granted during the quarter ended March 31, 2006.

The impact of expensing stock options granted in 2006 and the unvested portion of outstanding employee stock options at January 1, 2006 affected the Corporation's results of operations as follows:

|   | Three Months<br>Ended<br>June 30, 2006 | Six Months<br>Ended<br>June 30, 2006 |
|---|--|--------------------------------------|
| Decreased earnings from continuing operations before income tax expense by: | \$ 2,121,000                           | \$ 3,189,000                         |
| Decreased earnings from continuing operations and net earnings by:          | \$ 1,282,000                           | \$ 1,928,000                         |
| Decreased basic earnings per share by:                                      | \$ 0.03                                | \$ 0.04                              |
| Decreased diluted earnings per share by:                                    | \$ 0.03                                | \$ 0.04                              |

Furthermore, FAS 123(R) requires tax benefits attributable to stock-based compensation transactions to be classified as financing cash flows. Prior to the adoption of FAS 123(R), the Corporation presented excess tax benefits from stock-based compensation transaction as an operating cash flow on its consolidated statements of cash flows. The \$9,375,000 excess tax benefit classified as a financing cash flow for the six months ended June 30, 2006 would have been classified as an operating cash inflow had the Corporation not adopted FAS 123(R).

In connection with the adoption of FAS 123(R), the Corporation reclassified \$12,339,000 of stock-based compensation liabilities to additional paid-in-capital, thereby increasing shareholders' equity at January 1, 2006.

MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
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For the Quarter Ended June 30, 2006  
CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Continued)

**1. Significant Accounting Policies (continued)**

**Stock-Based Compensation (continued)**

Prior to January 1, 2006, the Corporation accounted for its stock-based compensation plans under the intrinsic value method prescribed by APB Opinion 25, *Accounting for Stock Issued to Employees*, and related Interpretations. As the Corporation granted stock options with an exercise price equal to the market value of the stock on the date of grant, no stock-based compensation cost for stock options granted was recognized in net earnings as reported in the consolidated statements of earnings prior to adopting FAS 123(R). The following table illustrates the effect on net earnings and earnings per share if the Corporation had applied the fair value recognition provisions of Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* ( FAS 123 ) (dollars in thousands, except per share amounts):

|   | Three Months<br>Ended<br>June 30, 2005 | Six Months<br>Ended<br>June 30, 2005 |
|---|--|--------------------------------------|
| Net earnings, as reported   | \$ 61,472                              | \$ 68,549                            |
| Add: Stock-based compensation expense included in reported net earnings, net of related tax effects             | 428                                    | 856                                  |
| Deduct: Stock-based compensation expense determined under fair value for all awards, net of related tax effects | (1,654)                                | (2,941)                              |
| Pro forma net earnings  | \$ 60,246                              | \$ 66,464                            |
| Earnings per share:   |  |                                      |
| Basic-as reported   | \$ 1.32                                | \$ 1.46                              |
| Basic-pro forma   | \$ 1.29                                | \$ 1.42                              |
| Diluted-as reported   | \$ 1.30                                | \$ 1.44                              |
| Diluted-pro forma   | \$ 1.28                                | \$ 1.40                              |

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CONDENSED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
(Continued)

**1. Significant Accounting Policies (continued)**

**Stock-Based Compensation (continued)**

The Corporation used a lattice valuation model to determine the fair value of stock option awards granted in 2006 and 2005 and the Black-Scholes valuation model for stock options granted prior to 2004. The lattice valuation model takes into account employees' exercise patterns based on changes in the Corporation's stock price and other variables and is considered to result in a more accurate valuation of employee stock options than the Black-Scholes valuation model. The period of time for which options are expected to be outstanding, or expected term of the option, is a derived output of the lattice valuation model. The Corporation considers the following factors when estimating the expected term of options: vesting period of the award, expected volatility of the underlying stock, employees' ages and external data. Other key assumptions used in determining the fair value of the stock options awarded in 2006 and 2005 were:

|                         |           |           |
|-------------------------|-----------|-----------|
|                         | 2006      | 2005      |
| Risk-free interest rate | 4.90%     | 3.80%     |
| Dividend yield          | 1.10%     | 1.60%     |
| Volatility factor       | 31.20%    | 30.80%    |
| Expected term           | 6.9 years | 6.3 years |

Based on these assumptions, the weighted-average fair value of each stock option granted was \$33.21 for 2006 and \$18.72 for 2005.

The risk-free interest rate reflects the interest rate on zero-coupon U.S. government bonds available at the time each option was granted having a remaining life approximately equal to the option's expected life. The dividend yield represents the dividend rate expected to be paid over the option's expected life and is based on the Corporation's history and targeted dividend pattern. The Corporation's volatility factor measures the amount by which its stock price is expected to fluctuate during the expected life of the option and is based on historical stock price changes and other factors. Additionally, FAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The Corporation estimated forfeitures and will ultimately recognize compensation cost only for those stock-based awards that vest.



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**1. Significant Accounting Policies (continued)****Earnings per Common Share**

The following table sets forth the computation of basic and diluted earnings (loss) per share:

|   | Three Months Ended June 30, |            | Six Months Ended June 30, |            |
|---|-----------------------------|------------|---------------------------|------------|
|   | 2006                        | 2005       | 2006                      | 2005       |
| Earnings from continuing operations   | \$ 75,984                   | \$ 62,781  | \$ 105,645                | \$ 71,391  |
| (Loss) Gain on discontinued operations  | (194)                       | (1,309)    | 1,151                     | (2,842)    |
| Net earnings  | \$ 75,790                   | \$ 61,472  | \$ 106,796                | \$ 68,549  |
| Reconciliation of denominators for basic and diluted earnings per share computations: |                             |            |                           |            |
| Basic weighted average number of common shares  | 45,662,541                  | 46,569,420 | 45,706,196                | 46,814,271 |
| Effect of dilutive employee and director awards                                       | 960,376                     | 604,226    | 997,361                   | 640,190    |
| Diluted weighted average number of common shares and assumed conversions              | 46,622,917                  | 47,173,646 | 46,703,557                | 47,454,461 |
| Net earnings (loss) per common share:   |                             |            |                           |            |
| Basic from continuing operations  | \$ 1.66                     | \$ 1.35    | \$ 2.31                   | \$ 1.52    |
| Discontinued operations   |                             | (0.03)     | 0.03                      | (0.06)     |
|   | \$ 1.66                     | \$ 1.32    | \$ 2.34                   | \$ 1.46    |
| Diluted from continuing operations  | \$ 1.63                     | \$ 1.33    | \$ 2.26                   | \$ 1.50    |
| Discontinued operations   |                             | (0.03)     | 0.03                      | (0.06)     |
|   | \$ 1.63                     | \$ 1.30    | \$ 2.29                   | \$ 1.44    |

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**2. Business Combinations and Divestitures**

In 2006 and 2005, the Corporation disposed of certain underperforming operations in its Aggregates operating segment. These divestitures represent discontinued operations, and, therefore, the results of their operations through the dates of disposal and any gain or loss on disposals are included in discontinued operations on the consolidated statements of earnings.

The discontinued operations included the following net sales, pretax loss on operations, pretax gain or loss on disposals, income tax expense or benefit and overall net earnings or loss (dollars in thousands):

|                                 | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|---------------------------------|--------------------------------|------------|------------------------------|------------|
|                                 | 2006                           | 2005       | 2006                         | 2005       |
| Net sales                       | \$ 142                         | \$ 2,151   | \$ 237                       | \$ 6,245   |
| Pretax loss on operations       | \$ (148)                       | \$ (1,906) | \$ (402)                     | \$ (3,172) |
| Pretax gain (loss) on disposals |                                |            | 2,223                        | (924)      |
| Pretax (loss) gain              | (148)                          | (1,906)    | 1,821                        | (4,096)    |
| Income tax expense (benefit)    | 46                             | (597)      | 670                          | (1,254)    |
| Net (loss) earnings             | \$ (194)                       | \$ (1,309) | \$ 1,151                     | \$ (2,842) |

**3. Inventories**

|                                       | June 30,<br>2006              | December<br>31,<br>2005 |
|---------------------------------------|-------------------------------|-------------------------|
|                                       | <i>(Dollars in Thousands)</i> |                         |
| Finished products                     | \$ 199,529                    | \$ 185,681              |
| Products in process and raw materials | 18,195                        | 17,990                  |
| Supplies and expendable parts         | 37,845                        | 31,158                  |
|                                       | 255,569                       | 234,829                 |
| Less allowances                       | (11,855)                      | (12,101)                |
| Total                                 | \$ 243,714                    | \$ 222,728              |

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**4. Goodwill**

The following table shows changes in goodwill, all of which relate to the Aggregates segment (dollars in thousands):

|   | Three Months<br>Ended<br>June 30, 2006 | Six Months<br>Ended<br>June 30, 2006 |
|---|--|--------------------------------------|
| Balance at beginning of period            | \$ 570,336                             | \$ 569,263                           |
| Adjustments to purchase price allocations |  | 1,998                                |
| Amounts allocated to divestitures         |  | (925)                                |
| Balance at end of period                  | \$ 570,336                             | \$ 570,336                           |

**5. Long-Term Debt**

|  | June 30,<br>2006              | December<br>31,<br>2005 |
|--|-------------------------------|-------------------------|
|  | <i>(Dollars in Thousands)</i> |                         |
| 6.875% Notes, due 2011   | \$ 249,814                    | \$ 249,800              |
| 5.875% Notes, due 2008   | 205,265                       | 206,277                 |
| 6.9% Notes, due 2007   | 124,992                       | 124,988                 |
| 7% Debentures, due 2025  | 124,304                       | 124,295                 |
| Commercial paper and line of credit, interest rates ranging from 4.40 % to 5.45% | 13,539                        |                         |
| Acquisition notes, interest rates ranging from 2.11% to 8.00%                    | 769                           | 3,657                   |
| Other notes  | 665                           | 1,005                   |
|  | 719,348                       | 710,022                 |
| Less current maturities  | (13,989)                      | (863)                   |
| Total  | \$ 705,359                    | \$ 709,159              |

The carrying values of the notes due in 2008 included \$5,570,000 and \$6,640,000 at June 30, 2006 and December 31, 2005, respectively, for the unamortized value of terminated interest rate swaps.

In June 2006, the Corporation extended the expiration date of its \$250,000,000 five-year revolving credit agreement (the Credit Agreement) by one year to June 30, 2011. No borrowings were outstanding under the Credit Agreement at June 30, 2006 or December 31, 2005. However, the Credit Agreement supports a \$250,000,000 commercial paper program, of which borrowings of \$10,000,000 were outstanding at June 30, 2006. No borrowings were outstanding under the commercial paper program at December 31, 2005.

The Corporation had \$3,539,000 outstanding under a \$10,000,000 line of credit.



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**6. Income Taxes**

|                                      | Six Months Ended June<br>30, |       |
|--------------------------------------|------------------------------|-------|
|                                      | 2006                         | 2005  |
| Estimated effective income tax rate: |                              |       |
| Continuing operations                | 31.2%                        | 28.0% |
| Discontinued operations              | 36.8%                        | 30.6% |
| Overall                              | 31.3%                        | 27.9% |

The Corporation's effective tax rate reflects the effect of state income taxes and the impact of differences in book and tax accounting arising from the net permanent benefits associated with the depletion allowances for mineral reserves, the domestic production deduction, foreign operating earnings and the tax effect of nondeductibility of goodwill related to asset sales. The effective income tax rates for discontinued operations reflect the tax effects of individual operations' transactions and are not indicative of the Corporation's overall effective tax rate.

The overall effective income tax rate for the six months ended June 30, 2005 reflects the benefit of a decrease in tax reserves related to certain international tax issues currently under examination that increased net earnings by \$1,000,000, or \$0.02 per diluted share. Additionally, the State of Ohio enacted tax reform legislation that reduced income tax expense and increased net earnings by \$1,200,000, or \$0.02 per diluted share, during the quarter ended June 30, 2005.

**7. Pension and Postretirement Benefits**

The following presents the estimated components of the recorded net periodic benefit cost for pension and postretirement benefits for the quarter ended June 30 (dollars in thousands):

|                                 | Pension  |          | Postretirement<br>Benefits |        |
|---------------------------------|----------|----------|----------------------------|--------|
|                                 | 2006     | 2005     | 2006                       | 2005   |
| Service cost                    | \$ 3,072 | \$ 2,637 | \$ 134                     | \$ 70  |
| Interest cost                   | 4,540    | 4,022    | 652                        | 370    |
| Expected return on assets       | (4,904)  | (4,322)  |                            |        |
| Amortization of:                |          |          |                            |        |
| Prior service cost              | 219      | 161      | (340)                      | (161)  |
| Actuarial loss (gain)           | 650      | 512      | (98)                       | (18)   |
| Total net periodic benefit cost | \$ 3,577 | \$ 3,010 | \$ 348                     | \$ 261 |

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**7. Pension and Postretirement Benefits (continued)**

The following presents the estimated components of the recorded net periodic benefit cost for pension and postretirement benefits for the six months ended June 30 (dollars in thousands):

|                                 | Pension  |          | Postretirement<br>Benefits |          |
|---------------------------------|----------|----------|----------------------------|----------|
|                                 | 2006     | 2005     | 2006                       | 2005     |
| Service cost                    | \$ 6,104 | \$ 5,457 | \$ 276                     | \$ 284   |
| Interest cost                   | 9,054    | 8,320    | 1,339                      | 1,490    |
| Expected return on assets       | (9,810)  | (8,942)  |                            |          |
| Amortization of:                |          |          |                            |          |
| Prior service cost              | 371      | 334      | (648)                      | (647)    |
| Actuarial loss (gain)           | 1,430    | 1,059    | (119)                      | (74)     |
| Total net periodic benefit cost | \$ 7,149 | \$ 6,228 | \$ 848                     | \$ 1,053 |

The Corporation has no required pension plan contribution for 2006. However, the Corporation is currently considering a contribution of up to \$23,000,000 during the third quarter of 2006 depending on its then current cash position and an evaluation of alternative uses of available cash.

**8. Contingencies**

In the opinion of management and counsel, it is unlikely that the outcome of litigation and other proceedings, including those pertaining to environmental matters, relating to the Corporation and its subsidiaries, will have a material adverse effect on the results of the Corporation's operations or its financial position.

**9. Stock-Based Compensation**

The shareholders approved, on May 8, 1998, the Martin Marietta Materials, Inc. Stock-Based Award Plan, as amended from time to time (along with the Amended Omnibus Securities Award Plan, originally approved in 1994, the Plans). The Corporation has been authorized by the Board of Directors to repurchase shares of the Corporation's common stock for issuance under the Plans.

Under the Plans, the Corporation grants options to employees to purchase its common stock at a price equal to the market value at the date of grant. The Corporation granted 141,393 employee stock options during the six months ended June 30, 2006. Options granted in 2006 and 2005 become exercisable in four annual installments beginning one year after date of grant and expire eight years from such date. Options granted in years prior to 2005 become exercisable in three equal annual installments beginning one year after date of grant and expire ten years from such date.

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**9. Stock-Based Compensation (continued)**

Pursuant to the Plans, each nonemployee director currently receives 3,000 non-qualified stock options annually. During the six months ended June 30, 2006, the Corporation granted 27,000 options to nonemployee directors. These options have an exercise price equal to the market value at the date of grant, vest immediately and expire ten years from the grant date.

The following table includes summary information for stock options for employees and nonemployee directors for the six months ended June 30, 2006:

|                                  | Number of<br>Options | Weighted-<br>Average<br>Exercise<br>Price | Aggregate<br>Intrinsic Value |
|----------------------------------|----------------------|---|------------------------------|
| Outstanding at December 31, 2005 | 2,478,220            | \$ 43.97                                  |                              |
| Granted                          | 168,393              | \$ 89.02                                  |                              |
| Exercised                        | (610,491)            | \$ 42.87                                  | \$32,659,000                 |
| Terminated                       | (3,728)              | \$ 42.38                                  |                              |
| Outstanding at June 30, 2006     | 2,032,394            | \$ 48.04                                  | \$87,611,000                 |
| Exercisable at June 30, 2006     | 1,307,709            | \$ 45.28                                  | \$59,989,000                 |

For the six months ended June 30, 2005, the intrinsic value of options exercised was \$6,860,000. The intrinsic values of options exercised during the six months ended June 30, 2006 and 2005 were based on the closing prices of the Corporation's common stock on the dates of exercise. The aggregate intrinsic value for options outstanding and exercisable at June 30, 2006 was based on the closing price of the Corporation's common stock at June 30, 2006, which was \$91.15.

The following tables summarize information for options outstanding and exercisable at June 30, 2006:

| Range of<br>Exercise Prices | <b>Options Outstanding</b> |   |                                    |
|-----------------------------|----------------------------|---|------------------------------------|
|                             | Number of<br>Shares        | Weighted-Average<br>Remaining Life<br>(years) | Weighted-Average<br>Exercise Price |
| \$24.25-\$35.50             | 18,084                     | 1.1   | \$ 35.50                           |
| \$36.55-\$51.50             | 1,684,783                  | 5.8   | \$ 42.83                           |
| \$61.05-\$89.02             | 329,527                    | 7.6   | \$ 75.39                           |
|                             | 2,032,394                  | 6.1   |                                    |





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**9. Stock-Based Compensation (continued)**

| Range of<br>Exercise Prices | <b>Options Exercisable</b> |  | Weighted-Average<br>Remaining Life<br>(years) | Weighted-Average<br>Exercise Price |
|-----------------------------|----------------------------|--|---|------------------------------------|
|                             | Number of<br>Shares        |  |   |                                    |
| \$24.25-\$35.50             | 18,084                     |  | 1.1   | \$ 35.50                           |
| \$36.55-\$51.50             | 1,197,608                  |  | 5.1   | \$ 43.57                           |
| \$61.05-\$89.02             | 92,017                     |  | 8.0   | \$ 69.44                           |
|                             | 1,307,709                  |  | 5.2   |                                    |

Additionally, an incentive stock plan has been adopted under the Plans whereby certain participants may elect to use up to 50% of their annual incentive compensation to acquire units representing shares of the Corporation's common stock at a 20% discount to the market value on the date of the incentive compensation award. Certain executive officers are required to participate in the incentive stock plan at certain minimum levels. Participants earn the right to receive their respective shares at the discounted value generally at the end of a 35-month period of additional employment from the date of award or at retirement beginning at age 62. All rights of ownership of the common stock convey to the participants upon the issuance of their respective shares at the end of the ownership-vesting period, with the exception of dividend equivalents that are paid on the units during the vesting period.

The Corporation grants restricted stock awards under the Plans to a group of executive officers and key personnel. Certain restricted stock awards are based on specific common stock performance criteria over a specified period of time. In addition, certain awards were granted to individuals to encourage retention and motivate key employees. These awards generally vest if the employee is continuously employed over a specified period of time and require no payment from the employee.

The following table summarizes information for incentive compensation awards and restricted stock awards for the six months ended June 30, 2006:

|                              | <b>Incentive Compensation<br/>Awards</b> |  | <b>Restricted Stock<br/>Awards</b> |  |
|------------------------------|--|--|------------------------------------|--|
|                              | Number of<br>Awards                      | Weighted-<br>Average<br>Grant-Date<br>Fair Value | Number of<br>Awards                | Weighted-<br>Average<br>Grant-Date<br>Fair Value |
| Balance at December 31, 2005 | 69,855                                   |  | 276,712                            |  |
| Awarded                      | 27,302                                   | \$91.05  | 109,306                            | \$89.49  |
| Distributed                  | (2,199)                                  |  | (463)                              |  |
| Forfeited                    | (241)                                    |  | (956)                              |  |

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|                           |             |              |
|---------------------------|-------------|--------------|
| Balance at June 30, 2006  | 94,717      | 384,599      |
| Aggregate intrinsic value | \$3,899,000 | \$13,715,000 |

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**9. Stock-Based Compensation (continued)**

The weighted-average grant-date fair value for incentive compensation awards and restricted awards granted during the six months ended June 30, 2005 was \$55.15 and \$60.63, respectively.

The aggregate intrinsic values for incentive compensation awards and restricted stock awards at June 30, 2006 were based on the closing price of the Corporation's common stock at June 30, 2006, which was \$91.15.

At June 30, 2006, approximately 1,246,000 shares were available for grant under the Plans.

In 1996, the Corporation adopted the Shareholder Value Achievement Plan to award shares of the Corporation's common stock to key senior employees based on certain common stock performance criteria over a long-term period. Under the terms of this plan, 250,000 shares of common stock were reserved for issuance. Through June 30, 2006, 42,025 shares have been issued under this plan. No awards have been granted under this plan after 2000.

Also, the Corporation adopted and the shareholders approved the Common Stock Purchase Plan for Directors in 1996, which provides nonemployee directors the election to receive all or a portion of their total fees in the form of the Corporation's common stock. The Corporation has reserved 300,000 shares of common stock for issuance in connection with this plan. Currently, directors are required to defer at least 50% of their retainer in the form of the Corporation's common stock at a 20% discount to market value. Directors elected to defer portions of their fees representing 5,940 shares of the Corporation's common stock under this plan during the six months ended June 30, 2006.

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**9. Stock-Based Compensation (continued)**

The following table summarizes stock-based compensation expense for the three and six months ended June 30, 2006 and 2005, unrecognized compensation cost for nonvested awards not yet recognized at June 30, 2006 and the weighted-average period over which unrecognized compensation cost is expected to be recognized:

|   | <b>Stock<br/>Options</b> | <b>Restricted<br/>Stock Awards</b> | <b>Incentive<br/>Compensation<br/>Awards</b> | <b>Directors<br/>Awards</b> | <b>Total</b> |
|---|--------------------------|------------------------------------|--|-----------------------------|--------------|
| Stock-based compensation expense recognized for three months ended June 30:         |                          |                                    |  |                             |              |
| 2006  | \$2,121,000              | \$ 1,412,000                       | \$124,000                                    | \$188,000                   | \$ 3,845,000 |
| 2005  | \$                       | \$ 516,000                         | \$ 76,000                                    | \$171,000                   | \$ 763,000   |
| Stock-based compensation expense recognized for six months ended June 30:           |                          |                                    |  |                             |              |
| 2006  | \$3,189,000              | \$ 2,262,000                       | \$255,000                                    | \$359,000                   | \$ 6,065,000 |
| 2005  | \$                       | \$ 1,040,000                       | \$157,000                                    | \$330,000                   | \$ 1,527,000 |
| Unrecognized compensation cost at June 30, 2006:                                    | \$6,238,000              | \$14,587,000                       | \$593,000                                    | \$336,000                   | \$21,754,000 |
| Weighted-average period over which unrecognized compensation cost to be recognized: | 1.8 years                | 2.6 years                          | 1.5 years                                    | 0.8 years                   |              |

For the six months ended June 30, 2006, the Corporation recognized a tax benefit related to stock-based compensation of \$2,020,000.

The following presents expected stock-based compensation expense in future periods for outstanding awards as of June 30, 2006:

|                   |              |
|-------------------|--------------|
| Remainder of 2006 | \$ 7,350,000 |
| 2007              | 7,330,000    |
| 2008              | 4,292,000    |
| 2009              | 2,234,000    |
| 2010              | 548,000      |

Total

\$ 21,754,000

Stock-based compensation expense is included in selling, general and administrative expenses on the Corporation's consolidated statements of earnings.

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**10. Business Segments**

The Corporation conducts its operations through two reportable business segments: Aggregates and Specialty Products. The following tables display selected financial data for the Corporation's reportable business segments (dollars in thousands):

|                                     | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|-------------------------------------|--------------------------------|------------|------------------------------|------------|
|                                     | 2006                           | 2005       | 2006                         | 2005       |
| <u>Total revenues</u>               |                                |            |                              |            |
| Aggregates                          | \$ 548,068                     | \$ 509,607 | \$ 986,739                   | \$ 865,289 |
| Specialty Products                  | 40,573                         | 34,234     | 85,866                       | 68,280     |
| Total                               | \$ 588,641                     | \$ 543,841 | \$ 1,072,605                 | \$ 933,569 |
| <br><u>Net sales</u>                |                                |            |                              |            |
| Aggregates                          | \$ 481,843                     | \$ 446,578 | \$ 864,845                   | \$ 754,261 |
| Specialty Products                  | 36,428                         | 30,681     | 77,837                       | 61,215     |
| Total                               | \$ 518,271                     | \$ 477,259 | \$ 942,682                   | \$ 815,476 |
| <br><u>Earnings from operations</u> |                                |            |                              |            |
| Aggregates                          | \$ 112,555                     | \$ 98,122  | \$ 156,916                   | \$ 115,099 |
| Specialty Products                  | 7,065                          | 1,734      | 13,989                       | 4,208      |
| Total                               | \$ 119,620                     | \$ 99,856  | \$ 170,905                   | \$ 119,307 |

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**11. Accounting Changes**

In March 2006, the Financial Accounting Standards Board ( FASB ) issued an Exposure Draft, *Employers Accounting for Defined Benefit Pension and Other Postretirement Benefits, an amendment of FAS 87, 88, 106 and 132(R)*. In its current form, the proposed statement requires an employer that sponsors one or more defined benefit pension or other postretirement plans to recognize an asset or liability for the overfunded or underfunded status of the plan. Additionally, employers would be required to record all unrecognized prior service costs and credits, unrecognized actual gains and losses and any unrecognized transition obligations or assets in accumulated other comprehensive income. Such amounts would be reclassified into earnings as components of net period benefit cost/income pursuant to the current recognition and amortization provisions of Statements of Financial Accounting Standards No. 87, *Employers Accounting for Pensions* ( FAS 87 ) and No. 106, *Employers Accounting for Postretirement Benefits Other than Pensions* ( FAS 106 ). Finally, the proposed statement requires an employer to measure plan assets and benefit obligations as of the date of the employer's statement of financial position. The FASB has indicated that it expects to issue a final standard later this year. Except for the measurement date requirement, the proposed statement would be effective for fiscal years ending after December 15, 2006 and should be applied prospectively. The measurement date requirement would be effective for fiscal years beginning after December 31, 2006. At December 31, 2005, the Corporation's pension plans were underfunded by \$59.7 million and its postretirement plans, which provide medical benefits for retirees, were underfunded by \$51.6 million. Further, the Corporation currently uses an annual measurement date of November 30.

In July 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertain Tax Positions, an Interpretation of FAS 109* ( FIN 48 ), which clarifies the criteria for recognition and measurement of benefits from uncertain tax positions. Under FIN 48, an entity should recognize a tax benefit when it is more-likely-than-not, based on the technical merits, that the position would be sustained upon examination by a taxing authority. The amount to be recognized should be measured as the largest amount of tax benefit that is greater than 50 percent likely of being realized upon ultimate settlement with a taxing authority that has full knowledge of all relevant information. Furthermore, any change in the recognition, derecognition or measurement of a tax position should be recognized in the interim period in which the change occurs. FIN 48 is effective January 1, 2007 for the Corporation, and any change in net assets as a result of applying the Interpretation will be recognized as an adjustment to retained earnings at that date. Management is in the process of evaluating its uncertain tax positions in accordance with FIN 48.

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MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND  
RESULTS OF OPERATIONS

Second Quarter and Six Months Ended June 30, 2006

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

**OVERVIEW** Martin Marietta Materials, Inc. (the Corporation), conducts its operations through two reportable business segments: Aggregates and Specialty Products. The Corporation's net sales and earnings are predominately derived from its Aggregates segment, which processes and sells granite, limestone, and other aggregates products from a network of 322 quarries, distribution facilities and plants in 28 states in the southeastern, southwestern, midwestern and central regions of the United States and in the Bahamas and Canada. The Aggregates segment's products are used primarily by commercial customers principally in domestic construction of highways and other infrastructure projects and for commercial and residential buildings. The Specialty Products segment produces magnesia-based chemicals products used in industrial, agricultural and environmental applications; dolomitic lime sold primarily to customers in the steel industry; and structural composite products used in a wide variety of applications, both military and commercial.

**CRITICAL ACCOUNTING POLICIES** The Corporation outlined its critical accounting policies in its Annual Report on Form 10-K for the year ended December 31, 2005, filed with the Securities and Exchange Commission on February 27, 2006. As discussed in Note 9 to the Consolidated Financial Statements, the Corporation adopted Statement of Financial Accounting Standards No. 123 (revised 2004), *Share-Based Payment* (FAS 123(R)) on January 1, 2006. FAS 123(R) requires all forms of share-based payments to employees, including employee stock options, to be recognized as compensation expense. The compensation expense is the fair value of the awards at the measurement date. The Corporation adopted the provisions of FAS 123(R) using the modified prospective transition method, which recognizes stock option awards as compensation expense for unvested awards as of January 1, 2006 and awards granted or modified subsequent to that date. In accordance with the modified prospective transition method, the Corporation's consolidated statements of earnings and cash flows for the prior-year periods have not been restated. The impact to the Corporation of adopting FAS 123(R) and expensing stock options granted in 2006 and the unvested portion of outstanding employee stock options was as follows:

|   | Three Months<br>Ended<br>June 30, 2006 | Six Months<br>Ended<br>June 30, 2006 |
|---|--|--------------------------------------|
| Decreased earnings from continuing operations before income tax expense by: | \$ 2,121,000                           | \$ 3,189,000                         |
| Decreased earnings from continuing operations and net earnings by:          | \$ 1,282,000                           | \$ 1,928,000                         |
| Decreased basic earnings per share by:                                      | \$ 0.03                                | \$ 0.04                              |
| Decreased diluted earnings per share by:                                    | \$ 0.03                                | \$ 0.04                              |

In addition, the Corporation reclassified \$12,339,000 of stock-based compensation liabilities to additional paid-in-capital, thereby increasing shareholders' equity at January 1, 2006.



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Prior to January 1, 2006, the Corporation accounted for its stock-based compensation plans under the intrinsic value method prescribed by APB Opinion 25, *Accounting for Stock Issued to Employees*, and related Interpretations. Compensation cost was recognized in net earnings for awards granted under those plans with an exercise price less than the market value of the underlying common stock on the date of grant. For nonqualified stock options granted under those plans with an exercise price equal to the market value of the stock on the date of grant, no compensation cost was recognized in net earnings as reported in the consolidated statement of earnings. Rather, stock-based compensation expense was included as a pro forma disclosure in the notes to the financial statements. Pro forma disclosures of net earnings and earnings per share continue to be provided for periods prior to January 1, 2006. The Corporation has stock-based compensation plans for certain of its employees and its nonemployee directors. All stock-based compensation equity awards are units until distributed as shares of common stock upon vesting. The plans provide for the following types of equity awards:

Nonqualified stock options to certain employees and nonemployee directors

Restricted stock awards to certain employees ( restricted stock awards )

Stock awards to certain employees related to incentive compensation ( incentive compensation awards )

Common stock purchase plan for nonemployee directors related to their annual retainer and meeting fees ( directors awards )

In 2005, the Corporation's Management Development and Compensation Committee redesigned the Corporation's long-term compensation program to more directly tie pay with performance. Prior to redesign, the long-term compensation program consisted primarily of stock options, which were awarded based on a multiple of base compensation and targeted to be competitive with equity awards granted for comparable positions in other corporations similar to the Corporation. The revised program consists of a mix of stock options and restricted stock awards for senior level employees and restricted stock awards for other participants. Awards granted under the revised program are based on the Corporation's achievement of specific goals related to the return on invested capital as compared to its weighted average cost of capital. Additionally, the Corporation may grant restricted stock awards based on its performance relative to peer groups to certain employees.

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The following table summarizes stock-based compensation expense for the three and six months ended June 30, 2006 and 2005, unrecognized compensation cost for nonvested awards not yet recognized at June 30, 2006 and the weighted-average period over which unrecognized compensation cost is expected to be recognized:

|   | <b>Stock<br/>Options</b> | <b>Restricted<br/>Stock Awards</b> | <b>Incentive<br/>Compensation<br/>Awards</b> | <b>Directors<br/>Awards</b> | <b>Total</b> |
|---|--------------------------|------------------------------------|--|-----------------------------|--------------|
| Stock-based compensation expense recognized for three months ended June 30:         |                          |                                    |  |                             |              |
| 2006  | \$2,121,000              | \$ 1,412,000                       | \$124,000                                    | \$188,000                   | \$ 3,845,000 |
| 2005  | \$                       | \$ 516,000                         | \$ 76,000                                    | \$171,000                   | \$ 763,000   |
| Stock-based compensation expense recognized for six months ended June 30:           |                          |                                    |  |                             |              |
| 2006  | \$3,189,000              | \$ 2,262,000                       | \$255,000                                    | \$359,000                   | \$ 6,065,000 |
| 2005  | \$                       | \$ 1,040,000                       | \$157,000                                    | \$330,000                   | \$ 1,527,000 |
| Unrecognized compensation cost at June 30, 2006:                                    | \$6,238,000              | \$14,587,000                       | \$593,000                                    | \$336,000                   | \$21,754,000 |
| Weighted-average period over which unrecognized compensation cost to be recognized: | 1.8 years                | 2.6 years                          | 1.5 years                                    | 0.8 years                   |              |

The following presents a horizon for stock-based compensation expense for outstanding awards as of June 30, 2006:

|                   |               |
|-------------------|---------------|
| Remainder of 2006 | \$ 7,350,000  |
| 2007              | 7,330,000     |
| 2008              | 4,292,000     |
| 2009              | 2,234,000     |
| 2010              | 548,000       |
| Total             | \$ 21,754,000 |



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Valuation of Stock-Based Compensation Awards

The Corporation used a lattice valuation model to determine the fair value of stock option awards granted in 2006, 2005 and 2004. The Black-Scholes valuation model was used for stock options granted prior to 2004. The lattice valuation model takes into account exercise patterns based on changes in the Corporation's stock price, the lack of transferability of the awards and other complex and subjective variables and is considered to result in a more accurate valuation of stock options than the Black-Scholes valuation model. The period of time for which options are expected to be outstanding, or expected term of the option, is a derived output of the lattice valuation model. The Corporation considers the following factors when estimating the expected term of options: vesting period of the award, expected volatility of the underlying stock, employees' ages and external data.

Other key assumptions used in determining the fair value of the stock options awarded in 2006 and 2005 were:

|                         | 2006      | 2005      |
|-------------------------|-----------|-----------|
| Risk-free interest rate | 4.90%     | 3.80%     |
| Dividend yield          | 1.10%     | 1.60%     |
| Volatility factor       | 31.20%    | 30.80%    |
| Expected term           | 6.9 years | 6.3 years |

Based on these assumptions, the weighted-average fair value of each stock option granted was \$33.21 for 2006 and \$18.72 for 2005.

The risk-free interest rate reflects the interest rate on zero-coupon U.S. government bonds available at the time each option was granted having a remaining life approximately equal to the option's expected life. The dividend yield represents the dividend rate expected to be paid over the option's expected life and is based on the Corporation's historical dividend payments and targeted dividend pattern. The Corporation's dividend pattern is outlined in its Annual Report on Form 10-K for the year ended December 31, 2005, filed with the Securities and Exchange Commission on February 27, 2006. The Corporation's volatility factor measures the amount by which its stock price is expected to fluctuate during the expected life of the option and is based on historical stock price changes.

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Any change in the aforementioned assumptions could affect the estimated fair value of future stock options. The following table shows the impact on the fair value estimate if there were a change in any of the key assumptions:

| <b>An increase to the:</b>           | <b>Results in a fair value that is:</b> |
|--------------------------------------|---|
| Price of the underlying common stock | Higher                                  |
| Exercise price of option             | Lower                                   |
| Expected term of option              | Higher                                  |
| Risk-free interest rate              | Higher                                  |
| Expected dividends on stock          | Lower                                   |
| Expected volatility of stock         | Higher                                  |

Restricted stock awards require no payment from the employee upon distribution. Therefore, the closing price of the Corporation's common stock on the measurement date represents the fair value of these awards.

Incentive compensation awards allow participants to use up to 50% of their annual incentive compensation to acquire units representing shares of the Corporation's common stock at a 20% discount to the market value on the date of the incentive compensation award. Certain executive officers are required to participate in the incentive compensation plan at certain minimum levels. The Corporation expenses the 80% purchase price to the employees in the year the employees earn the incentive compensation. Additionally, the Corporation amortizes the 20% discount over 35 months for unvested awards as of January 1, 2006 and/or over the requisite service period for awards granted subsequent to the adoption of FAS 123(R). The expense related to the 20% discount is based on the closing price of the Corporation's common stock on the measurement date of the award.

Common stock awards provide nonemployee directors the election to receive all or a portion of their total fees in the form of the Corporation's common stock. Currently, directors are required to defer at least 50% of their annual retainer in the form of the Corporation's common stock at a 20% discount to market value. The Corporation expenses directors fees in the period in which they are earned, with the exception of the annual retainer, which is expensed over a 12 month period from the award date. Additionally, the Corporation amortizes the 20% discount over 12 months. The expense related to the 20% discount is based on the closing price of the Corporation's common stock on the measurement date of the award.

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Expense Allocation

FAS 123(R) requires stock-based compensation cost to be recognized over the requisite service period for all awards granted subsequent to adoption. The requisite service period is defined as the period of time over which an employee must provide service in exchange for an award under a share-based payment arrangement. Certain of the Corporation's stock-based compensation plans provide for accelerated vesting of awards when an employee retires from active service and is eligible to receive unreduced retirement benefits under the Corporation's pension plans (defined as age 62 or normal retirement age). The requisite service period for employees of the Corporation who reach normal retirement age of 62 prior to the end of the stated vesting period of the award is the period from the measurement date of the award until the date the employee reaches retirement age. For stock-based payment awards granted to employees that are close to age 62 or have already reached the age of 62, the expense will be front-loaded as compared with the vesting period. Stock options granted to nonemployee directors vest immediately. Therefore, these awards have no requisite service period and are expensed on the measurement date.

Prior to the adoption of FAS 123(R), the Corporation expensed stock-based payment awards for recognition or pro forma purposes, as required, over their stated vesting periods. The Corporation will recognize compensation cost over the stated vesting period for the unvested portion of existing awards as of January 1, 2006, with acceleration for any remaining unrecognized compensation cost if an employee actually retires prior to the vesting date. The stated vesting periods for existing awards as of January 1, 2006 are as follow:

|   |                                  |
|---|----------------------------------|
| <i>Options granted in 2006 and 2005</i> | 4-year graded vesting            |
| <i>Options granted prior to 2005</i>    | 3-year graded vesting            |
| <i>Restricted stock awards</i>          | 35 to 93 months (award specific) |
| <i>Incentive compensation awards</i>    | 35 months                        |

Under FAS 123(R), an entity may elect either the accelerated expense recognition method or a straight-line recognition method for awards subject to graded vesting based on a service condition. The Corporation elected to use the accelerated expense recognition method for stock options issued to employees. The accelerated recognition method requires stock options that vest ratably to be divided into tranches. The expense for each tranche is allocated to its particular vesting period.

FAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. The Corporation estimated forfeitures for each homogenous group of employees granted awards. Employee groups consist of Directors; Section 16 Officers and Division Presidents; Vice Presidents/General Managers; and Others. The Corporation will ultimately recognize compensation cost only for those stock-based awards that vest.

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Other Factors

FAS 123(R), similar to other accounting rulemaking, is complex and requires significant estimates and assumptions. In response to certain implementation issues, the Financial Accounting Standards Board has created the FAS 123(R) Resource Group (the Resource Group) to deliberate certain issues. The Corporation's accounting and reporting treatment of certain issues may change as a result of the issuance of any future guidance by the Resource Group.

**RESULTS OF OPERATIONS**

Except as indicated, the following comparative analysis in the Results of Operations section of this Management's Discussion and Analysis of Financial Condition and Results of Operations reflects results from continuing operations and is based on net sales and cost of sales.

Gross margin as a percentage of net sales and operating margin as a percentage of net sales represent non-GAAP measures. The Corporation presents these ratios calculated based on net sales, as it is consistent with the basis by which management reviews the Corporation's operating results. Further, management believes it is consistent with the basis by which investors analyze the Corporation's operating results given that freight and delivery revenues and costs represent pass-throughs and have no mark-up. Gross margin and operating margin calculated as percentages of total revenues represent the most directly comparable financial measures calculated in accordance with generally accepted accounting principles (GAAP). The following tables present the calculations of gross margin and operating margin for the three and six months ended June 30 in accordance with GAAP and reconciliations of the ratios as percentages of total revenues to percentages of net sales (dollars in thousands).

**Gross Margin in Accordance with GAAP**

|                | Three Months Ended |            | Six Months Ended |            |
|----------------|--------------------|------------|------------------|------------|
|                | June 30,           |            | June 30,         |            |
|                | 2006               | 2005       | 2006             | 2005       |
| Gross profit   | \$ 153,265         | \$ 129,625 | \$ 237,228       | \$ 179,294 |
| Total revenues | \$ 588,641         | \$ 543,841 | \$ 1,072,605     | \$ 933,569 |
| Gross margin   | 26.0%              | 23.8%      | 22.1%            | 19.2%      |

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**Gross Margin Excluding Freight and Delivery Revenues**

|  | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|--|--------------------------------|------------|------------------------------|------------|
|  | 2006                           | 2005       | 2006                         | 2005       |
| Gross profit   | \$ 153,265                     | \$ 129,625 | \$ 237,228                   | \$ 179,294 |
| Total revenues                                       | \$ 588,641                     | \$ 543,841 | \$ 1,072,605                 | \$ 933,569 |
| Less: Freight and delivery revenues                  | (70,370)                       | (66,582)   | (129,923)                    | (118,093)  |
| Net sales  | \$ 518,271                     | \$ 477,259 | \$ 942,682                   | \$ 815,476 |
| Gross margin excluding freight and delivery revenues | 29.6%                          | 27.2%      | 25.2%                        | 22.0%      |

**Operating Margin in Accordance with GAAP**

|                          | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|--------------------------|--------------------------------|------------|------------------------------|------------|
|                          | 2006                           | 2005       | 2006                         | 2005       |
| Earnings from operations | \$ 119,620                     | \$ 99,856  | \$ 170,905                   | \$ 119,307 |
| Total revenues           | \$ 588,641                     | \$ 543,841 | \$ 1,072,605                 | \$ 933,569 |
| Operating margin         | 20.3%                          | 18.4%      | 15.9%                        | 12.8%      |



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**Operating Margin Excluding Freight and Delivery Revenues**

|  | Three Months Ended<br>June 30, |            | Six Months Ended<br>June 30, |            |
|--|--------------------------------|------------|------------------------------|------------|
|  | 2006                           | 2005       | 2006                         | 2005       |
| Earnings from operations                                 | \$ 119,620                     | \$ 99,856  | \$ 170,905                   | \$ 119,307 |
| Total revenues   | \$ 588,641                     | \$ 543,841 | \$ 1,072,605                 | \$ 933,569 |
| Less: Freight and delivery revenues                      | (70,370)                       | (66,582)   | (129,923)                    | (118,093)  |
| Net sales  | \$ 518,271                     | \$ 477,259 | \$ 942,682                   | \$ 815,476 |
| Operating margin excluding freight and delivery revenues | 23.1%                          | 20.9%      | 18.1%                        | 14.6%      |

Quarter Ended June 30

Notable items for the quarter ended June 30, 2006 included:

Earnings per diluted share of \$1.63, up 25.4% from the prior-year quarter

Net sales of \$518.3 million, up 8.6% from the prior-year quarter

Heritage aggregates pricing up 11.8%; heritage volume decreased 2.4% (primarily weather-related)

Heritage aggregates product line gross margin excluding freight and delivery revenues up 220 basis points over prior-year quarter

Magnesia Specialties earnings from operations up 56.1% over prior-year quarter

Consolidated operating margin excluding freight and delivery revenues of 23.1%, up 220 basis points over prior-year quarter

Repurchased 500,000 shares of common stock

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The following table present net sales, gross profit, selling, general and administrative expenses, other operating (income) and expenses, net, and earnings from operations data for the Corporation and each of its segments for the three months ended June 30, 2006 and 2005. In each case, the data is stated as a percentage of net sales, of the Corporation or the relevant segment, as the case may be.

Earnings from operations include research and development expense. This expense for the Corporation was \$0.1 million and \$0.2 million for the quarters ended June 30, 2006 and 2005, respectively.

|   | Three Months Ended June 30,   |                      | 2005       | % of<br>Net<br>Sales |
|---|-------------------------------|----------------------|------------|----------------------|
|   | 2006                          | % of<br>Net<br>Sales |            |                      |
|   | Amount                        | Amount               | Amount     | Amount               |
|   | <i>(Dollars in Thousands)</i> |                      |            |                      |
| Net sales:                                  |                               |                      |            |                      |
| Aggregates                                  | \$ 481,843                    | 100.0                | \$ 446,578 | 100.0                |
| Specialty Products                          | 36,428                        | 100.0                | 30,681     | 100.0                |
| Total                                       | \$ 518,271                    | 100.0                | \$ 477,259 | 100.0                |
| Gross profit:                               |                               |                      |            |                      |
| Aggregates                                  | \$ 143,422                    | 29.8                 | \$ 124,884 | 28.0                 |
| Specialty Products                          | 9,843                         | 27.0                 | 4,741      | 15.5                 |
| Total                                       | \$ 153,265                    | 29.6                 | \$ 129,625 | 27.2                 |
| Selling, general & administrative expenses: |                               |                      |            |                      |
| Aggregates                                  | \$ 34,451                     | 7.1                  | \$ 29,056  | 6.5                  |
| Specialty Products                          | 2,697                         | 7.4                  | 2,745      | 8.9                  |
| Total                                       | \$ 37,148                     | 7.2                  | \$ 31,801  | 6.7                  |
| Other operating (income) and expenses, net: |                               |                      |            |                      |
| Aggregates                                  | \$ (3,584)                    | (0.7)                | \$ (2,295) | (0.5)                |
| Specialty Products                          | (59)                          | (0.2)                | 70         | 0.2                  |
| Total                                       | \$ (3,643)                    | (0.7)                | \$ (2,225) | (0.5)                |

Earnings from operations:

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|                    |            |      |           |      |
|--------------------|------------|------|-----------|------|
| Aggregates         | \$ 112,555 | 23.4 | \$ 98,122 | 22.0 |
| Specialty Products | 7,065      | 19.4 | 1,734     | 5.7  |
| Total              | \$ 119,620 | 23.1 | \$ 99,856 | 20.9 |

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Net sales for the Aggregates segment for the 2006 second quarter were \$481.8 million, a 7.9 percent increase over 2005 second-quarter sales of \$446.6 million. The heritage aggregates average selling price increased 11.8 percent with price increases being strongest in the high growth southern markets. A decline of 2.4 percent in heritage aggregates shipments partially offset pricing gains. The decline in shipments for the quarter was primarily weather driven, with North Carolina experiencing one of the wettest Junes in recorded history. Rail and barge transportation issues also played a role in keeping shipments below expectations.

The following tables present volume and pricing data and shipments data for heritage operations, acquisitions and discontinued operations. Heritage aggregates operations exclude acquisitions that were not included in prior-year operations for the comparable period and divestitures.

|   | Three Months Ended<br>June 30, 2006 |         |
|---|-------------------------------------|---------|
|   | Volume                              | Pricing |
| Volume/Pricing Variance <sup>(1)</sup>        |                                     |         |
| Heritage Aggregates Operations <sup>(2)</sup> | (2.4%)                              | 11.8%   |
| Aggregates Segment <sup>(3)</sup>             | (2.9%)                              | 11.9%   |

  

|   | Three Months Ended<br>June 30, |        |
|---|--------------------------------|--------|
|   | 2006                           | 2005   |
| Shipments (tons in thousands)                 |                                |        |
| Heritage Aggregates Operations <sup>(2)</sup> | 54,989                         | 56,364 |
| Acquisitions                                  |                                |        |
| Divestitures <sup>(4)</sup>                   | 13                             | 290    |
| Aggregates Segment <sup>(3)</sup>             | 55,002                         | 56,654 |

(1) *Volume/pricing variances reflect the percentage increase from the comparable period in the prior year.*

(2) *Heritage aggregates operations exclude acquisitions that have not been*

*included in  
prior-year  
operations for a  
full year and  
divestitures.*

(3) *Aggregates  
segment  
includes all  
acquisitions  
from the date of  
acquisition and  
divested  
operations  
through the  
dates of  
divestiture.*

(4) *Divestitures  
represent tons  
related to  
divested  
operations up to  
the dates of  
divestiture.*

Heritage aggregates product line gross margin as a percentage of net sales increased 220 basis points during the quarter. Pricing gains, coupled with continued focus on cost management, more than offset aggregates shipment declines, significantly higher costs related to energy, supplies and freight embedded in the Corporation's long-haul transportation network, and higher than expected start-up costs for major capacity expansion projects. Diesel fuel, natural gas and liquid asphalt costs used in aggregates and asphalt production increased approximately \$9 million when compared with the prior-year's quarter. During the quarter ended June 30, 2006, the Corporation reduced an accrual for purchases against cost of sales, thereby increasing net earnings by \$1.5 million, or \$0.03 per diluted share.

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Selling, general and administrative expenses as a percentage of net sales for the Aggregates segment were 7.1 percent for the second quarter 2006 as compared with 6.5 percent in the prior-year quarter. The increase in the expense ratio reflects the impact of expensing stock options. Total stock-based compensation expense for the quarter was \$3.8 million in 2006 compared with \$0.8 million in 2005. The initial expensing of stock options increased selling, general and administrative expenses by \$2.1 million during the quarter. After consideration of the impact of increased stock-based compensation expense, selling, general and administrative expenses as a percentage of net sales is flat with the prior quarter.

Among other items, other operating income and expenses, net, includes gains and losses on the sale of assets; gains and losses related to certain accounts receivable; rental, royalty and services income; and expenses related to Statement of Financial Accounting Standards No. 143, *Accounting for Asset Retirement Obligations*. For the second quarter, other operating income and expenses, net, for the Aggregates segment was income of \$3.6 million in 2006 compared with \$2.3 million in 2005, primarily as a result of higher gains on the sales of assets.

The Aggregates segment's business is significantly affected by seasonal changes and other weather-related conditions. Consequently, the Aggregates segment's production and shipment levels coincide with general construction activity levels, most of which typically occur in the spring, summer and fall for the segment's markets, and production and shipment levels vary by quarter. Further because of the potentially significant impact of weather on the Corporation's operations, second quarter results are not indicative of expected performance for the year.

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Second-quarter results for the Specialty Products segment, which includes the Magnesia Specialties and Structural Composite Products businesses, were positive. Magnesia Specialties net sales grew 21.3 percent as a result of improved pricing and volume of dolomitic lime to the steel industry and chemicals products to a variety of end users. Earnings from operations at Magnesia Specialties were \$10.0 million compared with \$6.4 million in the prior-year period. Specialty Products results for the second quarter included a pretax loss from operations in the Structural Composite Products business of \$3.0 million in 2006 compared with \$4.7 million in 2005. The 2005 pretax loss reduction in the Structural Composite Products business results from the difference in second quarter inventory write-offs of \$0.4 million in 2006 and \$2.0 million in 2005. If the Structural Composite Products business does not meet certain performance objectives during the remainder of 2006, management will evaluate alternative approaches. In addition to other offsetting amounts, other nonoperating income and expenses, net, are comprised generally of interest income, net equity earnings from nonconsolidated investments and eliminations of minority interests for consolidated non-wholly owned subsidiaries. Consolidated other nonoperating income and expenses, net, for the quarter ended June 30, were \$0.3 million in income in 2006 compared with an expense of \$1.0 million in 2005.

Six Months Ended June 30

Notable items for the six months ended June 30, 2006 included:

Earnings per diluted share of \$2.29, up 59.0% as compared with \$1.44 in the prior year

Net sales of \$942.7 million, up 15.6% as compared with the prior year

Heritage aggregates pricing up 13.2% and volume up 2.1%

Specialties Products segment earnings from operations increased \$9.8 million over prior year on continued improvement in the Magnesia Specialties business

Selling, general and administrative expenses as a percentage of net sales remained flat at 7.8%, despite increased stock-based compensation expense in 2006

Consolidated operating margin excluding freight and delivery revenues of 18.1%, up 350 basis points over prior year

Repurchased 914,400 shares of common stock for \$83.2 million

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MARTIN MARIETTA MATERIALS, INC. AND CONSOLIDATED SUBSIDIARIES  
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(Continued)

The following table present net sales, gross profit, selling, general and administrative expenses, other operating (income) and expenses, net, and earnings from operations data for the Corporation and each of its segments for the six months ended June 30, 2006 and 2005. In each case, the data is stated as a percentage of net sales, of the Corporation or the relevant segment, as the case may be.

Earnings from operations include research and development expense. This expense for the Corporation was \$0.3 million for the six months ended June 30, 2006 and 2005.

|   | Six Months Ended June 30,     |                      | 2005       | % of<br>Net<br>Sales |
|---|-------------------------------|----------------------|------------|----------------------|
|   | 2006                          | % of<br>Net<br>Sales |            |                      |
|   | Amount                        | Amount               | Amount     | % of<br>Net<br>Sales |
|   | <i>(Dollars in Thousands)</i> |                      |            |                      |
| Net sales:                                  |                               |                      |            |                      |
| Aggregates                                  | \$ 864,845                    | 100.0                | \$ 754,261 | 100.0                |
| Specialty Products                          | 77,837                        | 100.0                | 61,215     | 100.0                |
| Total                                       | \$ 942,682                    | 100.0                | \$ 815,476 | 100.0                |
| Gross profit:                               |                               |                      |            |                      |
| Aggregates                                  | \$ 217,801                    | 25.2                 | \$ 169,171 | 22.4                 |
| Specialty Products                          | 19,427                        | 25.0                 | 10,123     | 16.5                 |
| Total                                       | \$ 237,228                    | 25.2                 | \$ 179,294 | 22.0                 |
| Selling, general & administrative expenses: |                               |                      |            |                      |
| Aggregates                                  | \$ 67,864                     | 7.8                  | \$ 58,048  | 7.7                  |
| Specialty Products                          | 5,445                         | 7.0                  | 5,581      | 9.1                  |
| Total                                       | \$ 73,309                     | 7.8                  | \$ 63,629  | 7.8                  |
| Other operating (income) and expenses, net: |                               |                      |            |                      |
| Aggregates                                  | \$ (6,979)                    | (0.8)                | \$ (3,976) | (0.5)                |
| Specialty Products                          | (311)                         | (0.4)                | (7)        | (0.0)                |
| Total                                       | \$ (7,290)                    | (0.8)                | \$ (3,983) | (0.5)                |
| Earnings from operations:                   |                               |                      |            |                      |
| Aggregates                                  | \$ 156,916                    | 18.1                 | \$ 115,099 | 15.3                 |



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|                    |            |      |            |      |
|--------------------|------------|------|------------|------|
| Specialty Products | 13,989     | 18.0 | 4,208      | 6.9  |
| Total              | \$ 170,905 | 18.1 | \$ 119,307 | 14.6 |

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The following tables present volume and pricing data and shipments data for heritage operations, acquisitions and discontinued operations. Heritage aggregates operations exclude acquisitions that were not included in prior-year operations for the comparable period and divestitures.

|   | Six Months Ended<br>June 30, 2006 |         |
|---|-----------------------------------|---------|
|   | Volume                            | Pricing |
| Volume/Pricing Variance <sup>(1)</sup>        |                                   |         |
| Heritage Aggregates Operations <sup>(2)</sup> | 2.1%                              | 13.2%   |
| Aggregates Segment <sup>(3)</sup>             | 1.5%                              | 13.1%   |

  

|   | Six Months Ended<br>June 30, |        |
|---|------------------------------|--------|
|   | 2006                         | 2005   |
| Shipments (tons in thousands)                 |                              |        |
| Heritage Aggregates Operations <sup>(2)</sup> | 97,560                       | 95,592 |
| Acquisitions                                  |                              |        |
| Divestitures <sup>(4)</sup>                   | 31                           | 538    |
| Aggregates Segment <sup>(3)</sup>             | 97,591                       | 96,130 |

(1) *Volume/pricing variances reflect the percentage increase from the comparable period in the prior year.*

(2) *Heritage aggregates operations exclude acquisitions that have not been included in prior-year operations for a full year and divestitures.*

(3) *Aggregates segment includes all acquisitions from the date of acquisition and divested operations through the dates of divestiture.*

(4) *Divestitures represent tons related to divested operations up to the dates of divestiture.*

**LIQUIDITY AND CAPITAL RESOURCES** Net cash provided by operating activities during the six months ended June 30, 2006 was \$113.9 million compared with \$108.7 million in the comparable period of 2005. Operating cash flow is generally from net earnings, before deducting depreciation, depletion and amortization, offset by working capital requirements. The increase in cash provided by operating activities for the first six months of 2006 as compared with the year-earlier period was primarily due to higher earnings and was partially offset by a larger increase in inventories. Additionally, in accordance with FAS 123(R), excess tax benefits attributable to stock-based compensation transactions are classified as a financing cash flow as compared with the pre-adoption presentation in operating cash inflows.

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Depreciation, depletion and amortization was as follows (amounts in millions):

|              | Six Months Ended<br>June 30, |         |
|--------------|------------------------------|---------|
|              | 2006                         | 2005    |
| Depreciation | \$ 62.4                      | \$ 63.1 |
| Depletion    | 2.2                          | 2.1     |
| Amortization | 2.0                          | 2.5     |
|              | \$ 66.6                      | \$ 67.7 |

The seasonal nature of the construction aggregates business impacts quarterly operating cash flow when compared with the year. Full year 2005 net cash provided by operating activities was \$317.8 million, compared with \$108.7 million in the first six months of 2005.

The Corporation has no required pension plan contribution for 2006. However, the Corporation is currently considering a contribution of up to \$23.0 million during the third quarter of 2006 depending on its then current cash position and an evaluation of alternative uses of available cash. Any such contribution would be fully tax deductible for tax year 2005.

First six months capital expenditures, exclusive of acquisitions, were \$157.7 million in 2006 and \$101.3 million in 2005. Capital expenditures increased during the first six months, when compared with the prior-year period, as the Corporation continued work on major plant expansion and efficiency projects. Comparable full-year capital expenditures were \$221.4 million in 2005. Full-year capital spending is expected to approximate \$260.0 million for 2006, including the Hunt Martin joint venture and exclusive of acquisitions.

During the first six months of 2006, the Corporation received repayment of a \$12.5 million note receivable related to the divestiture of its Houston asphalt operations. The Corporation continues to have a continuing financial interest in the Houston asphalt market via a supply agreement and therefore continues to include the divested locations in continuing operations.

During 2006, the Corporation continued its common stock repurchase plan through open-market purchases pursuant to authority granted by its Board of Directors. For the quarter ended June 30, 2006, the Corporation repurchased 500,000 shares at an aggregate cost of \$43.2 million. During the six months ended June 30, the Corporation repurchased 914,400 shares at an aggregate cost of \$83.2 million in 2006 compared with 1,339,200 shares at an aggregate cost of \$78.0 million in 2005. In February 2006, the Board of Directors authorized management to repurchase up to an additional 5.0 million shares of its common stock. At June 30, 2006, 5,190,800 shares of common stock were remaining under the Corporation's repurchase authorization.

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In June 2006, the Corporation extended the expiration date of its \$250,000,000 five-year revolving credit agreement (the Credit Agreement) by one year to June 30, 2011. No borrowings were outstanding under the Credit Agreement at June 30, 2006 or December 31, 2005.

During the third quarter of 2006, the Corporation's \$125.0 million 6.9% Notes, which will mature in August, 2007, will become a current obligation. Management currently intends to refinance the Notes.

Based on prior performance and current expectations, the Corporation's management believes that cash flows from internally generated funds and its access to capital markets are expected to continue to be sufficient to provide the capital resources necessary to fund the operating needs of its existing businesses, cover debt service requirements, and allow for payment of dividends in 2006.

The Corporation may be required to obtain additional levels of financing in order to fund certain strategic acquisitions, if any such opportunities arise. Currently, the Corporation's senior unsecured debt is rated BBB+ by Standard & Poor's and A3 by Moody's. The Corporation's commercial paper obligations are rated A-2 by Standard & Poor's and P-2 by Moody's. While management believes its credit ratings will remain at an investment-grade level, no assurance can be given that these ratings will remain at the above-mentioned levels.

ACCOUNTING CHANGES Accounting changes resulting from the adoption of new accounting standards that may potentially impact the Corporation are included in Note 11 to the Consolidated Financial Statements.

TRENDS AND RISKS The Corporation outlined the risks associated with its business in its Annual Report on Form 10-K for the year ended December 31, 2005, filed with the Securities and Exchange Commission on February 27, 2006. In July 2006, the Corporation was notified by the Internal Revenue Service that it will audit the consolidated federal income tax return of the Corporation for the year ended December 31, 2004. Management continues to evaluate its exposure to all operating risks on an ongoing basis.

OUTLOOK 2006 The outlook for the Aggregates segment for the remainder of 2006 is positive. For the full year 2006, management currently expects aggregates shipments volume to increase 2% to 4% and aggregates pricing to increase 11.5% to 13%. Further, management expects the Aggregates segment operating margin excluding freight and delivery revenues to increase approximately 300 basis points. The Magnesia Specialties business is expected to generate between \$30 million and \$32 million in pretax earnings. The Corporation continues to work on its goal of increasing revenues in the Structural Composite Products business to a level that will support breakeven operations. However, a \$7 million to \$9 million loss from operations is expected in 2006.

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With this backdrop, management currently expects net earnings per diluted share for the third quarter to range from \$1.70 to \$1.90 and the range for the year is \$5.30 to \$5.60, inclusive of \$0.05 to \$0.07 per diluted share for the initial expensing of stock options under FAS 123(R), *Share-Based Payment*.

**OTHER MATTERS** If you are interested in Martin Marietta Materials, Inc. stock, management recommends that, at a minimum, you read the Corporation's current Annual Report and 10-K, 10-Q and 8-K reports to the SEC over the past year. The Corporation's recent proxy statement for the annual meeting of shareholders also contains important information. These and other materials that have been filed with the SEC are accessible through the Corporation's web site at [www.martinmarietta.com](http://www.martinmarietta.com) and are also available at the SEC's web site at [www.sec.gov](http://www.sec.gov). You may also write or call the Corporation's Corporate Secretary, who will provide copies of such reports.

Investors are cautioned that all statements in this Quarterly Report that relate to the future involve risks and uncertainties, and are based on assumptions that the Corporation believes in good faith are reasonable but which may be materially different from actual results. Forward-looking statements give the investor our expectations or forecasts of future events. You can identify these statements by the fact that they do not relate only to historical or current facts. They may use words such as anticipate, estimate, expect, project, intend, plan, believe, and other words of meaning in connection with future events or future operating or financial performance. Any or all of our forward-looking statements here and in other publications may turn out to be wrong.

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Factors that the Corporation currently believes could cause actual results to differ materially from the forward-looking statements in this Quarterly Report on Form 10-Q include, but are not limited to, the level and timing of federal and state transportation funding, particularly in North Carolina, one of the Corporation's largest and most profitable states; levels of construction spending in the markets the Corporation serves, including the severity of declines in the residential construction market; unfavorable weather conditions, particularly the increase in hurricane activity predicted along the east coast of the United States; volatility of fuel costs, most notably diesel fuel and natural gas; continued increases in the cost of repair and supply parts; the costs of large-scale plant projects coming on line in 2006; transportation availability and costs in the Corporation's long-haul network, notably barge availability on the Mississippi River system and the availability of railcars and locomotive power to move trains to supply the Corporation's Texas and the Gulf Coast markets; continued strength in the steel industry markets served by the Corporation's Magnesia Specialties business; successful development and implementation of the structural composite technological process and commercialization of strategic products for specific market segments to generate earnings streams sufficient enough to support the recorded assets of the Structural Composite Products business; and other risk factors listed from time to time found in the Corporation's filings with the Securities and Exchange Commission. Other factors besides those listed here may also adversely affect the Corporation and may be material to the Corporation. The Corporation assumes no obligation to update any forward-looking statements.

INVESTOR ACCESS TO COMPANY FILINGS Shareholders may obtain, without charge, a copy of Martin Marietta Materials' Annual Report on Form 10-K, as filed with the Securities and Exchange Commission for the fiscal year ended December 31, 2005, by writing to:

Martin Marietta Materials, Inc.

Attn: Corporate Secretary

2710 Wycliff Road

Raleigh, North Carolina 27607-3033

Additionally, Martin Marietta Materials' Annual Report, press releases and filings with the Securities and Exchange Commission, including Forms 10-K, 10-Q, 8-K and 11-K, can generally be accessed via the Corporation's web site. Filings with the Securities and Exchange Commission accessed via the web site are available through a link with the Electronic Data Gathering, Analysis, and Retrieval ( EDGAR ) system. Accordingly, access to such filings is available upon EDGAR placing the related document in its database. Investor relations contact information is as follows:

Telephone: (919) 783-4660

Email: [investors@martinmarietta.com](mailto:investors@martinmarietta.com)

Web site address: [www.martinmarietta.com](http://www.martinmarietta.com)

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

The Corporation's operations are highly dependent upon the interest rate-sensitive construction and steelmaking industries. Consequently, these marketplaces could experience lower levels of economic activity in an environment of rising interest rates or escalating costs. Since June 30, 2004, the Federal Reserve Board has increased the federal funds rate from 1.00% to 5.25% at June 30, 2006. This increase could affect the residential construction market, which accounted for approximately 20 percent of the Corporation's aggregates shipments in 2005. Aside from these inherent risks from within its operations, the Corporation's earnings are affected also by changes in short-term interest rates, as a result of its temporary cash investments, including money market funds and overnight investments in Eurodollars; any outstanding commercial paper obligations; and defined benefit pension plans. Additionally, the Corporation's earnings are affected by energy costs.

*Commercial Paper Obligations.* The Corporation has a \$250 million commercial paper program in which borrowings bear interest at a variable rate based on LIBOR. At June 30, 2006, there were outstanding commercial paper borrowings of \$10 million. As commercial paper borrowings bear interest at a variable rate, the Corporation has interest rate risk. The effect of a hypothetical 1% increase in interest rates on borrowings of \$10 million would increase interest expense by \$100,000 on an annual basis.

*Pension Expense.* The Corporation's results of operations are affected by its pension expense. Assumptions that affect this expense include the discount rate and, for the defined benefit pension plans only, the expected long-term rate of return on assets. Therefore, the Corporation has interest rate risk associated with these factors. The impact of hypothetical changes in these assumptions on the Corporation's annual pension expense is discussed in the Corporation's Annual Report on Form 10-K for the year ended December 31, 2005, filed with the Securities and Exchange Commission on February 27, 2006.

*Energy Costs.* Energy costs, including diesel fuel, natural gas and liquid asphalt, represent significant production costs for the Corporation. Increases in these costs generally are tied to energy sector inflation. In 2005, energy costs increased significantly, with fuel price increases lowering earnings per diluted share by \$0.38. A hypothetical 10% change in the Corporation's energy prices in 2006 as compared with 2005, assuming constant volumes, would impact 2006 pretax earnings by approximately \$12 million.

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*Aggregate Risk for Interest Rates and Energy Sector Inflation.* The pension expense for 2006 is calculated based on assumptions selected at December 31, 2005. Therefore, interest rate risk in 2006 is limited to the potential effect related to outstanding commercial paper. Assuming outstanding commercial paper borrowings of \$10 million, the impact of a hypothetical increase in interest rates of 1% would increase interest expense and decrease pretax earnings by \$100,000. Additionally, a 10% change in energy costs would impact annual pretax earnings by \$12 million.

Item 4. Controls and Procedures

As of June 30, 2006, an evaluation was performed under the supervision and with the participation of the Corporation's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and the operation of the Corporation's disclosure controls and procedures. Based on that evaluation, the Corporation's management, including the Chief Executive Officer and Chief Financial Officer, concluded that the Corporation's disclosure controls and procedures were effective as of June 30, 2006.

There have been no other significant changes in the Corporation's internal controls or in other factors that could significantly affect the internal controls subsequent to June 30, 2006.

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PART II-OTHER INFORMATION

Item 1. Legal Proceedings.

Reference is made to *Part I. Item 3. Legal Proceedings* of the Martin Marietta Materials, Inc. Annual Report on Form 10-K for the year ended December 31, 2005.

Item 1A. Risk Factors.

Reference is made to *Part I. Item 1A. Risk Factors and Forward-Looking Statements* of the Martin Marietta Materials, Inc. Annual Report on Form 10-K for the year ended December 31, 2005.

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

## ISSUER PURCHASES OF EQUITY SECURITIES

| Period        |                | Total Number<br>of<br>Shares<br>Purchased | Average<br>Price<br>Paid per<br>Share<br>\$ | Total Number of<br>Shares<br>Purchased as Part<br>of<br>Publicly<br>Announced<br>Plans or Programs | Maximum<br>Number of<br>Shares that May<br>Yet be<br>Purchased Under<br>the<br>Plans or Programs |
|---------------|----------------|---|---|--|--|
| April 1, 2006 | April 30, 2006 |   |   |  | 5,690,798  |
| May 1, 2006   | May 31, 2006   | 120,000                                   | \$ 90.06                                    | 120,000  | 5,570,798  |
| June 1, 2006  | June 30, 2006  | 380,000                                   | \$ 85.21                                    | 380,000  | 5,190,798  |
| Total         |                | 500,000                                   | \$ 86.37                                    | 500,000  | 5,190,798  |

The Corporation's initial stock repurchase program, which authorized the repurchase of 2.5 million shares of common stock, was announced in a press release dated May 6, 1994, and has been updated as appropriate. On February 22, 2006, the Corporation's Board of Directors authorized the repurchase of an additional 5.0 million shares of common stock. The program does not have an expiration date.

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

At the Annual Meeting of Shareholders held on May 23, 2006, the shareholders of Martin Marietta Materials, Inc.:

- (a) Elected David G. Maffucci, William E. McDonald, Frank H. Menaker, Jr. and Richard A. Vinroot to the Board of Directors of the Corporation to terms expiring at the Annual Meeting of Shareholders in the year 2009. The following table sets forth the votes for each director.

|                       | Votes Cast For | Withheld   |
|-----------------------|----------------|------------|
| David G. Maffucci     | 41,654,155     | 222,396    |
| William E. McDonald   | 41,472,059     | 404,492    |
| Frank H. Menaker, Jr. | 40,992,169     | 884,382    |
| Richard A. Vinroot    | 26,463,868     | 15,412,683 |

- (b) Ratified the amendments to the Stock-Based Award Plan. The voting results for this ratification were 35,268,725 *For*; 2,564,376 *Against*; and 43,813 *Abstained*.

- (c) Ratified the selection of Ernst & Young LLP as independent auditors for the year ending December 31, 2006. The voting results for this ratification were 41,474,464 *For*; 393,072 *Against*; and 9,013 *Abstained*.

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(Continued)

Item 6. Exhibits.

| Exhibit No. | Document  |
|-------------|---|
| 10.01       | Amended and Restated Stock-Based Award Plan dated April 3, 2006   |
| 10.02       | Amended and Restated Consulting Agreement dated June 26, 2006, between Janice Henry and Martin Marietta Materials Inc.  |
| 10.03       | Extension Agreement to \$250,000,000 Five-Year Credit Agreement dated as of June 2, 2006 among Martin Marietta Materials, Inc., the bank parties thereto, and JPMorgan Chase Bank, N.A., as Administrative Agent                    |
| 31.01       | Exhibit Regulation FD Disclosure Written Statement dated August 1, 2006 of Chief Executive Officer pursuant to Securities and Exchange Act of 1934 rule 13a-14 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 31.02       | Exhibit Regulation FD Disclosure Written Statement dated August 1, 2006 of Chief Financial Officer pursuant to Securities and Exchange Act of 1934 rule 13a-14 as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 |
| 32.01       | Additional Exhibit Regulation FD Disclosure Written Statement dated August 1, 2006 of Chief Executive Officer required by 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                      |
| 32.02       | Additional Exhibit Regulation FD Disclosure Written Statement dated August 1, 2006 of Chief Financial Officer required by 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002                      |

SIGNATURES

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

MARTIN MARIETTA  
MATERIALS, INC.  
(Registrant)

Date: August 1, 2006

By: /s/ ANNE H. LLOYD

Anne H. Lloyd  
Senior Vice President and  
Chief Financial Officer  
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