TERADYNE, INC
Form 10-Q
November 09, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2007

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 No. 001-06462

TERADYNE, INC.

(Exact name of registrant as specified in its charter)

Massachusetts	**04-2272148**
(State or Other Jurisdiction of Incorporation or Organization)	**(I.R.S. Employer Identification No.)**

600 Riverpark Drive, North Reading, Massachusetts **01864**
(Address of Principal Executive Offices) **(Zip Code)**
978-370-2700

(Registrant s Telephone Number, Including Area Code)

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

The number of shares outstanding of the registrant s only class of Common Stock as of November 2, 2007 was 173,640,993 shares.

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PART I

Item 1: Financial Statements

TERADYNE, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(unaudited)

	September 30, 2007	December 31, 2006
	(in thousands, except per share data)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 429,078	$ 568,025
Marketable securities	187,176	47,766
Accounts receivable, net of allowance for doubtful accounts of $4,757 and $4,962 on September 30, 2007 and December 31, 2006, respectively	231,561	155,770
Inventories:		
Parts	38,344	42,152
Assemblies in process	53,508	50,661
	91,852	92,813
Prepayments and other current assets	31,345	21,527
Current assets of discontinued operations		3,509
Total current assets	971,012	889,410
Property, plant, and equipment, at cost	821,849	862,062
Less: accumulated depreciation	470,137	496,541
Net property, plant, and equipment	351,712	365,521
Marketable securities	131,409	328,827
Goodwill	69,147	69,147
Intangible and other assets	36,622	35,819
Retirement plans assets	36,400	31,503
Long-term assets of discontinued operations		828
Total assets	$ 1,596,302	$ 1,721,055
LIABILITIES		
Current liabilities:		
Accounts payable	$ 64,516	$ 39,918
Accrued employees compensation and withholdings	65,188	87,811
Deferred revenue and customer advances	38,711	44,053
Other accrued liabilities	48,375	47,023
Income taxes payable	5,262	36,052
Current liabilities of discontinued operations		4,859
Total current liabilities	222,052	259,716
Retirement plans liabilities	83,736	81,121
Long-term other accrued liabilities	21,071	18,352
Long-term liabilities of discontinued operations		679
Total liabilities	326,859	359,868

Commitments and contingencies (Note O)		
SHAREHOLDERS EQUITY		
Common stock, $0.125 par value, 1,000,000 shares authorized, 177,817 and 188,952 shares issued and outstanding at September 30, 2007 and December 31, 2006, respectively	22,227	23,619
Additional paid-in capital	1,136,748	1,179,015
Accumulated other comprehensive loss	(57,065)	(66,309)
Retained earnings	167,533	224,862
Total shareholders equity	1,269,443	1,361,187
Total liabilities and shareholders equity	$ 1,596,302	$ 1,721,055

The accompanying notes, together with the Notes to Consolidated Financial Statements included in Teradyne s Annual Report on Form 10-K for the year ended December 31, 2006 are an integral part of the condensed consolidated financial statements.

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TERADYNE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(unaudited)

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
	(in thousands, except per share amounts)			
Net revenues:				
Products	$ 239,299	$ 294,838	$ 663,435	$ 919,846
Services	60,162	59,879	178,429	177,719
Total net revenues	299,461	354,717	841,864	1,097,565
Cost of revenues:				
Cost of products	117,268	142,301	329,597	451,123
Cost of services	37,947	38,031	117,404	114,348
Total cost of revenues	155,215	180,332	447,001	565,471
Gross profit	144,246	174,385	394,863	532,094
Operating expenses:				
Engineering and development	52,245	51,791	153,924	154,193
Selling and administrative	62,870	70,452	188,642	214,789
In-process research and development			16,700	
Restructuring and other, net	(3,119)	(15,112)	(304)	(36,806)
Operating expenses	111,996	107,131	358,962	332,176
Operating income from continuing operations	32,250	67,254	35,901	199,918
Interest income	7,784	12,453	27,182	33,595
Interest expense	(119)	(3,518)	(629)	(10,359)
Other income			1,832	
Income from continuing operations before income taxes	39,915	76,189	64,286	223,154
Provision for income taxes	4,717	9,866	9,556	27,874
Income from continuing operations	35,198	66,323	54,730	195,280
Income (loss) from discontinued operations before income taxes	6,084	(1,908)	6,795	(3,623)
Income tax provision	293	3,850	518	3,774
Income (loss) from discontinued operations	5,791	(5,758)	6,277	(7,397)
Net income	$ 40,989	$ 60,565	$ 61,007	$ 187,883
Income from continuing operations per common share:				
Basic	$ 0.19	$ 0.34	$ 0.29	$ 0.99
Diluted	$ 0.19	$ 0.34	$ 0.29	$ 0.97

Net income per common share:

Basic	$ 0.22	$ 0.31	$ 0.33	$ 0.96
Diluted	$ 0.22	$ 0.31	$ 0.32	$ 0.94
Weighted average common shares basic	183,566	193,563	187,527	196,608
Weighted average common shares diluted	185,298	204,551	189,222	208,585

The accompanying notes, together with the Notes to Consolidated Financial Statements included in Teradyne s Annual Report on Form 10-K for the year ended December 31, 2006 are an integral part of the condensed consolidated financial statements.

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TERADYNE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited)

	For the Nine Months Ended	
	September 30, 2007	October 1, 2006
	(in thousands)	
Cash flows from operating activities:		
Net income	$ 61,007	$ 187,883
Income (loss) from discontinued operations	381	(7,397)
Gain on sale from discontinued operations	5,896	
Income from continuing operations	54,730	195,280
Adjustments to reconcile income from continuing operations to net cash provided by operating activities:		
Depreciation	45,351	51,836
Amortization	5,902	3,866
Stock-based compensation	19,645	17,599
In-process research and development charge	16,700	
Gain on sale of land and building	(3,597)	(38,319)
Gain on sale of product lines	(906)	(406)
Provision for doubtful accounts	104	104
Provision for inventory	942	11,237
Other non-cash items, net	786	2,981
Changes in operating assets and liabilities, net of product lines and businesses sold:		
Accounts receivable	(75,896)	(5,742)
Inventories	27,261	66,797
Other assets	(17,638)	4,274
Accounts payable, deferred revenue and accrued expenses	2,900	33,068
Retirement plans contributions	(2,128)	(25,300)
Income taxes payable	(30,790)	25,105
Net cash provided by continuing operations	43,366	342,380
Net cash used for discontinued operations	(3,103)	(477)
Net cash provided by operating activities	40,263	341,903
Cash flows from investing activities:		
Investments in property, plant and equipment	(63,788)	(82,353)
Acquisition of technology	(17,600)	
Proceeds from sale of product lines	906	406
Proceeds from sale of land and building	7,888	79,220
Purchases of available-for-sale marketable securities	(333,165)	(372,570)
Proceeds from sale and maturities of available-for-sale marketable securities	396,436	578,999
Net cash (used for) provided by continuing operations	(9,323)	203,702
Net cash provided by (used for) discontinued operations	10,765	(317)
Net cash provided by investing activities	1,442	203,385

Cash flows from financing activities:		
Payments of long term debt and notes payable		(43,648)
Repurchase of common stock	(203,562)	(109,312)
Issuance of common stock under employee stock option and stock purchase plans	22,910	22,006
Net cash used for financing activities	(180,652)	(130,954)
(Decrease)/increase in cash and cash equivalents	(138,947)	414,334
Cash and cash equivalents at beginning of period	568,025	340,699
Cash and cash equivalents at end of period	$ 429,078	$ 755,033

The accompanying notes, together with the Notes to Consolidated Financial Statements included in Teradyne s Annual Report on Form 10-K for the year ended December 31, 2006 are an integral part of the condensed consolidated financial statements

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

A. The Company

Teradyne, Inc. is a leading supplier of automatic test equipment.

Teradyne s automatic test equipment offerings include:

Semiconductor test products and services (Semiconductor Test);

Circuit-board test and inspection products and services, military/aerospace instrumentation test products and services, and automotive diagnostic test products and services (Systems Test Group)

Statements in this Quarterly Report on Form 10-Q which are not historical facts, so called forward looking statements, are made pursuant to the safe harbor provisions of Section 21E of the Securities Exchange Act of 1934, as amended. Investors are cautioned that all forward looking statements involve risks and uncertainties, including those detailed in Teradyne s filings with the Securities and Exchange Commission (the SEC). See also Item 2: Management s Discussion and Analysis of Financial Condition and Results of Operations Certain Factors That May Affect Future Results and Teradyne s Annual Report on Form 10-K for the year ended December 31, 2006.

B. Accounting Policies

Basis of Presentation

The condensed consolidated interim financial statements include the accounts of Teradyne and its subsidiaries. All significant intercompany balances and transactions have been eliminated. These interim financial statements are unaudited and reflect all normal recurring adjustments that are, in the opinion of management, necessary for the fair statement of such interim financial statements. Certain prior years amounts were reclassified to conform to the current year presentation. The December 31, 2006 condensed consolidated balance sheet data were derived from audited financial statements, but do not include all disclosures required by generally accepted accounting principles.

The accompanying financial information should be read in conjunction with the consolidated financial statements and notes thereto contained in Teradyne s Annual Report on Form 10-K, filed with the SEC on March 1, 2007 for the year ended December 31, 2006.

On August 1, 2007, Teradyne completed the sale of Broadband Test Systems, its voice and broadband access network test division. The results of operations of Broadband Test Systems as well as balance sheet and cash flow amounts pertaining to this business have been classified as discontinued operations in the condensed consolidated financial statements (see Note E: Discontinued Operations).

Preparation of Financial Statements

The preparation of consolidated financial statements requires management to make estimates and judgments that affect the amounts reported in the financial statements. Actual results may differ significantly from these estimates.

C. Recently Issued Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 establishes a framework for measuring fair value and requires expanded disclosures regarding fair value measurements. This accounting standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. Teradyne is currently evaluating the impact of adopting this standard.

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

D. Product Warranty

Teradyne generally provides a one-year warranty on its products commencing upon installation or shipment. A provision is recorded upon revenue recognition to cost of revenues for estimated warranty expense based on historical experience. Related costs are charged to the warranty accrual as incurred. The balance below is included in other accrued liabilities (in thousands).

	For the Nine Months Ended	
	September 30, 2007	October 1, 2006
Balance at beginning of period	$ 12,897	$ 10,496
Accruals for warranties issued during the period	10,369	18,075
Accruals related to pre-existing warranties (includes changes in estimates)	(1,696)	(154)
Settlements made during the period	(11,530)	(12,742)
Balance at end of period	$ 10,040	$ 15,675

When Teradyne receives revenue for extended warranties beyond one year, it is deferred and recognized on a straight-line basis over the contract period. Related costs are expensed as incurred. The balance below is included in deferred revenue and customer advances and long-term other accrued liabilities (in thousands):

	For the Nine Months Ended	
	September 30, 2007	October 1, 2006
Balance at beginning of period	$ 8,350	$ 5,596
Deferral of new extended warranty revenue	2,550	5,142
Recognition of extended warranty deferred revenue	(4,204)	(2,224)
Balance at end of period	$ 6,696	$ 8,514

E. Discontinued Operations

On August 1, 2007, Teradyne completed the sale of its Broadband Test Systems division to Tollgrade Communications, Inc. for $11.3 million in cash. Teradyne sold this business as its growth potential as a stand-alone business within Teradyne was not attractive. The financial information for discontinued businesses has been reclassified to discontinued operations for all periods presented. Net revenues and income (loss) from discontinued operations for the three and nine months ended September 30, 2007 and October 1, 2006 are as follows (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Net revenues	$ 929	$ 4,405	$ 11,153	$ 16,106
(Loss) income from discontinued operations before income taxes	$ (198)	$ (1,908)	$ 513	$ (3,623)
Gain from sale of discontinued operations before income taxes	6,282		6,282	
Income tax provision	293	3,850	518	3,774
Income (loss) from discontinued operations	$ 5,791	$ (5,758)	$ 6,277	$ (7,397)

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Included in the September 30, 2007 nine months discontinued operations are $0.9 million of fees directly related to the sale transaction between Teradyne and Tollgrade Communications Inc.

F. Stock-Based Compensation

During the nine months ended September 30, 2007, Teradyne granted restricted stock units to employees, executives and directors. The total number of shares granted was 2.0 million at the weighted average grant date fair value of $15.19. Awards granted to employees and executives vest in equal installments over four years. Awards granted to non-employee directors vest after one year. A significant number of awards granted to executive officers are performance-based restricted stock units. The amount of actual performance-based restricted stock units that will vest over four years is determined on or near the first anniversary of the grant.

G. Other Comprehensive Income

Other comprehensive income is calculated as follows for the three months ended (in thousands):

	For the Three Months Ended	
	September 30, 2007	October 1, 2006
Net income	$ 40,989	$ 60,565
Foreign currency translation adjustments	(272)	1,038
Change in unrealized loss on foreign exchange contracts, net of tax of $0	(55)	
Change in unrealized loss on marketable securities, net of tax of $0	2,047	4,974
Retirement plans net gain, net of tax of $(13)	861	
Retirement plans net prior service gain, net of tax of $0	153	
Retirement plans net transition asset, net of tax of $(28)	29	
Additional minimum pension liability, net of tax of $0		(130)
Other comprehensive income	$ 43,752	$ 66,447

Other comprehensive income is calculated as follows for the nine months ended (in thousands):

	For the Nine Months Ended	
	September 30, 2007	October 1, 2006
Net income	$ 61,007	$ 187,883
Foreign currency translation adjustments	(38)	1,746
Change in unrealized loss on foreign exchange contracts, net of tax of $0		(31)
Change in unrealized loss on marketable securities, net of tax of $0	4,212	2,303
Retirement plans net gain, net of tax of $47	4,605	

Retirement plans net prior service gain, net of tax of $0	460	
Retirement plans net transition asset, net of tax of $(47)	5	
Additional minimum pension liability, net of tax of $0		(342)
Other comprehensive income	$ 70,251	$ 191,559

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

H. Intangible Assets

Amortizable intangible assets consist of the following and are included in intangible and other assets on the balance sheet (in thousands):

	September 30, 2007			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Useful Life
Completed technology	$ 19,193	$ 15,206	$ 3,987	7.5 years
Service and software maintenance contracts and customer relationships	4,779	3,528	1,251	8 years
Trade names and trademarks	3,800	2,810	990	8 years
Acquired workforce	700	88	612	4 years
Total intangible assets	$ 28,472	$ 21,632	$ 6,840	7.6 years

	December 31, 2006			
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Weighted Average Useful Life
Completed technology	$ 19,193	$ 13,281	$ 5,912	7.5 years
Service and software maintenance contracts and customer relationships	4,779	3,078	1,701	8.0 years
Trade names and trademarks	3,800	2,454	1,346	8.0 years
Total intangible assets	$ 27,772	$ 18,813	$ 8,959	7.7 years

Aggregate amortization expense was $1.0 million for the three months ended September 30, 2007 and $0.9 million for the three months ended October 1, 2006. Aggregate amortization expense for the nine months ended September 30, 2007 was $2.8 million and for the nine months ended October 1, 2006 was $2.7 million. Estimated amortization expense for each of the five succeeding fiscal years is as follows (in thousands):

Year	Amount
2007 (remainder)	$ 840
2008	3,137
2009	2,644
2010	175
2011	44

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

I. Net Income per Common Share

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

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Income from continuing operations	$ 35,198	$ 66,323	$ 54,730	$ 195,280
Income (loss) from discontinued operations	5,791	(5,758)	6,277	(7,397)
Net income for basic net income per share	40,989	60,565	61,007	187,883
Income impact of assumed conversion of convertible debt		2,562		7,945
Net income for diluted net income per share	$ 40,989	$ 63,127	$ 61,007	$ 195,828
Weighted average common shares basic	183,566	193,563	187,527	196,608
Effect of dilutive securities:				
Incremental shares from assumed conversion of convertible debentures		10,367		10,873
Employee and director stock options	858	235	991	748
Restricted stock units	837	361	647	303
Employee stock purchase rights	37	25	57	53
Dilutive potential common shares	1,732	10,988	1,695	11,977
Weighted average common shares diluted	185,298	204,551	189,222	208,585
Net income per common share basic				
Continued operations	$ 0.19	$ 0.34	$ 0.29	$ 0.99
Discontinued operations	0.03	(0.03)	0.04	(0.03)
	$ 0.22	$ 0.31	$ 0.33	$ 0.96
Net income per common share diluted				
Continued operations	$ 0.19	$ 0.34	$ 0.29	$ 0.97
Discontinued operations	0.03	(0.03)	0.03	(0.03)
	$ 0.22	$ 0.31	$ 0.32	$ 0.094

The computation of diluted net income per common share for the three and nine months ended September 30, 2007 excludes the effect of the potential exercise of options to purchase approximately 14.1 million and 14.1 million shares, respectively, because the option price was greater than the average market price of the common shares and the effect would have been anti-dilutive.

The computation of diluted net income per common share for the three and nine months ended October 1, 2006 excludes the effect of the potential exercise of options to purchase approximately 15.9 million and 16.0 million shares, respectively, because the option price was greater than the average market price of the common shares and the effect would have been anti-dilutive. The effect of Teradyne s outstanding convertible notes on diluted net income per share for the three and nine months ended October 1, 2006 was calculated using the if converted method as required by SFAS No. 128, Earnings per Share . In using the if converted method, $2.6 million and $7.9 million of interest expense related to the convertible notes for the three and nine

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

months ended October 1, 2006, net of tax and profit sharing expenses, was added back to net income to arrive at diluted net income. Accordingly, 10.4 million and 10.9 million incremental shares from the assumed conversion of the convertible debt are added to shares when calculating diluted net income per common share for the three and nine months ended October 1, 2006, respectively.

J. Restructuring and Other, Net

The tables below represent activity related to restructuring and other, net, in the nine months ended September 30, 2007. The accrual for severance and benefits is reflected in accrued employees compensation and withholdings. The accrual for lease payments on vacated facilities is reflected in other accrued liabilities and long-term other accrued liabilities and is expected to be paid out over the lease terms, the latest of which expires in 2012. Teradyne expects to pay out approximately $1.7 million against the lease accruals over the next twelve months. Teradyne s future lease commitments are net of expected sublease income of $10.3 million as of September 30, 2007.

2007 Activities

(in thousands)	Gain on Sale of Real Estate	Insurance Recovery	Vacated Facility Related	Severance and Benefits	Total
Balance at December 31, 2006	$	$	$	$	$
(Credits)/charges	(3,597)	(1,782)	53	6,417	1,091
Cash receipts/(payments)	3,597	1,782	(53)	(3,593)	1,733
Balance at September 30, 2007	$	$	$	$ 2,824	$ 2,824

During the nine months ended September 30, 2007, Teradyne recorded the following restructuring activities:

- $6.4 million of severance charges related to headcount reductions of 196 people across all functions and segments;
- $3.6 million gain on the sale of land and building in Deerfield, Illinois; and
- $1.8 million of cash proceeds recovered from insurance related to a facility fire in Taiwan.

2006 Activities

(in thousands)	Vacated Facility Related	Severance and Benefits	Total
Balance at December 31, 2006	$ 625	$ 1,865	$ 2,490
Credits		(135)	(135)
Cash payments	(444)	(1,635)	(2,079)

Balance at September 30, 2007	$ 181	$ 95	$ 276

TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Pre-2006 Activities

(in thousands)	Vacated Facility Related	Severance and Benefits	Gain on Sale of Product Lines	Total
Balance at December 31, 2006	$ 9,604	$ 1,183	$	$ 10,787
Credits	(69)	(285)	(906)	(1,260)
Cash (payments)/receipts	(2,705)	(648)	906	(2,447)
Balance at September 30, 2007	$ 6,830	$ 250	$	$ 7,080

During the nine months ended September 30, 2007, Teradyne recorded the following pre-2006 restructuring activities:

$0.9 million credit for earn-out payments received in the Systems Test Group from a product line divestiture; and

$0.3 million credit for revised estimates on severance payments.

K. Stock Repurchase Program

In July 2006, Teradyne s Board of Directors authorized a stock repurchase program. Under the program, Teradyne could spend up to an aggregate of $400 million to repurchase shares of its common stock in open market purchases, in privately negotiated transactions or through other appropriate means over two years. Shares were to be repurchased at Teradyne s discretion, subject to market conditions and other factors. During the three months ended September 30, 2007, Teradyne repurchased 11.4 million shares of common stock for $176.0 million at an average price of $15.38 per share. For the nine months ended September 30, 2007, Teradyne repurchased 13.1 million shares of common stock for $203.6 million at an average price of $15.52 per share. During October, 2007 Teradyne completed the $400 million stock repurchase program, repurchasing a cumulative total of 27.9 million shares of common stock at an average price of $14.31 per share.

On November 7, 2007, Teradyne s Board of Directors authorized a new stock repurchase program. Under the program, the Company is permitted to spend an aggregate of $400 million to repurchase shares of its common stock in open market purchases, in privately negotiated transactions or through other means. Shares are to be repurchased at the Company s discretion, subject to market conditions and other factors

L. Technology Acquisition

On March 7, 2007, Teradyne purchased in-process enabling test technology and hired certain engineers from MOSAID Technologies Inc. for $17.6 million, which includes $0.6 million in fees directly related to the acquisition. Of the purchase price, $16.7 million has been allocated to in-process research and development and therefore was immediately charged to the statement of operations. The balance of the purchase price was allocated to acquired workforce and fixed assets.

This technology was acquired for use in the development of a new semiconductor test product. As of the acquisition date, the technology had not reached technical feasibility, had no alternative future use and its fair value was estimable with reasonable reliability, and therefore was classified as in-process research and development. The technology is unique to the semiconductor test market and requires significant development. The estimated fair value of the in-process technology was determined based on the use of a discounted cash flow model using an income approach. Estimated cash flows were probability adjusted to take into account the stage of completion and the risks surrounding successful development and commercialization of the in-process

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

technology. Such a valuation requires significant estimates and assumptions including but not limited to determining the timing and estimated costs to complete the in-process project as well as the estimated cash flows to be generated as a result of completing the project development.

M. Retirement Plans

Defined Benefit Pension Plans

Teradyne has defined benefit pension plans covering a portion of U.S. employees and employees of certain non-U.S. subsidiaries. Benefits under these plans are based on employees years of service and compensation. Teradyne s funding policy is to make contributions to the plans in accordance with local laws and to the extent that such contributions are tax deductible. The assets of the plans consist primarily of equity and fixed income securities. In addition, Teradyne has an unfunded supplemental executive defined benefit plan in the United States to provide retirement benefits in excess of levels allowed by the Employment Retirement Income Security Act and the Internal Revenue Code, as well as unfunded foreign plans.

Components of net periodic pension cost for all plans for the three and nine months ended September 30, 2007 and October 1, 2006 are as follows (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Net Periodic Benefit Cost:				
Service cost	$ 1,387	$ 1,643	$ 4,197	$ 4,892
Interest cost	4,133	3,834	12,407	11,468
Expected return on plan assets	(4,866)	(4,282)	(14,629)	(12,826)
Amortization of unrecognized:				
Net transition obligation	(17)	(15)	(49)	(43)
Prior service cost	212	208	635	623
Net loss	905	1,479	2,727	4,425
Total expense	$ 1,754	$ 2,867	$ 5,288	$ 8,539

Teradyne contributed $1.1 million to its U.K. pension plan and $0.9 million to its Japan pension plan in the nine months ended September 30, 2007.

Postretirement Benefit Plans

In addition to receiving pension benefits, Teradyne s U.S. employees who meet specific retirement eligibility requirements as of their termination dates may participate in Teradyne s Welfare Plan, which includes death benefits, and medical and dental benefits up to age 65. Death benefits provide a fixed sum to retirees survivors and are available to all retirees. Substantially all of Teradyne s current U.S. employees could become eligible for these benefits, and the existing benefit obligation relates primarily to those employees.

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Components of net periodic postretirement cost are as follows (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Net Periodic Benefit Cost:				
Service cost	$ 63	$ (3)	$ 190	$ 186
Interest cost	329	229	986	1,046
Amortization of unrecognized:				
Prior service cost	(58)	(60)	(176)	(173)
Net loss (gain)	71	(70)	214	409
Total expense	$ 405	$ 96	$ 1,214	$ 1,468

N. Income Taxes

Teradyne adopted FIN 48, Accounting for Uncertainties in Income Taxes (FIN 48) effective January 1, 2007. FIN 48 applies to all income tax positions accounted for under FASB Statement No. 109, Accounting for Income Taxes , and addresses the determination of whether tax benefits claimed or expected to be claimed on a tax return should be recorded in the financial statements. FIN 48 also addressed other aspects of reporting and disclosing uncertain tax positions. Upon adoption, the amount of unrecognized tax benefits, if recognized, would have impacted the effective tax rate by $2.5 million. Upon adoption, it was anticipated that within the next twelve months of adoption $2.3 million of unrecognized tax benefits would no longer be considered unrecognized tax benefits due to audit settlements. Upon adoption and as of September 30, 2007, Teradyne has open tax years beginning in 2003 for major jurisdictions including U.S., Japan, Singapore and the United Kingdom. Teradyne records all interest and penalties related to income taxes as a component of income tax expense. Accrued interest and penalties related to income tax items upon adoption and recognized during the three and nine months ended September 30, 2007 was not material.

Teradyne s unrecognized tax benefits are as follows (in thousands):

	For the Nine Months Ended September 30, 2007
Beginning balance, upon adoption as of January 1, 2007	$ 10,584
Additions:	
Tax positions for current year	126
Tax positions for prior years	2,013
Ending balance as of April 1, 2007	$ 12,723
Additions:	
Tax positions for current year	37
Tax positions for prior years	2,407
Reductions:	
Settlements	(2,342)

Ending balance as of July 1, 2007	$	12,825
Additions:		
Tax positions for current year		202
Tax positions for prior years		204
Ending balance as of April 1, 2007	$	13,231

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Of the $13.2 million of unrecognized tax benefits as of September 30, 2007, $6.8 million would impact the consolidated income tax rate if ultimately recognized. The remaining $6.4 million would impact goodwill if ultimately recognized. As of September 30, 2007, it is anticipated that within the next twelve months, $2.0 million of unrecognized tax benefits will no longer be considered unrecognized tax benefits due to audit settlements.

Due to the continued uncertainty of realization of our U.S. deferred tax assets, Teradyne maintained its valuation allowance at September 30, 2007 and December 31, 2006. Teradyne does not expect to significantly reduce its valuation allowance until sufficient positive evidence exists, including sustained profitability, that realization is more likely than not.

O. Commitments and Contingencies

Legal Claims

On September 5, 2001, after Teradyne s August 2000 acquisition of Herco Technology Corp. and Perception Laminates, Inc., the former owners of those companies filed a complaint against Teradyne and two of its then executive officers in the Federal District Court in San Diego, California, asserting securities fraud and breach of contract related to the acquisition. The District Court dismissed certain of the plaintiffs claims, granted partial summary judgment against them with respect to their breach of contract claim and denied their motion for reconsideration. In July 2007, after an appeal by the plaintiffs, the U.S. Court of Appeals for the Ninth Circuit affirmed in part and reversed in part the District Court rulings. Teradyne petitioned the Ninth Circuit for rehearing of the ruling it reversed. In October 2007, the Ninth Circuit denied Teradyne s petition for rehearing. Teradyne will continue to defend the claim that was sent back to the District Court.

In 2001, Teradyne was designated as a Potentially Responsible Party (PRP) at a clean-up site in Los Angeles, California. This claim arose out of its acquisition of Perception Laminates in August 2000. Prior to that date, Perception Laminates had itself acquired certain assets of Alco Industries Inc. under an asset purchase agreement dated October 20, 1992. Neither Teradyne nor Perception Laminates has ever conducted any operations at the Los Angeles site. Teradyne has asked the State of California to drop the PRP designation, but California has not yet agreed to do so.

Teradyne believes that it has meritorious defenses against the above unsettled claims and intends to vigorously contest them. While it is not possible to predict or determine the outcomes of the unsettled claims or to provide possible ranges of losses that may arise, Teradyne believes the losses associated with all of these actions will not have a material adverse effect on its consolidated financial position or liquidity, but could possibly be material to its consolidated results of operations of any one period.

In addition, Teradyne is subject to legal proceedings, claims and investigations that arise in the ordinary course of business such as, but not limited to, patent, employment, commercial and environmental matters. Although there can be no assurance, there are no such matters pending that Teradyne expects to be material with respect to its business, financial position or results of operations.

P. Segment Information

Teradyne s two reportable segments are Semiconductor Test and Systems Test Group. The Semiconductor Test segment includes operations related to the design, manufacturing and marketing of semiconductor test products and services. The Systems Test Group segment includes operations related to the design, manufacturing and marketing of circuit-board test and inspection products and services, military/aerospace instrumentation test products and services, and automotive diagnostic and test products and services.

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

During the third quarter of 2007, the internal management reporting of the Company changed to better align with the company s operational management structure, resulting in a change in the Company s reportable segments. Segment reporting has been restated for all periods presented to reflect this change. The reportable segments presented reflect the information reviewed and used by the chief operating decision maker.

Teradyne evaluates performance based on several factors, of which the primary financial measure is business segment income from continuing operations before taxes. The accounting policies of the business segments are the same as those described in Note B: Accounting Policies in Teradyne s Annual Report on Form 10-K for the year ended December 31, 2006. Due to the sale on August 1, 2007 of Broadband Test Systems, its results have been excluded from segment reporting and included in discontinued operations for all periods presented. Previously, Broadband Test Systems and Diagnostic Solutions had been combined to form the Other Test Systems segment. Diagnostic Solutions and Assembly Test are now components of the Systems Test Group segment. Segment information for the three and nine months ended September 30, 2007 and October 1, 2006 is as follows (in thousands):

	Semiconductor Test	Systems Test Group	Corporate and Eliminations	Consolidated
Three months ended September 30, 2007:				
Net revenues	$ 243,470	$ 55,991	$	$ 299,461
Income from continuing operations before taxes (1)(2)	24,507	3,623	11,785	39,915
Total assets (3)	572,004	228,099	796,199	1,596,302
Three months ended October 1, 2006:				
Net revenues	$ 282,776	$ 71,941	$	$ 354,717
Income from continuing operations before taxes (1)(2)	63,246	6,437	6,506	76,189
Total assets (3)	563,671	256,423	1,148,331	1,968,425
Nine months ended September 30, 2007:				
Net revenues	$ 668,118	$ 173,746	$	$ 841,864
Income from continuing operations before taxes (1)(2)	18,119	13,075	33,092	64,286
Nine months ended October 1, 2006:				
Net revenues	$ 892,284	$ 205,281	$	$ 1,097,565
Income from continuing operations before taxes (1)(2)	185,750	18,145	19,259	223,154

(1) Net interest income is included in Corporate and Eliminations.

(2) Included in the income from continuing operations before taxes for each of the segments are charges for the three and nine months ended September 30, 2007 and October 1, 2006 that include restructuring and other, net and in-process research and development charges, as follows:

(3) Total business assets are directly attributable to each business. Corporate assets consist of cash and cash equivalents, marketable securities, unallocated fixed assets of support divisions and common facilities and certain other assets.

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Included in the Semiconductor Test segment are charges for the following (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Restructuring and other, net	$ (830)	$ (16,261)	$ 1,742	$ (35,699)
In-process research and development			16,700	
Total	$ (830)	$ (16,261)	$ 18,442	$ (35,699)

Also included in income from continuing operations before taxes for the nine months ended September 30, 2007 is an inventory provision of $0.5 million related to non-FLEX products.

Included in the Systems Test Group are charges for the following (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Restructuring and other, net	$ 1,351	$ 427	$ 1,055	$ (1,311)

Included in the Corporate and Eliminations segment are charges for the following (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Restructuring and other, net	$ (3,640)	$ 722	$ (3,101)	$ 204

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

Critical Accounting Policies and Estimates

We have identified the policies which are critical to understanding our business and our results of operations. Management believes that there have been no significant changes during the nine months ended September 30, 2007 to the items disclosed as our critical accounting policies and estimates in Management s Discussion and Analysis of Financial Condition and Results of Operations in its Annual Report on Form 10-K for the fiscal year ended December 31, 2006.

SELECTED RELATIONSHIPS WITHIN THE CONDENSED CONSOLIDATED

STATEMENTS OF OPERATIONS

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Percentage of total net revenues:				
Products	80%	83%	79%	84%
Services	20	17	21	16
Total net revenues	100	100	100	100
Cost of revenues:				
Cost of products	39	40	39	41
Cost of services	13	11	14	10
Total cost of revenues	52	51	53	51
Gross profit	48	49	47	49
Operating expenses:				
Engineering and development	17	14	18	14
Selling and administrative	21	20	23	20
In-process research and development			2	
Restructuring and other, net	(1)	(4)	0	(3)
Operating expenses	37	30	43	31
Operating income from continuing operations	11	19	4	18
Interest income	3	3	3	3
Interest expense	(1)	(1)	(0)	(1)
Other income			0	
Income from continuing operations before income taxes	13	21	7	20
Provision for income taxes	1	2	1	2
Income from continuing operations	12	19	6	18
Income (loss) from discontinued operations before income taxes	2	(1)	1	(0)
Income tax provision	0	1	0	1

Income (loss) from discontinued operations	2	(2)	1	(1)
Net income	14%	17%	7%	17%
Provision for income taxes as a percentage of income from continuing operations before income taxes	12%	13%	15%	12%

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Results of Operations

On August 1, 2007, we closed the sale of our Broadband Test Systems division with Tollgrade Communications, Inc. for $11.3 million in cash. We sold this business as its growth potential as a stand-alone business within Teradyne was not attractive. The financial results of Broadband Test Systems have been reported as discontinued operations in the condensed consolidated financial statements for all periods presented throughout this Form 10-Q. Previously, Broadband Test Systems and Diagnostic Solutions had been combined to form the Other Test Systems segment. Diagnostic Solutions and Assembly Test are now components of Systems Test Group segment. Unless indicated otherwise, the discussion and amounts provided in this Results of Operations section and elsewhere in this Form 10-Q relate to continuing operations only.

Discontinued businesses net revenues and income (loss) for the three and nine months ended September 30, 2007 and October 1, 2006 are as follows (in thousands):

	For the Three Months Ended		For the Nine Months Ended	
	September 30, 2007	October 1, 2006	September 30, 2007	October 1, 2006
Net revenues	$ 929	$ 4,405	$ 11,153	$ 16,106
(Loss) income before income taxes	$ (198)	$ (1,908)	$ 513	$ (3,623)
Gain from sale of discontinued operations	6,282		6,282	
Income tax provision	293	3,850	518	3,774
Income (loss) from discontinued operations	$ 5,791	$ (5,758)	$ 6,277	$ (7,397)

Included in discontinued operations are $0.9 million fees directly related to the sale transaction between Teradyne and Tollgrade Communications, Inc.

Third Quarter 2007 Compared to Third Quarter 2006

Bookings

Net bookings for our two reportable segments were as follows (dollars in millions, except percent change):

	For the Three Months Ended		
	September 30, 2007	October 1, 2006	% Change
Semiconductor Test	$ 217.2	$ 182.3	19.1%
Systems Test Group	56.1	55.8	0.5%
	$ 273.3	$ 238.1	14.8%

Semiconductor Test orders increased 19.1% driven by more demand across a wide range of end markets, applications and geographies. Additionally, there was a mix shift compared to prior year with subcontractors making up a larger percentage of orders. Semiconductor Test business is dependent on the current and anticipated market for test equipment, which historically has been highly cyclical.

Systems Test Group increase in orders was primarily due to increased military/aerospace board test program-related bookings partially offset by a decrease in automotive test and commercial board test orders. Automotive test orders are program related and have significant fluctuations. The decrease in automotive test bookings was primarily due to a large program rollout in 2006 for the Vehicle Measurement Module product line.

Customers may delay delivery of products or cancel orders suddenly and without significant notice, subject to possible cancellation penalties. Due to possible changes in delivery schedules and cancellations of orders, our

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backlog at any particular date is not necessarily indicative of the actual sales for any succeeding period. Delays in delivery schedules and/or cancellations of backlog during any particular period could have a material adverse effect on our business, financial condition and results of operations.

Net bookings by region as a percentage of total net bookings were as follows:

	For the Three Months Ended	
	September 30, 2007	October 1, 2006
United States	22.5%	31.2%
South East Asia	19.1	18.5
Taiwan	15.2	6.8
Singapore	13.5	10.2
Europe	10.5	15.5
Japan	9.5	10.8
Korea	9.2	5.7
Rest of World	0.5	1.3
	100%	100%

Backlog of unfilled orders for our two reportable segments was as follows (dollars in millions):

	For the Three Months Ended	
	September 30, 2007	October 1, 2006
Semiconductor Test	$ 224.5	$ 207.1
Systems Test Group	93.0	100.9
	$ 317.5	$ 308.0

Revenue

Net revenues for our two reportable segments were as follows (dollars in millions, except percent changes):

	For the Three Months Ended		
	September 30, 2007	October 1, 2006	% Change
Semiconductor Test	$ 243.5	$ 282.8	(13.9)%
Systems Test Group	56.0	71.9	(22.1%)

	$ 299.5	$ 354.7	(15.6)%

The decrease in Semiconductor Test revenue is due to System-On-a-Chip (SOC) device units growing at a lower rate in 2007 compared to 2006. This resulted in decreased demand across a wide range of end markets, applications, and geographies.

The decrease in Systems Test Group revenue was due primarily to the large program rollout in 2006 for the Vehicle Measurement Module product line.

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Our sales by region as a percentage of total net sales were as follows:

	For the Three Months Ended	
	September 30, 2007	October 1, 2006
United States	19.3%	22.3%
South East Asia	17.2	17.8
Singapore	15.3	7.0
Europe	12.9	13.1
Korea	11.7	7.9
Japan	10.6	17.3
Taiwan	10.6	12.3
Rest of the World	2.4	2.3
	100%	100%

Gross Profit

Our gross profit was as follows (dollars in millions):

	For the Three Months Ended		
	September 30, 2007	October 1, 2006	Period Change
Gross Profit	$ 144.2	$ 174.4	$ (30.2)
Percent of Total Revenue	48.2%	49.2%	

Gross profit as a percentage of revenue decreased from the third quarter of 2006 to 2007 by 1.0 percentage point. Of the decrease, 2.0 points can be attributed to lower volume in Semiconductor Test offset in part by lower fixed costs and greater manufacturing efficiencies.

We assess the carrying value of our inventory on a quarterly basis by estimating future demand and comparing that demand against on-hand and on-order inventory provisions. Forecasted revenue information is obtained from the sales and marketing groups and incorporates factors such as backlog and future revenue demand. This quarterly process identifies obsolete and excess inventory. Obsolete inventory, which represents items for which there is no demand, is fully reserved. Excess inventory, which represents inventory items that are not expected to be consumed during the next four quarters, is written down to estimated net realizable value.

During the three months ended September 30, 2007 and October 1, 2006, we scrapped $3.0 million and $5.3 million of inventory, respectively, and sold $0.0 million and $0.7 million of previously written-down or written-off inventory, respectively. As of September 30, 2007, we have inventory related reserves for amounts which had been written-down or written-off totaling $127.5 million. We have no pre-determined timeline to scrap the remaining inventory.

Engineering and Development

Engineering and development expenses were as follows (dollars in millions):

	For the Three Months Ended		
	September 30, 2007	October 1, 2006	Period Change
Engineering and Development	$ 52.2	$ 51.8	$ 0.4
Percent of Total Revenue	17.4%	14.6%	

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The increase of $0.4 million in engineering and development expenses is due to an increase in Semiconductor Test spending related to entry into an adjacent market offset in part by a reduction in variable employee compensation expense in each segment.

Selling and Administrative

Selling and administrative expenses were as follows (dollars in millions):

	For the Three Months Ended		
	September 30, 2007	October 1, 2006	Period Change
Selling and Administrative	$ 62.9	$ 70.5	$ (7.6)
Percent of Total Revenue	21.0%	19.9%	

The decrease of $7.6 million from the third quarter of 2006 to 2007 is primarily the result of:

- a decrease of $5.4 million in transition expenses, including the consolidation of facilities in Massachusetts and costs associated with the outsourcing of certain information technology functions; and

- a decrease of $2.1 million in variable employee compensation.

Restructuring and Other, Net

The tables below represent activity related to restructuring and other, net, in the three months ended September 30, 2007. The accrual for severance and benefits is reflected in accrued employees compensation and withholdings. The accrual for lease payments on vacated facilities is reflected in other accrued liabilities and long-term other accrued liabilities and is expected to be paid out over the lease terms, the latest of which expires in 2012. We expect to pay out approximately $1.7 million against the lease accruals over the next twelve months. Our future lease commitments are net of expected sublease income of $10.3 million as of September 30, 2007.

2007 Activities

(in thousands)	Gain on Sale of Real Estate	Insurance Recovery	Severance and Benefits	Total
Balance at July 1, 2007	$	$	$ 2,249	$ 2,249
(Credits)/charges	(3,628)	(1,782)	2,285	(3,125)
Cash receipts/(payments)	3,628	1,782	(1,679)	3,731
Balance at September 30, 2007	$	$	$ 2,855	$ 2,855

During the three months ended September 30, 2007, we recorded the following 2007 restructuring activities:

- $3.6 million gain on the sale of land and building in Deerfield, Illinois;

- $1.8 million of cash proceeds recovered from insurance related to a facility fire in Taiwan; and

- $2.3 million of severance charges related to headcount reductions of 57 people across all functions and segments.

The restructuring actions taken during the three months ended September 30, 2007, are expected to generate quarterly cost savings of approximately $1.1 million.

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2006 Activities

(in thousands)	Vacated Facility Related	Severance and Benefits	Total
Balance at July 1, 2007	$ 335	$ 167	$ 502
Charges		6	6
Cash payments	(154)	(78)	(232)
Balance at September 30, 2007	$ 181	$ 95	$ 276

Pre-2006 Activities

(in thousands)	Vacated Facility Related	Severance and Benefits	Total
Balance at July 1, 2007	$ 7,353	$ 400	$ 7,753
Cash payments	(523)	(150)	(673)
Balance at September 30, 2007	$ 6,830	$ 250	$ 7,080

Interest Income and Expense

Interest income decreased to $7.8 million for the third quarter of 2007 from $12.5 million in the third quarter of 2006, due to lower cash balances primarily from the repayment of our 3.75% Convertible Notes (the Notes) in the fourth quarter of 2006 and stock repurchases made beginning in the second half of 2006. Interest expense decreased to $0.1 million in the third quarter of 2007 from $3.5 million in the third quarter of 2006, due primarily to the repayment of the Notes.

Income Taxes

The tax expense of $4.7 million and $9.9 million for the third quarter of 2007 and 2006, respectively consists primarily of foreign taxes. As a result of incurring significant operating losses from 2001 through 2003, we determined that it is more likely than not that our deferred tax assets may not be realized, and since the fourth quarter of 2002 we have established a full valuation allowance for our net deferred tax assets. If we generate sustained future taxable income against which these tax attributes may be applied, some portion or all of the valuation allowance would be reversed. If the valuation allowance were reversed, a portion would be recorded as an increase to additional paid in capital, and the remainder would be recorded as a reduction to income tax expense.

Nine Months of 2007 Compared to Nine Months of 2006

Bookings

Net bookings for our two reportable segments were as follows (in millions, except percent change):

	For the Nine Months Ended	Percent Change

	September 30, 2007	October 1, 2006	
Semiconductor Test	$ 679.2	$ 810.3	(16.2)%
Systems Test Group	146.7	189.0	(22.4)
	$ 825.9	$ 999.3	(17.4)%

Semiconductor Test orders decreased 16% driven by less demand across a wide range of end markets, applications and geographies, as SOC device units grew at a lower rate in 2007 than in 2006. Semiconductor Test business is dependent on the current and anticipated market for test equipment, which historically has been highly cyclical.

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Systems Test Group orders decreased 22% primarily due to a decrease in automotive test. Automotive test orders are program related and have significant fluctuations. The decrease in automotive test bookings was primarily due to a large program rollout in 2006 for the Vehicle Measurement Module product line.

Customers may delay delivery of products or cancel orders suddenly and without significant notice, subject to possible cancellation penalties. Due to possible changes in delivery schedules and cancellations of orders, our backlog at any particular date is not necessarily indicative of the actual sales for any succeeding period. Delays in delivery schedules and/or cancellations of backlog during any particular period could have a material adverse effect on our business, financial condition and results of operations.

Net bookings by region as a percentage of total net bookings were as follows:

	For the Nine Months Ended	
	September 30, 2007	October 1, 2006
United States	20.4%	25.0%
Taiwan	17.0	12.3
Singapore	15.1	12.0
South East Asia	16.3	17.4
Japan	11.0	12.5
Europe	10.6	13.4
Korea	8.8	6.4
Rest of the World	0.8	1.0
	100%	100%

Revenue

Net revenues for our two reportable segments were as follows (in millions, except percent changes):

	For the Nine Months Ended		
	September 30, 2007	October 1, 2006	% Change
Semiconductor Test	$ 668.2	$ 892.3	(25.1)%
Systems Test Group	173.7	205.3	(15.4)
	$ 841.9	$ 1,097.6	(23.3)%

Semiconductor Test revenue decrease is attributed to decreased demand across a wide range of end markets, applications and geographies as SOC device units grew at a lower rate in 2007 than in 2006.

The decrease in Systems Test Group revenue is due to a decrease in automotive test revenue due primarily to the large program rollout in 2006 for the Vehicle Measurement Module product line.

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Our sales by region as a percentage of total net sales were as follows:

	For the Nine Months Ended	
	September 30, 2007	October 1, 2006
United States	22.7%	21.5%
Singapore	15.5	10.9
South East Asia	15.3	19.2
Europe	12.4	14.2
Taiwan	12.2	14.4
Japan	11.6	11.9
Korea	7.8	6.4
Rest of the World	2.5	1.5
	100%	100%

Gross Profit

Our gross profit was as follows (dollars in millions):

	For the Nine Months Ended		
	September 30, 2007	October 1, 2006	Period Change
Gross Profit	$ 394.9	$ 532.1	$ (137.2)
Percent of Total Revenue	46.9%	48.5%	

The decrease in gross profit as a percentage of revenue from the first nine months of 2006 to 2007 was primarily the result of lower volume in Semiconductor Test and to a lesser extent a revenue mix shift towards service in 2007, together accounting for 4.5 points of the decrease. This decrease was partially offset by 2.9 points resulting from the 2006 charge in non-FLEX inventory writedowns in Semiconductor Test as well as lower fixed manufacturing costs in the first nine months of 2007 compared to the first nine months of 2006.

We assess the carrying value of our inventory on a quarterly basis by estimating future demand and comparing that demand against on-hand and on-order inventory provisions. Forecasted revenue information is obtained from the sales and marketing groups and incorporates factors such as backlog and future revenue demand. This quarterly process identifies obsolete and excess inventory. Obsolete inventory, which represents items for which there is no demand, is fully reserved. Excess inventory, which represents inventory items that are not expected to be consumed during the next four quarters, is written down to estimated net realizable value.

Included in gross profit for the nine months ended October 1, 2006 is an inventory provision of $8.0 million related to non-FLEX products. During the nine months ended September 30, 2007 and October 1, 2006, we scrapped $12.8 million and $17.1 million of inventory, respectively, and sold $0.6 million and $2.8 million of previously written-down or written-off inventory, respectively. As of September 30, 2007, we have inventory related reserves for amounts which had been written-down or written-off of $127.5 million. We have no pre-determined timeline to scrap the remaining inventory.

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Engineering and Development

Engineering and development expenses were as follows (dollars in millions):

	For the Nine Months Ended September 30, 2007	October 1, 2006	Period Change
Engineering and Development	$ 153.9	$ 154.2	$ (0.3)
Percent of Total Revenue	18.3%	14.0%	

The decrease of $0.3 million in engineering and development expenses is due to a reduction in variable employee compensation expense in each segment offset in part by an increase in Semiconductor Test spending related to entry into an adjacent market.

Selling and Administrative

Selling and administrative expenses were as follows (dollars in millions):

	For the Nine Months Ended September 30, 2007	October 1, 2006	Period Change
Selling and Administrative	$ 188.6	$ 214.8	$ (26.2)
Percent of Total Revenue	22.4%	19.6%	

The decrease of $26.2 million from the third quarter of 2006 to 2007 is primarily the result of:

- a decrease of $13.5 million in transition expenses, including the consolidation of facilities in Massachusetts and costs associated with the outsourcing of certain information technology functions; and
- a decrease of $11.3 million in variable employee compensation.

Restructuring and Other, Net

The tables below represent activity related to restructuring and other, net, in the nine months ended September 30, 2007. The accrual for severance and benefits is reflected in accrued employees compensation and withholdings. The accrual for lease payments on vacated facilities is reflected in other accrued liabilities and long-term other accrued liabilities and is expected to be paid out over the lease terms, the latest of which expires in 2012. We expect to pay out approximately $1.7 million against the lease accruals over the next twelve months. Our future lease commitments are net of expected sublease income of $10.3 million as of September 30, 2007.

2007 Activities

(in thousands)	Gain on Sale of Real Estate	Insurance Recovery	Vacated Facility Related	Severance and Benefits	Total

Balance at December 31, 2006	$	$	$	$	$
(Credits)/charges	(3,597)	(1,782)	53	6,417	1,091
Cash receipts/(payments)	3,597	1,782	(53)	(3,593)	1,733
Balance at September 30, 2007	$	$	$	$ 2,824	$ 2,824

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During the nine months ended September 30, 2007, we recorded the following 2007 restructuring activities:

$3.6 million gain on the sale of land and building in Deerfield, Illinois; and

$1.8 million of cash proceeds recovered from insurance related to a facility fire in Taiwan.

$6.4 million of severance charges related to headcount reductions of 196 people across all functions and segments; and

The restructuring actions taken during the nine months ended September 30, 2007, are expected to generate quarterly cost savings of approximately $3.3 million.

2006 Activities

(in thousands)	Vacated Facility Related	Severance and Benefits	Total
Balance at December 31, 2006	$ 625	$ 1,865	$ 2,490
Credits		(135)	(135)
Cash payments	(444)	(1,635)	(2,079)
Balance at September 30, 2007	$ 181	$ 95	$ 276

Pre-2006 Activities

(in thousands)	Vacated Facility Related	Severance and Benefits	Gain on Sale of Product Lines	Total
Balance at December 31, 2006	$ 9,604	$ 1,183	$	$ 10,787
Credits	(69)	(285)	(906)	(1,260)
Cash (payments)/receipts	(2,705)	(648)	906	(2,447)
Balance at September 30, 2007	$ 6,830	$ 250	$	$ 7,080

During the nine months ended September 30, 2007, Teradyne recorded the following pre-2006 restructuring activities:

$0.3 million credit for revised estimates on severance payments; and

$0.9 million credit for earn-out payments received in the Systems Test Group from product line divestiture.

In-process Research and Development

On March 7, 2007, we purchased in-process enabling test technology and hired certain engineers from MOSAID Technologies Inc. for $17.6 million, which includes $0.6 million in fees directly related to the acquisition. Of the purchase price, $16.7 million was allocated to in-process research and development and therefore was immediately charged to the statement of operations. The balance of the purchase price was allocated to acquired workforce and fixed assets.

This technology was acquired for use in the development of a new semiconductor test product. As of the acquisition date, the technology had not reached technical feasibility, had no alternative future use and its fair value was estimable with reasonable reliability, and therefore has been classified as in-process research and development. The technology is unique to the semiconductor test market and requires significant development. The estimated fair value of the in-process technology was determined based on the use of a discounted cash flow model using an income approach. Estimated cash flows were probability adjusted to take into account the stage

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of completion and the risks surrounding successful development and commercialization of the in-process technology. Such a valuation requires significant estimates and assumptions including but not limited to determining the timing and estimated costs to complete the in-process project as well as the estimated cash flows to be generated as a result of completing the project development.

Interest Income and Expense

Interest income decreased to $27.2 million for the first nine months of 2007 from $33.6 million in the first nine months of 2006 due to lower cash balances from the repayment of our Notes in the fourth quarter of 2006 and stock repurchases made beginning in the second half of 2006. Interest expense decreased to $0.6 million in the first nine months of 2007 from $10.4 million in the first nine months of 2006 due primarily to the repayment of the Notes.

Income Taxes

The tax expense of $9.6 million and $27.9 million for the first nine months of 2007 and 2006, respectively, consists primarily of foreign taxes. As a result of incurring significant operating losses from 2001 through 2003, we determined that it is more likely than not that our deferred tax assets may not be realized, and since the fourth quarter of 2002 we have established a full valuation allowance for our net deferred tax assets. If we generate sustained future taxable income against which these tax attributes may be applied, some portion or all of the valuation allowance would be reversed. If the valuation allowance were reversed, a portion would be recorded as an increase to additional paid in capital, and the remainder would be recorded as a reduction to income tax expense.

Contractual Obligations

As of September 30, 2007, our purchase obligations with vendors totaled $140.3 million.

Liquidity and Capital Resources

Our cash, cash equivalents and marketable securities balance decreased $197.0 million in the first nine months of 2007, to $747.7 million. Cash and cash equivalents activity for the first nine months of 2007 and 2006 was as follows (in millions):

	For the Nine Months Ended	
	September 30, 2007	**October 1, 2006**
Cash provided by operating activities:		
Net income from continuing operations, adjusted for non-cash items	$ 139.7	$ 244.2
Changes in operating assets and liabilities, net of product lines and businesses sold	(96.3)	98.2
Cash (used for) discontinued operations	(3.1)	(0.5)
Total cash provided by operating activities	40.3	341.9
Cash (used for) provided by investing activities from continuing operations	(9.3)	203.7
Cash provided by (used for) investing activities from discontinued operations	10.8	(0.3)
Total cash provided by investing activities	1.5	203.4
Total cash used for financing activities	(180.7)	(131.0)
(Decrease)/increase in cash and cash equivalents	$ (138.9)	$ 414.3

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Changes in operating assets and liabilities used cash of $96.3 million in the first nine months of 2007 due primarily to an increase in accounts receivable of $75.9 million and a decrease in income taxes payable of $30.8 million for taxes paid primarily in foreign jurisdictions. Accounts receivable increased $75.8 million, primarily in the Semiconductor Test segment, partially due to increased volume since the end of the year and partially due to an increase in days sales outstanding from 65 days as of December 31, 2006 to 71 days as of September 30, 2007 due to an increase in extended payment terms to certain customers which are generally secured by bank letters of credit. Inventory decreased $27.3 million in the first nine months of 2007 primarily in our Semiconductor Test and to a lesser extent in the Systems Test Group. Changes in operating assets and liabilities provided cash of $98.2 million in the first nine months of 2006 due primarily to a $66.8 million decrease in inventory as a result of shorter final configuration and test cycle time with our Flex products. We contributed $20.0 million to the U.S. pension plan and $5.3 million to the U.K. pension plan during the nine months ended October 1, 2006.

Investing activities consist of purchases of capital assets, the acquisition of technology for $17.6 million in the first quarter of 2007, proceeds from sales of buildings or product lines as well as the purchase, sale and maturity of marketable securities. Capital expenditures decreased by $18.6 million in the first nine months of 2007 compared to the first nine months of 2006 primarily in the Semiconductor Test due to a decrease in spending on internally manufactured test systems.

Financing activities represent the sale of our common stock, repurchases of our common stock and payments on our convertible senior notes and other debt. During the nine months ended September 30, 2007, we repurchased 13.1 million shares of our common stock for $203.6 million at an average price of $15.52 per share. During the nine months ended October 1, 2006, we repurchased $39.3 million of our Notes.

We believe our cash, cash equivalents and marketable securities balance of $747.4 million will be sufficient to meet working capital and expenditure needs for at least the foreseeable future. Inflation has not had a significant long-term impact on earnings.

Equity Compensation Plans

In addition to our 1996 Employee Stock Purchase Plan discussed in Note O: Stock Based Compensation in our 2006 Form 10-K, we have a 2006 Equity and Cash Compensation Incentive Plan (the 2006 Equity Plan), a cash and equity compensation incentive plan.

The purpose of the 1996 Employee Stock Purchase Plan is to encourage stock ownership by all eligible employees of Teradyne. The purpose of the 2006 Equity Plan is to provide equity ownership and compensation opportunities in Teradyne to our employees, officers, directors, consultants and/or advisors. Both plans were approved by our shareholders.

Recently Issued Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements (SFAS No. 157). SFAS No. 157 which establishes a framework for measuring fair value and requires expanded disclosures regarding fair value measurements. This accounting standard is effective for financial statements issued for fiscal years beginning after November 15, 2007. We are currently evaluating the impact of adopting this standard.

Certain Factors That May Affect Future Results

From time to time, information we provide, statements made by our employees or information included in our filings with the SEC (including this Form 10-Q) contain statements that are not purely historical, but are forward looking statements, made under Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act), which involve risks and uncertainties. In particular, forward looking statements made herein include projections, plans and objectives for our business, financial condition, operating results, future

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operations, or future economic performance, statements relating to the sufficiency of capital to meet working capital requirements, capital expenditures, including future lease payments and commitments and contributions to our pension plan, expectations as to customer orders and demand for our products and statements relating to backlog, bookings and cancellations, gross margins and pricing considerations. These statements are neither promises nor guarantees but involve risks and uncertainties, both known and unknown, which could cause our actual future results to differ materially from those stated in any forward looking statements. Factors that may cause such differences include, but are not limited to the following:

we are subject to intense competition;

our business is dependent on the current and anticipated market for electronics, which historically has been highly cyclical;

our operating results are likely to fluctuate significantly;

we are subject to risks of operating internationally;

if we fail to develop new technologies to adapt to our customers needs and if our customers fail to accept our new products, our revenues will be adversely affected;

if our suppliers do not meet product or delivery requirements, we could have reduced revenues and earnings;

our operations may be adversely impacted if our outsourced service providers fail to perform;

we have significant guarantees and indemnification obligations;

we have taken measures to ensure that we are prepared to address slowdowns in the market for our products, which could have long-term negative effects on our business or impact our ability to adequately address a rapid increase in customer demand;

we may incur significant liabilities if we fail to comply with environmental regulations;

we currently are and in the future may be subject to litigation that could have an adverse effect on our business;

if we are unable to protect our intellectual property, we may lose a valuable asset or may incur costly litigation to protect our rights;

our business may suffer if we are unable to attract and retain key employees;

we may incur higher tax rates than we expect;

- our business is impacted by worldwide economic cycles, which are difficult to predict;
- acts of war, terrorist attacks and the threat of domestic and international terrorist attacks may adversely impact our business;
- provisions of our charter and by-laws and Massachusetts law make a takeover of Teradyne more difficult; and
- we may acquire new businesses or form strategic alliances in the future, and we may not realize the benefits of such acquisitions.

These factors, and others, are discussed from time to time in our filings with the SEC, including our Annual Report on Form 10-K filed with the SEC on March 1, 2007 for the year ended December 31, 2006.

Item 3: Quantitative and Qualitative Disclosures about Market Risk

For Quantitative and Qualitative Disclosures about Market Risk affecting Teradyne, see Item 7a. Quantitative and Qualitative Disclosures About Market Risks, in our Annual Report on Form 10-K filed with the SEC on March 1, 2007. There were no material changes in our exposure to market risk from those set forth in our Annual Report for the fiscal year ended December 31, 2006.

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Item 4: Controls and Procedures

As of the end of the period covered by this report, our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15(b) promulgated under the Exchange Act. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures were effective in ensuring that material information required to be disclosed in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms, including ensuring that such material information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

During the period covered by this report, there have been no changes in our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met.

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PART II. OTHER INFORMATION

Item 1: Legal Proceedings

On September 5, 2001, after our August 2000 acquisition of Herco Technology Corp. and Perception Laminates, Inc., the former owners of those companies filed a complaint against Teradyne and two of our then executive officers in the Federal District Court in San Diego, California, asserting securities fraud and breach of contract related to the acquisition. The District Court dismissed certain of the plaintiffs claims, granted partial summary judgment against them with respect to their breach of contract claim and denied their motion for reconsideration. In July 2007, after an appeal by the plaintiffs, the U.S. Court of Appeals for the Ninth Circuit affirmed in part and reversed in part the District Court rulings. We petitioned the Ninth Circuit for rehearing of the ruling that it reversed. In October 2007, the Ninth Circuit denied our petition for rehearing. We will continue to defend the claim that was sent back to the District Court.

In 2001, we were designated as a Potentially Responsible Party (PRP) at a clean-up site in Los Angeles, California. This claim arose out of our acquisition of Perception Laminates in August 2000. Prior to that date, Perception Laminates had itself acquired certain assets of Alco Industries Inc. under an asset purchase agreement dated October 20, 1992. Neither Teradyne nor Perception Laminates has ever conducted any operations at the Los Angeles site. We have asked the State of California to drop the PRP designation, but California has not yet agreed to do so.

We believe that we have meritorious defenses against the above unsettled claims and intend to vigorously contest them. While it is not possible to predict or determine the outcomes of the unsettled claims or to provide possible ranges of losses that may arise, we believe the losses associated with all of these actions will not have a material adverse effect on our consolidated financial position or liquidity, but could possibly be material to our consolidated results of operations of any one period.

In addition, we are subject to legal proceedings, claims and investigations that arise in the ordinary course of business such as, but not limited to, patent, employment, commercial and environmental matters. Although there can be no assurance, there are no such matters pending that we expect to be material with respect to our business, financial position or results of operations.

Item 1A: Risk Factors

In addition to the other information set forth in this Form 10-Q, you should carefully consider the factors discussed in Part I, Item 1A: Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2006, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K are not the only risks that we face. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results.

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

(c) The following table includes information with respect to repurchases we made of our common stock during the three-month period ended September 30, 2007 (in thousands except per share price):

Period	(a) Total Number of Shares (or units) Purchased (1)	(b) Average Price Paid per Share (or Unit)	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (1)	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that may Yet Be Purchased Under the Plans or Programs (1)
July 2, 2007 July 29, 2007	541	$ 17.15	12,828	$ 225,350
July 30, 2007 August 26, 2007	8,495	$ 15.57	21,323	$ 93,041
August 27, 2007 September 30, 2007	2,405	$ 14.29	23,728	$ 58,672

(1) In July 2006, our Board of Directors authorized a stock repurchase program. Under the program, we were allowed to spend an aggregate of $400 million to repurchase shares of our common stock in open market repurchases, in privately negotiated transactions or through other appropriate means over the next two years. As of October 2007, we completed our authorized stock repurchase program. Since the inception of the program in the third quarter of 2006 we repurchased 27,947,230 shares at an average price of $14.31 per share.

Item 5: Other Information

On November 7, 2007, our Board of Directors authorized a new stock repurchase program. Under the program we are permitted to spend an aggregate of $400 million to repurchase shares of our common stock in open market purchases, in privately negotiated transactions or through other means. Shares are to be repurchased at our discretion, subject to market conditions and other factors.

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Item 6: Exhibits

Exhibit Number	Description
3.1	Amended and Restated By-laws of Teradyne (as amended on May 24, 2007) (filed herewith).
10.1	Standard Manufacturing Agreement entered into as of November 24, 2003 by and between Teradyne and Solectron Corporation (Solectron) (filed herewith).
10.2	Amendment 1 to Standard Manufacturing Agreement, dated as of January 18, 2007, by and between Teradyne and Solectron (filed herewith).
10.3	Second Amendment to Standard Manufacturing Agreement, dated as of August 27, 2007, by and between Teradyne and Solectron (filed herewith).
31.1	Certification of Principal Executive Officer, pursuant to Rule 13a-14(a) of Securities and Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
31.2	Certification of Principal Financial Officer, pursuant to Rule 13a-14(a) of Securities and Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith).
32.1	Certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).
32.2	Certification pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished herewith).

Confidential Treatment requested.

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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.

TERADYNE, INC.

Registrant

/s/ GREGORY R. BEECHER
Gregory R. Beecher
Vice President,
Chief Financial Officer and Treasurer
(Duly Authorized Officer
and Principal Financial Officer)

November 9, 2007

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