TENNECO INC
Form 10-Q
May 10, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

þ	QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 For the Quarterly Period Ended March 31, 2011 OR
o	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Commission file number 1-12387

TENNECO INC.
(Exact name of registrant as specified in its charter)

Delaware *(State or other jurisdiction of incorporation or organization)*	**76-0515284** *(I.R.S. Employer Identification No.)*
500 North Field Drive, Lake Forest, Illinois *(Address of principal executive offices)*	**60045** *(Zip Code)*

Registrant s telephone number, including area code: (847) 482-5000

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.
Yes þ No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes þ No o

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

Large accelerated filer þ Accelerated filer o Non-accelerated filer o Smaller reporting company o
(Do not check if a smaller reporting company)

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

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

Common Stock, par value $0.01 per share: 60,457,773 shares outstanding as of April 29, 2011.

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* No response to this item is included herein for the reason that it is inapplicable or the answer to such item is negative.

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CAUTIONARY STATEMENT FOR PURPOSES OF THE SAFE HARBOR PROVISIONS OF THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995

This Quarterly Report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 concerning, among other things, our prospects and business strategies. These forward-looking statements are included in various sections of this report, including the section entitled Outlook appearing in Item 2 of this report. The words may, will, believe, should, could, plan, expect, anticipate, estimate, and simila (and variations thereof), identify these forward-looking statements. Although we believe that the expectations reflected in these forward-looking statements are based on reasonable assumptions, these expectations may not prove to be correct. Because these forward-looking statements are also subject to risks and uncertainties, actual results may differ materially from the expectations expressed in the forward-looking statements. Important factors that could cause actual results to differ materially from the expectations reflected in the forward-looking statements include:

general economic, business and market conditions;

our ability to source and procure needed materials, components and other products and services in accordance with customer demand and at competitive prices, including any impact on our ability to source and procure such items and services due to supply disruptions that may be caused by the recent earthquake and tsunami in Japan;

changes in capital availability or costs, including increases in our cost of borrowing (i.e., interest rate increases), the amount of our debt, our ability to access capital markets at favorable rates, and the credit ratings of our debt;

changes in consumer demand, prices and our ability to have our products included on top selling vehicles, including any shifts in consumer preferences away from light trucks, which tend to be higher margin products for our customers and us, to other lower margin vehicles, for which we may or may not have supply contracts;

changes in automotive and commercial vehicle manufacturers production rates and their actual and forecasted requirements for our products, such as the significant production cuts during 2008 and 2009 by automotive manufacturers in response to difficult economic conditions;

the overall highly competitive nature of the automobile and commercial vehicle parts industry, and any resultant inability to realize the sales represented by our awarded book of business (which is based on anticipated pricing and volumes for the applicable program over its life);

the loss of any of our large original equipment manufacturer (OEM) customers (on whom we depend for a substantial portion of our revenues), or the loss of market shares by these customers if we are unable to achieve increased sales to other OEMs;

industrywide strikes, labor disruptions at our facilities or any labor or other economic disruptions at any of our significant customers or suppliers or any of our customers other suppliers (such as the 2008 strike at American Axle, which disrupted our supply of products for significant General Motors platforms);

increases in the costs of raw materials, including our ability to successfully reduce the impact of any such cost increases through materials substitutions, cost reduction initiatives, low cost country sourcing, and price recovery efforts with aftermarket and OE customers;

the negative impact of higher fuel prices on transportation and logistics costs, raw material costs and discretionary purchases of vehicles or aftermarket products;

the cyclical nature of the global vehicle industry, including the performance of the global aftermarket sector and the longer product lives of vehicle parts;

our ability to successfully execute cash management, restructuring and other cost reduction plans and to realize anticipated benefits from these plans;

costs related to product warranties and other customer satisfaction actions;

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the impact of consolidation among vehicle parts suppliers and customers on our ability to compete;

changes in distribution channels or competitive conditions in the markets and countries where we operate, including the impact of changes in distribution channels for aftermarket products on our ability to increase or maintain aftermarket sales;

the cost and outcome of existing and any future legal proceedings, including, but not limited to, proceedings against us or our customers relating to intellectual property rights;

economic, exchange rate and political conditions in the countries where we operate or sell our products;

customer acceptance of new products;

new technologies that reduce the demand for certain of our products or otherwise render them obsolete;

our ability to realize our business strategy of improving operating performance;

our ability to successfully integrate any acquisitions that we complete and effectively manage our joint ventures and other third-party partnerships;

changes by the Financial Accounting Standards Board or the Securities and Exchange Commission of authoritative generally accepted accounting principles or policies;

changes in accounting estimates and assumptions, including changes based on additional information;

any changes by International Standards Organization (ISO), Technical Specifications (TS) and other such committees in their certification processes for processes and products, which may have the effect of delaying or hindering our ability to bring new products to market;

the impact of changes in and compliance with laws and regulations, including environmental laws and regulations, which may result in our incurrence of environmental liabilities in excess of the amount reserved, the implementation of mandated timelines for worldwide emission regulation, which could impact the demand for certain of our products, and any changes to the timing of the funding requirements for our pension and other postretirement benefit liabilities;

decisions by federal, state and local governments to provide (or discontinue) incentive programs related to automobile or other vehicle purchases;

the potential impairment in the carrying value of our long-lived assets and goodwill or our deferred tax assets;

potential volatility in our effective tax rate;

acts of war and/or terrorism, as well as actions taken or to be taken by the United States and other governments as a result of further acts or threats of terrorism, and the impact of these acts on economic, financial and social conditions in the countries where we operate; and

the timing and occurrence (or non-occurrence) of other transactions, events and circumstances which may be beyond our control.

The risks included here are not exhaustive. Refer to Part I, Item 1A Risk Factors in our annual report on Form 10-K for the year ended December 31, 2010, for further discussion regarding our exposure to risks. Additionally, new risk factors emerge from time to time and it is not possible for us to predict all such risk factors, nor to assess the impact such risk factors might have on our business or the extent to which any factor or combination of factors may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results.

PART I.

FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS (UNAUDITED)

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Shareholders of
Tenneco Inc.:

We have reviewed the accompanying condensed consolidated balance sheet of Tenneco Inc. and consolidated subsidiaries as of March 31, 2011, and the related condensed consolidated statements of income, cash flows, changes in shareholders equity, and comprehensive income (loss) for the three-month periods ended March 31, 2011 and 2010. These interim financial statements are the responsibility of the Company s management.

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

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

We previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of December 31, 2010, and the related consolidated statements of income (loss), cash flows, changes in shareholders equity and comprehensive income (loss) for the year then ended (not presented herein), and in our report dated February 25, 2011, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2010, is fairly stated in all material respects in relation to the consolidated balance sheet from which it has been derived.

/s/ PricewaterhouseCoopers LLP

Chicago, Illinois
May 6, 2011

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TENNECO INC.

CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(Unaudited)

	Three Months Ended March 31, 2011	2010
	(Millions Except Share and Per Share Amounts)	
Revenues		
Net sales and operating revenues	$ 1,760	$ 1,316
Costs and expenses		
Cost of sales (exclusive of depreciation and amortization shown below)	1,466	1,073
Engineering, research, and development	35	27
Selling, general, and administrative	109	100
Depreciation and amortization of other intangibles	51	55
	1,661	1,255
Other income (expense)		
Loss on sale of receivables	(1)	(1)
Other income (expense)	(4)	(1)
	(5)	(2)
Earnings before interest expense, income taxes, and noncontrolling interests	94	59
Interest expense (net of interest capitalized of $1 million in each of the three months ended March 31, 2011 and 2010, respectively)	28	32
Income tax expense	14	15
Net income	52	12
Less: Net income attributable to noncontrolling interests	5	5
Net income attributable to Tenneco Inc.	$ 47	$ 7
Earnings per share		
Weighted average shares of common stock outstanding		
Basic	59,849,278	58,948,351
Diluted	62,074,523	60,811,047
Basic earnings per share of common stock	$ 0.78	$ 0.11
Diluted earnings per share of common stock	$ 0.75	$ 0.11

The accompanying notes to the condensed consolidated financial statements are an integral part of these condensed consolidated statements of income.

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TENNECO INC.

CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)

	March 31, 2011	December 31, 2010
	(Millions)	
ASSETS		
Current assets:		
Cash and cash equivalents	$ 199	$ 233
Receivables		
Customer notes and accounts, net	1,038	796
Other	52	30
Inventories		
Finished goods	266	222
Work in process	192	164
Raw materials	134	118
Materials and supplies	45	43
Deferred income taxes	39	38
Prepayments and other	164	146
Total current assets	2,129	1,790
Other assets:		
Long-term receivables, net	12	9
Goodwill	90	89
Intangibles, net	34	32
Deferred income taxes	91	92
Other	104	105
	331	327
Plant, property, and equipment, at cost	3,208	3,109
Less Accumulated depreciation and amortization	(2,136)	(2,059)
	1,072	1,050
Total assets	$ 3,532	$ 3,167
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Short-term debt (including current maturities of long-term debt)	$ 146	$ 63
Trade payables	1,205	1,048
Accrued taxes	59	51
Accrued interest	22	13

Accrued liabilities	240	227
Other	57	66
Total current liabilities	1,729	1,468
Long-term debt	1,185	1,160
Deferred income taxes	57	56
Postretirement benefits	306	311
Deferred credits and other liabilities	122	125
Commitments and contingencies		
Total liabilities	3,399	3,120
Redeemable noncontrolling interests	14	12
Tenneco Inc. Shareholders equity:		
Common stock	1	1
Premium on common stock and other capital surplus	3,009	3,008
Accumulated other comprehensive loss	(205)	(237)
Retained earnings (accumulated deficit)	(2,489)	(2,536)
	316	236
Less Shares held as treasury stock, at cost	240	240
Total Tenneco Inc. shareholders equity	76	(4)
Noncontrolling interests	43	39
Total equity	119	35
Total liabilities, redeemable noncontrolling interests and equity	$ 3,532	$ 3,167

The accompanying notes to the condensed consolidated financial statements are an integral part of these condensed consolidated balance sheets.

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TENNECO INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
	(Millions)	
Operating Activities		
Net income	$ 52	$ 12
Adjustments to reconcile net income to cash used by operating activities		
Depreciation and amortization of other intangibles	51	55
Deferred income taxes	(5)	(3)
Stock-based compensation	2	3
Loss on sale of assets		2
Changes in components of working capital		
(Increase) decrease in receivables	(251)	(191)
(Increase) decrease in inventories	(77)	(44)
(Increase) decrease in prepayments and other current assets	(15)	(7)
Increase (decrease) in payables	139	120
Increase (decrease) in accrued taxes	8	7
Increase (decrease) in accrued interest	8	9
Increase (decrease) in other current liabilities	1	(6)
Change in long-term assets	(3)	(1)
Change in long-term liabilities	(12)	(11)
Other	(1)	(2)
Net cash used by operating activities	(103)	(57)
Investing Activities		
Proceeds from the sale of assets	4	1
Cash payments for plant, property, and equipment	(46)	(38)
Cash payments for software related intangible assets	(3)	(2)
Other		1
Net cash used by investing activities	(45)	(38)
Financing Activities		
Retirement of long-term debt	(22)	(8)
Increase (decrease) in bank overdrafts	7	(1)
Net increase in revolver borrowings and short-term debt excluding current maturities of long-term debt and short-term borrowings secured by accounts receivable	47	2
Net increase in short-term borrowings secured by accounts receivable	82	126
Distributions to noncontrolling interest partners		(1)

Net cash provided by financing activities		114		118
Effect of foreign exchange rate changes on cash and cash equivalents				3
Increase (decrease) in cash and cash equivalents		(34)		26
Cash and cash equivalents January 1		233		167
Cash and cash equivalents, March 31 (Note)	$	199	$	193
Supplemental Cash Flow Information				
Cash paid during the period for interest	$	19	$	22
Cash paid during the period for income taxes (net of refunds)		10		8
Non-cash Investing and Financing Activities				
Period ended balance of payable for plant, property, and equipment	$	25	$	16

Note: Cash and cash equivalents include highly liquid investments with a maturity of three months or less at the date of purchase.

The accompanying notes to the condensed consolidated financial statements are an integral part of these condensed consolidated statements of cash flows.

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TENNECO INC.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS EQUITY (Unaudited)

	Three Months Ended March 31,			
	2011		2010	
	Shares	Amount	Shares	Amount
	(Millions Except Share Amounts)			
Tenneco Inc. Shareholders:				
Common Stock				
Balance January 1	61,541,760	$ 1	60,789,739	$ 1
Issued pursuant to benefit plans	59,904		149,417	
Stock options exercised	125,624		60,375	
Balance March 31	61,727,288	1	60,999,531	1
Premium on Common Stock and Other Capital Surplus				
Balance January 1		3,008		3,005
Purchase of additional noncontrolling equity interest				(11)
Premium on common stock issued pursuant to benefit plans		1		2
Balance March 31		3,009		2,996
Accumulated Other Comprehensive Loss				
Balance January 1		(237)		(212)
Other comprehensive income (loss)		32		(31)
Balance March 31		(205)		(243)
Retained Earnings (Accumulated Deficit)				
Balance January 1		(2,536)		(2,575)
Net income attributable to Tenneco Inc.		47		7
Balance March 31		(2,489)		(2,568)
Less Common Stock Held as Treasury Stock, at Cost				
Balance January 1 and March 31	1,294,692	240	1,294,692	240
Total Tenneco Inc. shareholders equity		$ 76		$ (54)
Noncontrolling Interests:				
Balance January 1		39		32
Net income		4		3

Sale of twenty percent equity interest to Tenneco Inc.				(4)
Balance March 31	$	43	$	31
Total equity	$	119	$	(23)

The accompanying notes to the condensed consolidated financial statements are an integral part of these condensed consolidated statements of changes in shareholders equity.

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TENNECO INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited)

	Three Months Ended March 31, 2011					
	Tenneco Inc.		Noncontrolling Interests		Total	
	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)
	(Millions)					
Net Income		$ 47		$ 5		$ 52
Accumulated Other Comprehensive Income (Loss)						
Cumulative Translation Adjustment						
Balance January 1	$ 8		$ 5		$ 13	
Translation of foreign currency statements	30	30	1	1	31	31
Balance March 31	38		6		44	
Additional Liability for Pension Benefits						
Balance January 1	(250)				(250)	
Additional Liability for Pension and Postretirement Benefits, net of tax	1	1			1	1
Balance March 31	(249)				(249)	
Balance March 31	$ (211)		$ 6		$ (205)	
Other Comprehensive Income		31		1		32
Comprehensive Income		$ 78		$ 6		$ 84

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

Three Months Ended March 31, 2010

	Tenneco Inc.		Noncontrolling Interests		Total	
	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)	Accumulated Other Comprehensive Income (Loss)	Comprehensive Income (Loss)
			(Millions)			
Net Income		$ 7		$ 5		$ 12
Accumulated Other Comprehensive Income (Loss)						
Cumulative Translation Adjustment						
Balance January 1	$ 37		$		$ 37	
Translation of foreign currency statements	(32)	(32)			(32)	(32)
Balance March 31	5				5	
Additional Liability for Pension Benefits						
Balance January 1	(249)				(249)	
Additional Liability for Pension and Postretirement Benefits, net of tax	1	1			1	1
Balance March 31	(248)				(248)	
Balance March 31	$ (243)		$		$ (243)	
Other Comprehensive Income (Loss)		(31)				(31)
Comprehensive Income (Loss)		$ (24)		$ 5		$ (19)

The accompanying notes to the condensed consolidated financial statements are in an integral part of these statements of comprehensive income (loss).

TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

(1) Consolidation and Presentation

As you read the accompanying financial statements you should also read our Annual Report on Form 10-K for the year ended December 31, 2010.

In our opinion, the accompanying unaudited financial statements contain all adjustments (consisting of normal recurring adjustments) necessary to present fairly Tenneco Inc. s financial position, results of operations, cash flows, changes in shareholders equity, and comprehensive income (loss) for the periods indicated. We have prepared the unaudited condensed consolidated financial statements pursuant to the rules and regulations of the U.S. Securities and Exchange Commission for interim financial information. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America (U.S. GAAP) for annual financial statements.

Our condensed consolidated financial statements include all majority-owned subsidiaries. We carry investments in 20 percent to 50 percent owned companies in which the Company does not have a controlling interest, as equity method investments, at cost plus equity in undistributed earnings since the date of acquisition and cumulative translation adjustments. We have eliminated all intercompany transactions. We have evaluated all subsequent events through the date the financial statements were issued.

(2) Financial Instruments

The carrying and estimated fair values of our financial instruments by class at March 31, 2011 and December 31, 2010 were as follows:

	March 31, 2011		December 31, 2010	
	Carrying Amount	Fair Value	Carrying Amount	Fair Value
		(Millions)		
Long-term debt (including current maturities)	$ 1,188	$ 1,236	$ 1,162	$ 1,201
Instruments with off-balance sheet risk:				
Foreign exchange forward contracts	1	1	2	2

Asset and Liability Instruments The fair value of cash and cash equivalents, short and long-term receivables, accounts payable, and short-term debt was considered to be the same as or was not determined to be materially different from the carrying amount.

Long-term Debt The fair value of our public fixed rate senior notes is based on quoted market prices. The fair value of our private borrowings under our senior credit facility and other long-term debt instruments is based on the market value of debt with similar maturities, interest rates and risk characteristics.

Foreign exchange forward contracts We use derivative financial instruments, principally foreign currency forward purchase and sales contracts with terms of less than one year, to hedge our exposure to changes in foreign currency exchange rates. Our primary exposure to changes in foreign currency rates results from intercompany loans made between affiliates to minimize the need for borrowings from third parties. Additionally, we enter into foreign currency forward purchase and sale contracts to mitigate our exposure to changes in exchange rates on certain intercompany and third-party trade receivables and payables. We manage counter-party credit risk by entering into derivative financial instruments with major financial institutions that can be expected to fully perform under the terms of such agreements. We do not enter into derivative financial instruments for speculative purposes. The fair value of our foreign currency forward contracts is based on an internally developed model which incorporates observable inputs including quoted spot rates, forward exchange rates and discounted future expected cash flows utilizing market interest rates with similar quality and maturity characteristics. We record the change in fair value of these foreign exchange forward contracts as part of currency gains (losses) within cost of sales in the condensed consolidated statements of income. The fair value of foreign exchange forward contracts are recorded in

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TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

prepayments and other current assets or other current liabilities in the condensed consolidated balance sheet. The fair value of our foreign exchange forward contracts, presented on a gross basis by derivative contract at March 31, 2011 and December 31, 2010, respectively, was as follows:

	Fair Value of Derivative Instruments (Millions)					
	March 31, 2011			December 31, 2010		
	Asset Derivatives	Liability Derivatives	Total	Asset Derivatives	Liability Derivatives	Total
Foreign exchange forward contracts	$ 1	$	$ 1	$ 2	$	$ 2

The fair value of our recurring financial assets and liabilities at March 31, 2011 and December 31, 2010, respectively, are as follows:

	March 31, 2011 (Millions)			December 31, 2010		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Financial Assets:						
Foreign exchange forward contracts	n/a	$ 1	n/a	n/a	$ 2	n/a

The fair value hierarchy definition prioritizes the inputs used in measuring fair value into the following levels:

Level 1 Quoted prices in active markets for identical assets or liabilities.

Level 2 Inputs, other than quoted prices in active markets, that are observable either directly or indirectly.

Level 3 Unobservable inputs based on our own assumptions.

The following table summarizes by major currency the notional amounts for foreign currency forward purchase and sale contracts as of March 31, 2011 (all of which mature in 2011):

		Notional Amount in Foreign Currency (Millions)
Australian dollars	Purchase	13
	Sell	(5)
British pounds	Purchase	2
	Sell	(1)

European euro	Sell	(20)
Czech Republic koruna	Purchase	122
Japanese Yen	Purchase	585
South African rand	Purchase	208
U.S. dollars	Purchase	6
	Sell	(31)
Other	Purchase	1
	Sell	(1)

(3) Long-Term Debt and Financing Arrangements

Our financing arrangements are primarily provided by a committed senior secured financing arrangement with a syndicate of banks and other financial institutions. The arrangement is secured by substantially all our domestic assets and pledges of up to 66 percent of the stock of certain first-tier foreign subsidiaries, as well as guarantees by our material domestic subsidiaries.

TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

On June 3, 2010, we completed an amendment and extension of our senior secured credit facility by extending the term of our revolving credit facility and replacing our $128 million term loan A with a larger and longer maturity term loan B facility. As a result of the amendment and extension, as of March 31, 2011, the senior credit facility provides us with a total revolving credit facility size of $622 million until March 16, 2012, when commitments of $66 million will expire. After March 16, 2012, the extended revolving credit facility will provide $556 million of revolving credit and will mature on May 31, 2014. The extended facility will mature earlier on December 15, 2013, if our $130 million tranche B-1 letter of credit/revolving loan facility is not refinanced by that date. Prior to maturity, funds may be borrowed, repaid and re-borrowed under the two revolving credit facilities without premium or penalty. The leverage ratio (consolidated indebtedness net of cash divided by consolidated EBITDA as defined in the senior credit facility agreement) was decreased from 5.00 to 4.50 for the second quarter of 2010; from 4.75 to 4.25 for the third quarter of 2010; and from 4.50 to 4.25 for the fourth quarter of 2010 as a result of the June 3, 2010 amendment.

As of March 31, 2011, the senior credit facility also provides a six-year, $150 million term loan B maturing in June 2016, and a seven-year $130 million tranche B-1 letter of credit/revolving loan facility maturing in March 2014. We are required to make quarterly principal payments of $375 thousand on the term loan B, beginning on September 20, 2010 through March 31, 2016 with a final payment of $141 million due June 3, 2016. The tranche B-1 letter of credit/revolving loan facility requires repayment by March 2014. We can enter into revolving loans and issue letters of credit under the $130 million tranche B-1 letter of credit/revolving loan facility. The tranche B-1 letter of credit/revolving loan facility is reflected as debt on our balance sheet only if we borrow money under this facility or if we use the facility to make payments for letters of credit. There is no additional cost to us for issuing letters of credit under the tranche B-1 letter of credit/revolving loan facility. However, outstanding letters of credit reduce our availability to enter into revolving loans under the facility. We pay the tranche B-1 lenders interest equal to LIBOR plus a margin on all borrowings under the facility. Funds deposited with the administrative agent by the lenders and not borrowed by the Company earn interest at an annual rate approximately equal to LIBOR less 25 basis points.

The financial ratios required under the senior credit facility for the remainder of 2011 and beyond are set forth below. As of March 31, 2011, we were in compliance with all the financial covenants and operational restrictions of the senior credit facility.

Period Ending	**Leverage Ratio**	**Interest Coverage Ratio**
June 30, 2011	3.75	2.55
September 30, 2011	3.50	2.55
December 31, 2011	3.50	2.55
Each quarter thereafter	3.50	2.75

Beginning June 3, 2010, our term loan B and revolving credit facility bear interest at an annual rate equal to, at our option, either (i) the London Interbank Offered Rate plus a margin of 475 and 450 basis points, respectively, or (ii) a rate consisting of the greater of (a) the JPMorgan Chase prime rate plus a margin of 375 and 350 basis points, respectively, (b) the Federal Funds rate plus 50 basis points plus a margin of 375 and 350 basis points, respectively, and (c) the Eurodollar Rate plus 100 basis points plus a margin of 375 and 350 basis points, respectively. The margin we pay on these borrowings will be reduced by 25 basis points following each fiscal quarter for which our consolidated net leverage ratio is less than 2.25 for extending lenders and for the term loan B and will be further reduced by an additional 25 basis points following each fiscal quarter for which the consolidated net leverage ratio is less than 2.0 for extending lenders. The margin we pay on these borrowings for extending lenders will increase by 50 basis points following each fiscal quarter for which our consolidated net leverage ratio is greater than or equal to 4.00 and will be further increased by an additional 50 basis points following each fiscal quarter for which the

TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

consolidated net leverage ratio is greater than or equal to 5.00. Our consolidated net leverage ratio was 2.32 and 2.24 as of March 31, 2011 and December 31, 2010, respectively. As a result, the margin we pay on these borrowings was reduced in February 2011 by 25 basis points for extending lenders. However, since the ratio increased during the quarter, the margin we pay on borrowings will increase by 25 basis points beginning in May 2011 and will remain at such level for so long as our consolidated net leverage ratio remains above 2.25 and less than 4.00.

The borrowings under our tranche B-1 letter of credit/revolving loan facility incur interest at an annual rate equal to, at our option, either (i) the London Interbank Offered Rate plus a margin of 500 basis points, or (ii) a rate consisting of the greater of (a) the JPMorgan Chase prime rate plus a margin of 400 basis points, (b) the Federal Funds rate plus 50 basis points plus a margin of 400 basis points, and (c) the Eurodollar Rate plus 100 basis points plus a margin of 400 basis points. The rate will increase by 50 basis points following each fiscal quarter for which our consolidated net leverage ratio is greater than or equal to 5.0.

At March 31, 2011, of the $752 million available under the two revolving credit facilities within our senior secured credit facility, we had unused borrowing capacity of $652 million with $47 million in outstanding borrowings and $53 million in letters of credit outstanding. As of March 31, 2011, our outstanding debt also included $250 million of 81/8 percent senior notes due November 15, 2015, $149 million term loan B due June 3, 2016, $225 million of 73/4 percent senior notes due August 15, 2018, $500 million of 67/8 percent senior notes due December 15, 2020, and $160 million of other debt.

On December 9, 2010, we commenced a cash tender offer of our outstanding $500 million 85/8 percent senior subordinated notes due in 2014 and a consent solicitation to amend the indenture governing these notes. The consent solicitation expired on December 22, 2010 and the cash tender offer expired on January 6, 2011. On December 23, 2010, we issued $500 million of 67/8 percent senior notes due December 15, 2020 in a private offering. The net proceeds of this transaction, together with cash and available liquidity, were used to finance the purchase of our 85/8 percent senior subordinated notes pursuant to the tender offer at a price of 103.25 percent of the principal amount, plus accrued and unpaid interest for holders who tendered prior to the expiration of the consent solicitation, and 100.25 percent of the principal amount, plus accrued and unpaid interest, for other participants. On January 7, 2011, we redeemed all remaining outstanding $20 million of senior subordinated notes that were not previously tendered, at a price of 102.875 percent of the principal amount, plus accrued and unpaid interest. To facilitate these transactions, we amended our senior credit agreement to permit us to refinance our senior subordinated notes with new senior unsecured notes. We did not incur any fee in connection with this amendment. The new notes are general senior obligations of Tenneco Inc. and are not secured by assets of Tenneco Inc. or any of our subsidiaries that guarantee the new notes. We recorded $20 million of pre-tax charges in December 2010 and an additional $1 million of pre-tax charges in the first quarter of 2011 related to our repurchase and redemption of our 85/8 percent senior subordinated notes. On March 14, 2011, we completed an offer to exchange the $500 million of 67/8 percent senior notes due in 2020 which have been registered under the Securities Act of 1933, for and in replacement of all outstanding unregistered 67/8 percent senior notes due in 2020. We received tenders from holders of all $500 million of the aggregate outstanding amount of the original notes. The terms of the new notes are substantially identical to the terms of the original notes for which they were exchanged, except that the transfer restrictions and the registration rights applicable to the original notes generally do not apply to the new notes.

On August 3, 2010, we issued $225 million of 73/4 percent senior notes due August 15, 2018 in a private offering. The net proceeds of this transaction, together with cash and available liquidity, were used to finance the redemption of our 101/4 percent senior secured notes due in 2013. We called the senior secured notes for redemption on August 3, 2010, and completed the redemption on September 2, 2010 at a price of 101.708 percent of the principal amount, plus accrued and unpaid interest. We recorded $5 million of expense related to our redemption of our 101/4 percent senior secured notes in the third quarter of 2010. The new notes are general senior obligations of Tenneco Inc. and are not secured by assets of Tenneco Inc. or any of our subsidiaries that guarantee the new notes. On February 14, 2011, we completed an offer to exchange the $225 million of 73/4 percent senior notes due in 2018

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which have been registered under the Securities Act of 1933, for and in replacement of all outstanding unregistered 73/4 percent senior notes due in 2018. We received tenders from holders of all $225 million of the aggregate outstanding amount of the original notes. The terms of the new notes are substantially identical to the terms of the original notes for which they were exchanged, except that the transfer restrictions and the registration rights applicable to the original notes generally do not apply to the new notes.

(4) Income Taxes

We evaluate our deferred income taxes quarterly to determine if valuation allowances are required or should be adjusted. U.S. GAAP requires that companies assess whether valuation allowances should be established against their deferred tax assets based on consideration of all available evidence, both positive and negative, using a more likely than not standard. This assessment considers, among other matters, the nature, frequency and amount of recent losses, the duration of statutory carryforward periods, and tax planning strategies. In making such judgments, significant weight is given to evidence that can be objectively verified.

Valuation allowances have been established for deferred tax assets based on a more likely than not threshold. The ability to realize deferred tax assets depends on our ability to generate sufficient taxable income within the carryforward periods provided for in the tax law for each tax jurisdiction. We have considered the following possible sources of taxable income when assessing the realization of our deferred tax assets:

- Future reversals of existing taxable temporary differences;

- Taxable income or loss, based on recent results, exclusive of reversing temporary differences and carryforwards; and

- Tax-planning strategies.

We reported income tax expense of $14 million in the first quarter of 2011. The tax expense recorded differs from the expense that would be recorded using a U.S. Federal statutory rate of 35 percent due to a net tax benefit of $10 million primarily related to U.S. taxable income with no associated tax expense due to our net operating loss (NOL) position, and income generated in lower tax rate jurisdictions, partially offset by the impact of recording a valuation allowance against the tax benefit for losses in certain foreign jurisdictions. In evaluating the requirements to record a valuation allowance, accounting standards do not permit us to consider an economic recovery in the U.S. or new business we have won. Consequently, beginning in 2008, given our historical losses, we concluded that our ability to fully utilize our NOLs was limited due to projecting the continuation of the negative economic environment and the impact of the negative operating environment on our tax planning strategies. As a result of our tax planning strategies which have not yet been implemented and which do not depend upon generating future taxable income, we carry deferred tax assets in the U.S. of $90 million relating to the expected utilization of those NOLs. The federal NOLs expire beginning in tax years ending in 2020 through 2029. The state NOLs expire in various tax years through 2029.

If our operating performance improves on a sustained basis, our conclusion regarding the need for a valuation allowance could change, resulting in the reversal of some or all of the valuation allowance in the future. The charge to establish the U.S. valuation allowance also includes items related to the losses allocable to certain state jurisdictions where it was determined that tax attributes related to those jurisdictions were potentially not realizable.

We are required to record a valuation allowance against deferred tax assets generated by taxable losses in each period in the U.S. as well as in other foreign jurisdictions. Our future provision for income taxes will include no tax benefit with respect to losses incurred and no tax expense with respect to income generated in these jurisdictions until the respective valuation allowance is eliminated. This will cause variability in our effective tax rate.

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(5) Accounts Receivable Securitization

We securitize some of our accounts receivable on a limited recourse basis in North America and Europe. As servicer under these accounts receivable securitization programs, we are responsible for performing all accounts receivable administration functions for these securitized financial assets including collections and processing of customer invoice adjustments. In North America, we have an accounts receivable securitization program with three commercial banks. We securitize original equipment and aftermarket receivables on a daily basis under the bank program. In March 2011, the North American program was amended and extended to March 23, 2012. The first priority facility continues to provide financing of up to $110 million and the second priority facility, which is subordinated to the first priority facility, continues to provide up to an additional $40 million of financing. Both facilities monetize accounts receivable generated in the U.S. and Canada that meet certain eligibility requirements, and the second priority facility also monetizes certain accounts receivable generated in the U.S. or Canada that would otherwise be ineligible under the first priority securitization facility. The amendments to the North American program expand the trade receivables that are eligible for purchase under the program and decrease the margin we pay to our banks. The amount of outstanding third party investments in our securitized accounts receivable under the North American program was $82 million at March 31, 2011 and zero at December 31, 2010.

Each facility contains customary covenants for financings of this type, including restrictions related to liens, payments, mergers or consolidation and amendments to the agreements underlying the receivables pool. Further, each facility may be terminated upon the occurrence of customary events (with customary grace periods, if applicable), including breaches of covenants, failure to maintain certain financial ratios, inaccuracies of representations and warranties, bankruptcy and insolvency events, certain changes in the rate of default or delinquency of the receivables, a change of control and the entry or other enforcement of material judgments. In addition, each facility contains cross-default provisions, where the facility could be terminated in the event of non-payment of other material indebtedness when due and any other event which permits the acceleration of the maturity of material indebtedness.

We also securitize receivables in our European operations with regional banks in Europe. The arrangements to securitize receivables in Europe are provided under seven separate facilities provided by various financial institutions in each of the foreign jurisdictions. The commitments for these arrangements are generally for one year, but some may be cancelled with notice 90 days prior to renewal. In some instances, the arrangement provides for cancellation by the applicable financial institution at any time upon 15 days, or less, notification. The amount of outstanding third party investments in our securitized accounts receivable in Europe was $147 million and $91 million at March 31, 2011 and December 31, 2010, respectively.

If we were not able to securitize receivables under either the North American or European securitization programs, our borrowings under our revolving credit agreements might increase. These accounts receivable securitization programs provide us with access to cash at costs that are generally favorable to alternative sources of financing, and allow us to reduce borrowings under our revolving credit agreements.

In our North American accounts receivable securitization programs, we transfer a partial interest in a pool of receivables and the interest that we retain is subordinate to the transferred interest. Accordingly, we account for our North American securitization program as a secured borrowing. In our European programs, we transfer accounts receivables in their entirety to the acquiring entities and satisfy all of the conditions established under ASC Topic 860, Transfers and Servicing, to report the transfer of financial assets in their entirety as a sale. The fair value of assets received as proceeds in exchange for the transfer of accounts receivable under our European securitization programs approximates the fair value of such receivables. We recognized $1 million in interest expense in both the three month period ended March 31, 2011 and 2010, respectively, relating to our North American securitization program. In addition, we recognized a loss of $1 million in both the three month period ended March 31, 2011 and 2010, respectively, on the sale of trade accounts receivable in our European accounts receivable securitization programs, representing the discount from book values at which these receivables were sold

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to our banks. The discount rate varies based on funding costs incurred by our banks, which averaged approximately three percent and four percent during the first quarter of 2011 and 2010, respectively.

(6) Restructuring and Other Charges

Over the past several years, we have adopted plans to restructure portions of our operations. These plans were approved by our Board of Directors and were designed to reduce operational and administrative overhead costs throughout the business. In 2010, we incurred $19 million in restructuring and related costs, of which $14 million was recorded in cost of sales and $5 million was recorded in depreciation and amortization expense. In the first quarter of 2011, we incurred $1 million in restructuring and related costs, all of which was recorded in cost of sales.

Amounts related to activities that are part of our restructuring plans are as follows:

	December 31, 2010 Restructuring Reserve	2011 Cash Payments	Impact of Exchange Rates	Reserve Adjustments	March 31, 2011 Restructuring Reserve
			(Millions)		
Severance	$ 7	(1)		(1)	$ 5

Under the terms of our amended and extended senior credit agreement that took effect on June 3, 2010, we are allowed to exclude $60 million of cash charges and expenses, before taxes, related to cost reduction initiatives incurred after June 3, 2010 from the calculation of the financial covenant ratios required under our senior credit facility. As of March 31, 2011, we have excluded $10 million in cumulative allowable charges relating to restructuring initiatives against the $60 million available under the terms of the senior credit facility.

On September 22, 2009, we announced that we will be closing our original equipment ride control plant in Cozad, Nebraska. We plan to hire at other facilities as we move production from Cozad to those facilities, resulting in a net decrease of approximately 60 positions. We originally planned to have completed the closing of this facility by the end of 2010, however, as a result of increased customer demand and to better optimize the transfer of some of the manufacturing activities, we plan to supply certain of our other facilities with components from Cozad to support this increased demand until capacity adjustments are completed at our other facilities. During 2009 and 2010, we recorded $11 million and $10 million, respectively, of restructuring and related expenses related to this initiative, of which approximately $16 million represents cash expenditures.

(7) Environmental Matters, Litigation and Product Warranties

We are subject to a variety of environmental and pollution control laws and regulations in all jurisdictions in which we operate. We expense or capitalize, as appropriate, expenditures for ongoing compliance with environmental regulations that relate to current operations. We expense costs related to an existing condition caused by past operations that do not contribute to current or future revenue generation. We record liabilities when environmental assessments indicate that required remedial efforts are probable and the costs can be reasonably estimated. Estimates of the liability are based upon currently available facts, existing technology, and presently enacted laws and regulations taking into consideration the likely effects of inflation and other societal and economic factors. We consider all available evidence including prior experience in remediation of contaminated sites, other companies cleanup experiences and data released by the United States Environmental Protection Agency or other organizations. These estimated liabilities are subject to revision in future periods based on actual costs or new information. Where future cash flows are fixed or reliably determinable, we have discounted the liabilities. All other environmental liabilities are recorded at their undiscounted amounts. We evaluate recoveries separately from the liability

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and, when they are assured, recoveries are recorded and reported separately from the associated liability in our condensed consolidated financial statements.

As of March 31, 2011, we have the obligation to remediate or contribute towards the remediation of certain sites, including two existing Federal Superfund sites. At March 31, 2011, our aggregated estimated share of environmental remediation costs for all these sites on a discounted basis was approximately $16 million, of which $5 million is recorded in other current liabilities and $11 million is recorded in deferred credits and other liabilities in our condensed consolidated balance sheet. For those locations in which the liability was discounted, the weighted average discount rate used was 2.6 percent. The undiscounted value of the estimated remediation costs was $21 million. Based on information known to us, we have established reserves that we believe are adequate for these costs. Although we believe these estimates of remediation costs are reasonable and are based on the latest available information, the costs are estimates and are subject to revision as more information becomes available about the extent of remediation required. At some sites, we expect that other parties will contribute towards the remediation costs. In addition, certain environmental statutes provide that our liability could be joint and several, meaning that we could be required to pay in excess of our share of remediation costs. Our understanding of the financial strength of other potentially responsible parties at these sites has been considered, where appropriate, in our determination of our estimated liability.

We do not believe that any potential costs associated with our current status as a potentially responsible party in the Federal Superfund sites, or as a liable party at the other locations referenced herein, will be material to our condensed consolidated results of operations, financial position or cash flows.

We also from time to time are involved in legal proceedings, claims or investigations that are incidental to the conduct of our business. Some of these proceedings allege damages against us relating to environmental liabilities (including toxic tort, property damage and remediation), intellectual property matters (including patent, trademark and copyright infringement, and licensing disputes), personal injury claims (including injuries due to product failure, design or warning issues, and other product liability related matters), taxes, employment matters, and commercial or contractual disputes, sometimes related to acquisitions or divestitures. For example, one of our Argentine subsidiaries is currently defending against a criminal complaint alleging the failure to comply with laws requiring the proceeds of export transactions to be collected, reported and/or converted to local currency within specified time periods. As another example, we are subject to an audit in 11 states of our practices with respect to the payment of unclaimed property to those states, which could cover over 30 years. We now have practices in place which we believe ensure that we pay unclaimed property as required. We vigorously defend ourselves against all of these claims. In future periods, we could be subject to cash costs or charges to earnings if any of these matters are resolved on unfavorable terms. However, although the ultimate outcome of any legal matter cannot be predicted with certainty, based on current information, including our assessment of the merits of the particular claim, we do not expect that these legal proceedings or claims will have any material adverse impact on our future consolidated financial position, results of operations or cash flows.

In addition, we are subject to a number of lawsuits initiated by a significant number of claimants alleging health problems as a result of exposure to asbestos. In the early 2000 s we were named in nearly 20,000 complaints, most of which were filed in Mississippi state court and the vast majority of which made no allegations of exposure to asbestos from our product categories. Most of these claims have been dismissed and our current docket of active and inactive cases is less than 500 cases nationwide. A small number of claims have been asserted by railroad workers alleging exposure to asbestos products in railroad cars manufactured by The Pullman Company, one of our subsidiaries. The balance of the claims is related to alleged exposure to asbestos in our automotive emission control products. Only a small percentage of the claimants allege that they were automobile mechanics and a significant number appear to involve workers in other industries or otherwise do not include sufficient information to determine whether there is any basis for a claim against us. We believe, based on scientific and other evidence, it is unlikely that mechanics were exposed to asbestos by our former muffler products and that, in any event, they would not be at

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increased risk of asbestos-related disease based on their work with these products. Further, many of these cases involve numerous defendants, with the number of each in some cases exceeding 100 defendants from a variety of industries. Additionally, the plaintiffs either do not specify any, or specify the jurisdictional minimum, dollar amount for damages. As major asbestos manufacturers continue to go out of business or file for bankruptcy, we may experience an increased number of these claims. We vigorously defend ourselves against these claims as part of our ordinary course of business. In future periods, we could be subject to charges to earnings if any of these matters are resolved unfavorably to us. To date, with respect to claims that have proceeded sufficiently through the judicial process, we have regularly achieved favorable resolutions. Accordingly, we presently believe that these asbestos-related claims will not have a material adverse impact on our future consolidated financial condition, results of operations or cash flows.

We provide warranties on some of our products. The warranty terms vary but range from one year up to limited lifetime warranties on some of our premium aftermarket products. Provisions for estimated expenses related to product warranty are made at the time products are sold or when specific warranty issues are identified on OE products. These estimates are established using historical information about the nature, frequency, and average cost of warranty claims. We actively study trends of our warranty claims and take action to improve product quality and minimize warranty claims. We believe that the warranty reserve is appropriate; however, actual claims incurred could differ from the original estimates, requiring adjustments to the reserve. The reserve is included in both current and long-term liabilities on the balance sheet.

Below is a table that shows the activity in the warranty accrual accounts:

	Three Months Ended March 31,	
	2011	**2010**
	(Millions)	
Beginning Balance January 1,	$ 33	$ 32
Accruals related to product warranties	1	4
Reductions for payments made	(1)	(4)
Ending Balance March 31,	$ 33	$ 32

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(8) Earnings Per Share

Earnings per share of common stock outstanding were computed as follows:

	Three Months Ended March 31,	
	2011	2010
	(Millions Except Share and Per Share Amounts)	
Basic earnings per share		
Net earnings attributable to Tenneco Inc.	$ 47	$ 7
Weighted average shares of common stock outstanding	59,849,278	58,948,351
Earnings per average share of common stock	$ 0.78	$ 0.11
Diluted earnings per share		
Net earnings attributable to Tenneco Inc.	$ 47	$ 7
Weighted average shares of common stock outstanding	59,849,278	58,948,351
Effect of dilutive securities:		
Restricted stock	352,512	449,259
Stock options	1,872,733	1,413,437
Weighted average shares of common stock outstanding including dilutive securities	62,074,523	60,811,047
Earnings per average share of common stock	$ 0.75	$ 0.11

Options to purchase 201,260 and 1,671,083 shares of common stock were outstanding as of March 31, 2011 and 2010, respectively, but not included in the computation of diluted earnings per share respectively, because the options were anti-dilutive.

(9) Common Stock

Equity Plans We have granted a variety of awards, including common stock, restricted stock, restricted stock units, performance units, stock appreciation rights (SARs), and stock options to our directors, officers, and employees.

Accounting Methods We have recorded $1 million in compensation expense in each of the quarters ended March 31, 2011 and 2010, respectively, related to nonqualified stock options as part of our selling, general and administrative expense. This resulted in a decrease of $.01 in both basic and diluted earnings per share for each of the quarters ended

March 31, 2011 and 2010, respectively.

We immediately expense stock options and restricted stock awarded to employees who are eligible to retire. When employees become eligible to retire during the vesting period, we recognize the remaining expense associated with their stock options and restricted stock.

As of March 31, 2011, there was approximately $7 million of unrecognized compensation costs related to our stock options awards that we expect to recognize over a weighted average period of 1.4 years.

Compensation expense for restricted stock, restricted stock units, long-term performance units and SARs was $4 million for each of the quarters ended March 31, 2011 and 2010 respectively, and was recorded in selling, general, and administrative expense on the statement of income.

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Cash received from stock option exercises for the three months ended March 31, 2011 and 2010 was $2 million, and less than $1 million, respectively. Stock option exercises in the first three months of 2011 and 2010 would have generated an excess tax benefit of $1 million and less than $1 million, respectively. We did not record the excess tax benefit as we have federal and state net operating losses which are not currently being utilized.

Assumptions We calculated the fair values of stock option awards using the Black-Scholes option pricing model with the weighted average assumptions listed below. The fair value of share-based awards is determined at the time the awards are granted which is generally in January of each year, and requires judgment in estimating employee and market behavior.

	Three Months Ended March 31, 2011	Three Months Ended March 31, 2010
Stock Options Granted		
Weighted average grant date fair value, per share	$ 26.13	$ 11.76
Weighted average assumptions used:		
Expected volatility	70.1%	75.37%
Expected lives	4.8	4.6
Risk-free interest rates	1.8%	2.2%
Dividend yields	0.0%	0.0%

Expected volatility is calculated based on current implied volatility and historical realized volatility for the Company.

Expected lives of options are based upon the historical and expected time to post-vesting forfeiture and exercise. We believe this method is the best estimate of the future exercise patterns currently available.

The risk-free interest rates are based upon the Constant Maturity Rates provided by the U.S. Treasury. For our valuations, we used the continuous rate with a term equal to the expected life of the options.

Stock Options The following table reflects the status and activity for all options to purchase common stock for the period indicated:

	Three Months Ended March 31, 2011			
	Shares Under Option	Weighted Avg. Exercise Prices	Weighted Avg. Remaining Life in Years	Aggregate Intrinsic Value (Millions)

Outstanding Stock Options						
Outstanding, January 1, 2011	3,129,241	$	14.43	4.3	$	68
Granted	201,133		45.42			
Canceled	(56,046)		3.66			
Forfeited	(13,184)		9.36			
Exercised	(125,624)		17.10			3
Outstanding, March 31, 2011	3,135,520	$	16.53	4.4	$	80

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Restricted Stock The following table reflects the status for all nonvested restricted shares for the period indicated:

	Three Months Ended March 31, 2011		
	Shares		Weighted Avg. Grant Date Fair Value
Nonvested Restricted Shares			
Nonvested balance at January 1, 2011	558,198	$	11.58
Granted	141,036		45.42
Vested	(268,891)		12.00
Forfeited	(4,822)		13.74
Nonvested balance at March 31, 2011	425,521	$	22.51

The fair value of restricted stock grants is equal to the average market price of our stock at the date of grant. As of March 31, 2011, approximately $8 million of total unrecognized compensation costs related to restricted stock awards is expected to be recognized over a weighted-average period of approximately 2.4 years.

Long-Term Performance Units, Restricted Stock Units and SARs Long-term performance units, restricted stock units and SARs are paid in cash and recognized as a liability based upon their fair value. As of March 31, 2011, $15 million of unrecognized compensation costs is expected to be recognized over a weighted-average period of approximately 1.9 years.

(10) Pension Plans, Postretirement and Other Employee Benefits

Net periodic pension costs (income) and postretirement benefit costs (income) consist of the following components:

	Three Months Ended March 31,											
	Pension								Postretirement			
	2011				2010				2011		2010	
	US		Foreign		US		Foreign		US		US	
	(Millions)											
Service cost benefits earned during the period	$		$	2	$		$	1	$		$	
Interest cost		5		5		5		5		2		2
Expected return on plan assets		(5)		(5)		(5)		(5)				
Net amortization:												
Actuarial loss		1		1		1		1		1		1
Prior service cost										(1)		(1)

Net pension and postretirement costs	$ 1	$ 3	$ 1	$ 2	$ 2	$ 2

For the three months ended March 31, 2011, we made pension contributions of $4 million for our domestic pension plans and $5 million for our foreign pension plans. Based on current actuarial estimates, we believe we will be required to make approximately $35 million in contributions for the remainder of 2011. Pension contributions beyond 2011 will be required, but those amounts will vary based upon many factors, including the performance of our pension fund investments during 2011.

We made postretirement contributions of approximately $2 million during the first three months of 2011. Based on current actuarial estimates, we believe we will be required to make approximately $8 million in contributions for the remainder of 2011.

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The assets of some of our pension plans are invested in trusts that permit commingling of the assets of more than one employee benefit plan for investment and administrative purposes. Each of the plans participating in the trust has interests in the net assets of the underlying investment pools of the trusts. The investments for all our pension plans are recorded at estimated fair value, in compliance with the recent accounting guidance on fair value measurement.

(11) Acquisitions

In January 2010, we purchased an additional 20 percent equity interest in our Tenneco Tongtai (Dalian) Exhaust System Co. Ltd. joint venture investment in China for $15 million in cash. As a result of this purchase, our equity ownership percentage of this joint venture investment increased to 80 percent from 60 percent.

(12) Guarantees

We have from time to time issued guarantees for the performance of obligations by some of our subsidiaries, and some of our subsidiaries have guaranteed our debt. All of our existing and future material domestic wholly-owned subsidiaries fully and unconditionally guarantee our senior credit facility and our senior notes on a joint and several basis. The arrangement for the senior credit facility is also secured by first-priority liens on substantially all our domestic assets and pledges of up to 66 percent of the stock of certain first-tier foreign subsidiaries. No assets or capital stock of our direct or indirect foreign subsidiaries secure our senior notes. For additional information, refer to Note 14 of the condensed consolidated financial statements of Tenneco Inc., where we present the Supplemental Guarantor Condensed Consolidating Financial Statements.

In March 2011, we entered into two performance guarantee agreements in the U.K. between Tenneco Management Europe Limited (TMEL) and the two Walker Group Retirement Plans, the Walker Group Employee Benefit Plan and the Walker Group Executive Retirement Benefit Plan (the Walker Plans), whereby TMEL will guarantee the payment of all current and future pension contributions in event of a payment default by the sponsoring or participating employers of the Walker Plans. As a result of our decision to enter into these performance guarantee agreements, the levy due to the U.K. Pension Protection Fund will be reduced. The Walker Plans are comprised of employees from Tenneco Walker (U.K.) Limited and our Futaba Tenneco U.K. joint venture. Employer contributions are funded by both Tenneco Walker (U.K.) Limited, as the sponsoring employer and Futaba Tenneco U.K., as a participating employer. The performance guarantee agreements are expected to remain in effect until all pension obligations for the Walker Plans sponsoring and participating employers have been satisfied. The maximum amount payable for these pension performance guarantees is approximately $26 million as of March 31, 2011 which is determined by taking 105 percent of the liability of the Walker Plans calculated under section 179 of the U.K. Pension Act of 2004 offset by plan assets. We did not record an additional liability in March 2011 for this performance guarantee since Tenneco Walker (U.K.) Limited, as the sponsoring employer of the Walker Plans, already recognizes 100 percent of the pension obligation calculated based on U.S. GAAP, for all of the Walker Plans participating employers on its balance sheet, which was $8 million and $9 million at March 31, 2011 and December 31, 2010, respectively. At March 31, 2011, all pension contributions under the Walker Plans were current for all of the Walker Plans sponsoring and participating employers.

We have issued guarantees through letters of credit in connection with some obligations of our affiliates. As of March 31, 2011, we have guaranteed $53 million in letters of credit to support some of our subsidiaries insurance arrangements, foreign employee benefit programs, environmental remediation activities and cash management and capital requirements.

Negotiable Financial Instruments   One of our European subsidiaries receives payment from one of its OE customers whereby the accounts receivable are satisfied through the delivery of negotiable financial instruments. We may collect these financial instruments before their maturity date by either selling them at a discount or using them to satisfy accounts receivable that have previously been sold to a European bank. Any of these financial

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instruments which are not sold are classified as other current assets. The amount of these financial instruments that was collected before their maturity date and sold at a discount totaled $5 million and $6 million at March 31, 2011 and December 31, 2010, respectively. No negotiable financial instruments were held by our European subsidiary as of March 31, 2011 and December 31, 2010, respectively.

In certain instances, several of our Chinese subsidiaries receive payment from OE customers and satisfy vendor payments through the receipt and delivery of negotiable financial instruments. Financial instruments used to satisfy vendor payables and not redeemed totaled $8 million at both March 31, 2011 and December 31, 2010, respectively, and were classified as notes payable. Financial instruments received from OE customers and not redeemed totaled $12 million and $11 million at March 31, 2011 and December 31, 2010, respectively. We classify financial instruments received from our OE customers as other current assets if issued by a financial institution of our customers or as customer notes and accounts, net if issued by our customer. We classified $12 million and $11 million in other current assets at March 31, 2011 and December 31, 2010, respectively. Some of our Chinese subsidiaries that issue their own negotiable financial instruments to pay vendors are required to maintain a cash balance if they exceed certain credit limits with the financial institution that guarantees those financial instruments. A restricted cash balance was not required at those Chinese subsidiaries at March 31, 2011 and December 31, 2010, respectively.

The negotiable financial instruments received by one of our European subsidiaries and some of our Chinese subsidiaries are checks drawn by our OE customers and guaranteed by their banks that are payable at a future date. The use of these instruments for payment follows local commercial practice. Because negotiable financial instruments are financial obligations of our customers and are guaranteed by our customers banks, we believe they represent a lower financial risk than the outstanding accounts receivable that they satisfy which are not guaranteed by a bank.

TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

(13) Segment Information

We are a global manufacturer with three geographic reportable segments: (1) North America, (2) Europe, South America and India (Europe), and (3) Asia Pacific. Each segment manufactures and distributes ride control and emission control products primarily for the automotive industry. We have not aggregated individual operating segments within these reportable segments. We evaluate segment performance based primarily on earnings before interest expense, income taxes, and noncontrolling interests. Products are transferred between segments and geographic areas on a basis intended to reflect as nearly as possible the market value of the products.

The following table summarizes certain Tenneco Inc. segment information:

	Segment				
	North America	Europe	Asia Pacific	Reclass & Elims	Consolidated
			(Millions)		
At March 31, 2011 and for the Three Months Then Ended					
Revenues from external customers	$ 851	$ 741	$ 168	$	$ 1,760
Intersegment revenues	3	37	6	(46)	
Earnings before interest expense, income taxes, and noncontrolling interests	62	24	8		94
Total assets	1,469	1,498	539	26	3,532
At March 31, 2010 and for the Three Months Then Ended					
Revenues from external customers	$ 605	$ 561	$ 150	$	$ 1,316
Intersegment revenues	3	29	5	(37)	
Earnings before interest expense, income taxes, and noncontrolling interests	36	12	11		59
Total assets	1,242	1,365	415	12	3,034

(14) Supplemental Guarantor Condensed Consolidating Financial Statements

Basis of Presentation

Subject to limited exceptions, all of our existing and future material domestic 100% owned subsidiaries (which are referred to as the Guarantor Subsidiaries) fully and unconditionally guarantee our senior notes due in 2015, 2018, and 2020 on a joint and several basis. The Guarantor Subsidiaries are combined in the presentation below.

These consolidating financial statements are presented on the equity method. Under this method, our investments are recorded at cost and adjusted for our ownership share of a subsidiary s cumulative results of operations, capital contributions and distributions, and other equity changes. You should read the condensed consolidating financial information of the Guarantor Subsidiaries in connection with our condensed consolidated financial statements and related notes of which this note is an integral part.

Distributions

There are no significant restrictions on the ability of the Guarantor Subsidiaries to make distributions to us.

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TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

STATEMENT OF INCOME

	For the Three Months Ended March 31, 2011				
	Guarantor Subsidiaries	Nonguarantor Subsidiaries	Tenneco Inc. (Parent Company)	Reclass & Elims	Consolidated
			(Millions)		
Revenues					
Net sales and operating revenues					
External	$ 773	$ 987	$	$	$ 1,760
Affiliated companies	41	131		(172)	
	814	1,118		(172)	1,760
Costs and expenses					
Cost of sales (exclusive of depreciation and amortization shown below)	724	914		(172)	1,466
Engineering, research, and development	15	20			35
Selling, general, and administrative	33	75	1		109
Depreciation and amortization of other intangibles	18	33			51
	790	1,042	1	(172)	1,661
Other income (expense)					
Loss on sale of receivables		(1)			(1)
Other income (expense)	(1)	(3)			(4)
	(1)	(4)			(5)
Earnings (loss) before interest expense, income taxes, noncontrolling interests and equity in net income from affiliated companies	23	72	(1)		94
Interest expense					
External (net of interest capitalized)		1	27		28
	49	(15)	(34)		

Affiliated companies (net of interest income)										
Income tax expense		1		13						14
Equity in net income (loss) from affiliated companies		65				41		(106)		
Net income		38		73		47		(106)		52
Less: Net income attributable to noncontrolling interests				5						5
Net income attributable to Tenneco Inc.	$	38	$	68	$	47	$	(106)	$	47

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TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

STATEMENT OF INCOME

	For the Three Months Ended March 31, 2010				
	Guarantor Subsidiaries	Nonguarantor Subsidiaries	Tenneco Inc. (Parent Company)	Reclass & Elims	Consolidated
	(Millions)				
Revenues					
Net sales and operating revenues					
External	$ 543	$ 773	$	$	$ 1,316
Affiliated companies	31	109		(140)	
	574	882		(140)	1,316
Costs and expenses					
Cost of sales (exclusive of depreciation and amortization shown below)	519	694		(140)	1,073
Engineering, research, and development	9	18			27
Selling, general, and administrative	37	63			100
Depreciation and amortization of other intangibles	22	33			55
	587	808		(140)	1,255
Other income (expense)					
Loss on sale of receivables		(1)			(1)
Other income (loss)		(1)			(1)
		(2)			(2)
Earnings (loss) before interest expense, income taxes, noncontrolling interests, and equity in net income from affiliated companies	(13)	72			59
Interest expense					
External (net of interest capitalized)		1	31		32
Affiliated companies (net of interest income)	37	(5)	(32)		
Income tax expense (benefit)	1	14			15

Equity in net income (loss) from affiliated companies	55		6	(61)	
Net Income	4	62	7	(61)	12
Less: Net income attributable to noncontrolling interests		5			5
Net income attributable to Tenneco Inc.	$ 4	$ 57	$ 7	$ (61)	$ 7

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TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

BALANCE SHEET

	March 31, 2011				
	Guarantor Subsidiaries	Nonguarantor Subsidiaries	Tenneco Inc. (Parent Company)	Reclass & Elims	Consolidated
			(Millions)		
ASSETS					
Current assets:					
Cash and cash equivalents	$ 2	$ 197	$	$	$ 199
Receivables, net	426	1,318	23	(677)	1,090
Inventories	252	385			637
Deferred income taxes	72			(33)	39
Prepayments and other	27	137			164
Total current assets	779	2,037	23	(710)	2,129
Other assets:					
Investment in affiliated companies	469		784	(1,253)	
Notes and advances receivable from affiliates	4,137	938	5,914	(10,989)	
Long-term receivables, net		12			12
Goodwill	22	68			90
Intangibles, net	14	20			34
Deferred income taxes	50	21	20		91
Other	27	46	31		104
	4,719	1,105	6,749	(12,242)	331
Plant, property, and equipment, at cost	989	2,219			3,208
Less Accumulated depreciation and amortization	(711)	(1,425)			(2,136)
	278	794			1,072
Total assets	$ 5,776	$ 3,936	$ 6,772	$ (12,952)	$ 3,532
LIABILITIES AND SHAREHOLDERS EQUITY					
Current liabilities:					

Short-term debt (including current maturities of long-term debt)					
Short-term debt non-affiliated	$	$ 145	$ 1	$	$ 146
Short-term debt affiliated	200	344	10	(554)	
Trade payables	444	861		(100)	1,205
Accrued taxes	25	34			59
Other	125	199	51	(56)	319
Total current liabilities	794	1,583	62	(710)	1,729
Long-term debt non-affiliated		11	1,174		1,185
Long-term debt affiliated	4,601	971	5,417	(10,989)	
Deferred income taxes		57			57
Postretirement benefits and other liabilities	340	84		4	428
Commitments and contingencies					
Total liabilities	5,735	2,706	6,653	(11,695)	3,399
Redeemable noncontrolling interests		14			14
Tenneco Inc. Shareholders equity	41	1,173	119	(1,257)	76
Noncontrolling interests		43			43
Total equity	41	1,216	119	(1,257)	119
Total liabilities, redeemable noncontrolling interests and equity	$ 5,776	$ 3,936	$ 6,772	$ (12,952)	$ 3,532

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TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

BALANCE SHEET

	December 31, 2010				
	Guarantor Subsidiaries	Nonguarantor Subsidiaries	Tenneco Inc. (Parent Company)	Reclass & Elims	Consolidated
			(Millions)		
ASSETS					
Current assets:					
Cash and cash equivalents	$	$ 233	$	$	$ 233
Receivables, net	402	1,106	24	(706)	826
Inventories	221	326			547
Deferred income taxes	103			(65)	38
Prepayments and other	35	111			146
Total current assets	761	1,776	24	(771)	1,790
Other assets:					
Investment in affiliated companies	391		707	(1,098)	
Notes and advances receivable from affiliates	4,119	788	5,853	(10,760)	
Long-term receivables, net	1	8			9
Goodwill	22	67			89
Intangibles, net	14	18			32
Deferred income taxes	37	21	34		92
Other	26	46	33		105
	4,610	948	6,627	(11,858)	327
Plant, property, and equipment, at cost	997	2,112			3,109
Less Accumulated depreciation and amortization	(713)	(1,346)			(2,059)
	284	766			1,050
Total assets	$ 5,655	$ 3,490	$ 6,651	$ (12,629)	$ 3,167

LIABILITIES AND SHAREHOLDERS EQUITY

Current liabilities:

Short-term debt (including current maturities of long-term debt)										
Short-term debt non-affiliated	$		$	62	$	1	$		$	63
Short-term debt affiliated		214		371		10		(595)		
Trade payables		367		773				(92)		1,048
Accrued taxes		20		31						51
Other		130		213		47		(84)		306
Total current liabilities		731		1,450		58		(771)		1,468
Long-term debt non-affiliated				11		1,149				1,160
Long-term debt affiliated		4,583		768		5,409		(10,760)		
Deferred income taxes				56						56
Postretirement benefits and other liabilities		347		85				4		436
Commitments and contingencies										
Total liabilities		5,661		2,370		6,616		(11,527)		3,120
Redeemable noncontrolling interests				12						12
Tenneco Inc. Shareholders equity		(6)		1,069		35		(1,102)		(4)
Noncontrolling interests				39						39
Total equity		(6)		1,108		35		(1,102)		35
Total liabilities, redeemable noncontrolling interests and equity	$	5,655	$	3,490	$	6,651	$	(12,629)	$	3,167

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TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

STATEMENT OF CASH FLOWS

	Three Months Ended March 31, 2011				
	Guarantor Subsidiaries	Nonguarantor Subsidiaries	Tenneco Inc. (Parent Company)	Reclass & Elims	Consolidated
			(Millions)		
Operating Activities					
Net cash provided (used) by operating activities	$ 106	$ (160)	$ (49)	$	$ (103)
Investing Activities					
Proceeds from sale of assets	4				4
Cash payments for plant, property, and equipment	(14)	(32)			(46)
Cash payments for software related intangible assets	(1)	(2)			(3)
Net cash used by investing activities	(11)	(34)			(45)
Financing Activities					
Retirement of long-term debt			(22)		(22)
Increase (decrease) in bank overdrafts		7			7
Net increase (decrease) in revolver borrowings and short-term debt excluding current maturities of long-term debt and short-term borrowings secured by accounts receivables			47		47
Net increase (decrease) in short-term borrowings secured by accounts receivables		82			82
Intercompany dividends and net increase (decrease) in intercompany obligations	(93)	69	24		
Net cash provided (used) by financing activities	(93)	158	49		114
Effect of foreign exchange rate changes on cash and cash equivalents	2	(36)			(34)

Increase (decrease) in cash and cash equivalents					
Cash and cash equivalents, January 1		233			233
Cash and cash equivalents, March 31 (Note)	$ 2	$ 197	$	$	$ 199

Note: Cash and cash equivalents include highly liquid investments with a maturity of three months or less at the date of purchase.

TENNECO INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Continued)
(Unaudited)

STATEMENT OF CASH FLOWS

	Three Months Ended March 31, 2010				
	Guarantor Subsidiaries	Nonguarantor Subsidiaries	Tenneco Inc. (Parent Company)	Reclass & Elims	Consolidated
			(Millions)		
Operating Activities					
Net cash provided (used) by operating activities	$ 28	$ (36)	$ (49)	$	$ (57)
Investing Activities					
Proceeds from sale of assets		1			1
Cash payments for plant, property, and equipment	(15)	(23)			(38)
Cash payments for software related intangible assets	(1)	(1)			(2)
Investments and other		1			1
Net cash used by investing activities	(16)	(22)			(38)
Financing Activities					
Issuance of common shares					
Issuance of long-term debt					
Retirement of long-term debt		(1)	(7)		(8)
Debt issuance cost on long-term debt					
Increase (decrease) in bank overdrafts		(1)			(1)
Net increase (decrease) in revolver borrowings and short-term debt excluding current maturities of long-term debt and short-term borrowings secured by accounts receivables		2			2
Net increase (decrease) in short-term borrowings secured by accounts receivables		126			126
Intercompany dividends and net increase (decrease) in intercompany obligations	(32)	(24)	56		
Distribution to noncontrolling interests partners		(1)			(1)
Net cash provided (used) by financing activities	(32)	101	49		118

Effect of foreign exchange rate changes on cash and cash equivalents		3			3
Increase (decrease) in cash and cash equivalents	(20)	46			26
Cash and cash equivalents, January 1	20	147			167
Cash and cash equivalents, March 31 (Note)	$	$ 193	$	$	$ 193

Note: Cash and cash equivalents include highly liquid investments with a maturity of three months or less at the date of purchase.

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

As you read the following review of our financial condition and results of operations, you should also read our condensed consolidated financial statements and related notes beginning on page 5.

Executive Summary

We are one of the world s leading manufacturers of automotive emission control and ride control products and systems for light, commercial and specialty vehicle applications. We serve both original equipment (OE) vehicle designers and manufacturers and the repair and replacement markets, or aftermarket, globally through leading brands, including Monroe®, Rancho®, Clevite® Elastomers, Marzocchi® and Fric Rot™ ride control products and Walker®, Fonos™, and Gillet™ emission control products. We serve more than 64 different original equipment manufacturers, and our products or systems are included on nine of the top 10 passenger models produced in Europe and nine of the top 10 light truck models produced in North America for 2010. Our aftermarket customers are comprised of full-line and specialty warehouse distributors, retailers, jobbers, installer chains and car dealers. As of December 31, 2010, we operated 86 manufacturing facilities worldwide and employed approximately 22,000 people to service our customers demands.

Factors that continue to be critical to our success include winning new business awards, managing our overall global manufacturing footprint to ensure proper placement and workforce levels in line with business needs, maintaining competitive wages and benefits, maximizing efficiencies in manufacturing processes and reducing overall costs. In addition, our ability to adapt to key industry trends, such as a shift in consumer preferences to other vehicles in response to higher fuel costs and other economic and social factors, increasing technologically sophisticated content, changing aftermarket distribution channels, increasing environmental standards and extended product life of automotive parts, also play a critical role in our success. Other factors that are critical to our success include adjusting to economic challenges such as increases in the cost of raw materials and our ability to successfully reduce the impact of any such cost increases through material substitutions, cost reduction initiatives and other methods.

Light vehicle production in 2010 continued to strengthen in all regions in which we operate, from the recession that began in 2008. North American light vehicle production was up 39 percent from 2009, while in Europe, light vehicle production in 2010 was up 15 percent from 2009. For the first quarter of 2011, light vehicle production has continued to improve in most geographic regions in which we operate. Light vehicle production was up 13 percent in North America, 10 percent in Europe and seven percent in China.

We have a substantial amount of indebtedness. As such, our ability to generate cash both to fund operations and service our debt is also a significant area of focus for our company. See Liquidity and Capital Resources below for further discussion of cash flows and Item 1A, Risk Factors included in our Annual Report on Form 10-K for the year ended December 31, 2010.

Total revenues for the first quarter of 2011 were $1,760 million, a 34 percent increase from $1,316 million in the first quarter of 2010. Excluding the impact of currency and substrate sales, revenue was up $244 million, or 23 percent, driven primarily by higher OE production in most geographic regions in which we operate, our strong positions on some of the best-selling vehicle platforms globally, higher aftermarket sales globally and new launches of light and commercial vehicle programs.

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Cost of sales: Cost of sales for the first quarter of 2011 was $1,466 million, or 83.3 percent of sales, compared to $1,073 million, or 81.5 percent of sales in the first quarter of 2010. The following table lists the primary drivers behind the change in cost of sales ($ millions).

Quarter ended March 31, 2010	$ 1,073
Volume and mix	326
Material	22
Currency	38
Restructuring	(3)
Other Costs	10
Quarter ended March 31, 2011	$ 1,466

The increase in cost of sales was due primarily to the year-over-year increase in production volumes, the impact of foreign currency, and higher material and other costs, mainly manufacturing.

Gross margin: Gross margin for the first three months of 2011 was 16.7 percent, down 1.8 percentage points from 18.5 percent in the first three months of 2010. The gross margin decline was primarily driven by a higher mix of OE revenues, higher substrate sales and the negative margin impact of material cost recoveries, which together had a 1.7 percentage point impact on gross margin. The remaining effects on gross margin resulting from higher volumes, lower restructuring and related expenses, unfavorable currency and pricing, primarily related to contractual price reductions, largely offset each other.

Engineering, research and development: Engineering, research and development expense was $35 million and $27 million in the first quarter of 2011 and 2010, respectively. Increased spending to support customer programs, technology applications, and growth in emerging markets, drove the increase in expense year-over-year.

Selling, general and administrative: Selling, general and administrative expense was up $9 million in the first quarter of 2011, at $109 million, compared to $100 million in the first quarter of 2010. Investments in new facilities in China and Thailand primarily drove the increase in expense year-over-year.

Depreciation and amortization: Depreciation and amortization expense in the first three months of 2011 was $51 million, compared to $55 million in the first three months of 2010. Included in 2010 was $1 million of restructuring and related expenses.

Goodwill impairment: There were no goodwill impairment charges in either first quarter of 2011 or 2010.

Earnings before interest expense, taxes and noncontrolling interests (EBIT) was $94 million for the first quarter of 2011, an improvement of $35 million, when compared to $59 million in the first quarter of 2010. Higher OE revenues, stronger margins on new light and commercial vehicle launches, lower depreciation and amortization expense, decreased restructuring and related costs, and higher aftermarket sales drove the year-over-year increase to EBIT. Partially offsetting the increase were higher selling, general, administrative and engineering spending, $1 million of negative currency and unfavorable pricing, primarily related to contractual price reductions.

Results from Operations

Net Sales and Operating Revenues for the Three Months Ended March 31, 2011 and 2010

The following tables reflect our revenues for 2011 and 2010. We present these reconciliations of revenues in order to reflect the trend in our sales in various product lines and geographic regions separately from the effects of doing business in currencies other than the U.S. dollar. We have not reflected any currency impact in the 2010 table since this is the base period for measuring the effects of currency during 2011 on our operations. We believe investors find this information useful in understanding period-to-period comparisons in our revenues.

Additionally, we show the component of our revenue represented by substrate sales in the following tables. While we generally have primary design, engineering and manufacturing responsibility for OE emission control systems, we do not manufacture substrates. Substrates are porous ceramic filters coated with a catalyst precious metals such as platinum, palladium and rhodium. These are supplied to us by Tier 2 suppliers as directed by our OE

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customers. We generally earn a small margin on these components of the system. As the need for more sophisticated emission control solutions increases to meet more stringent environmental regulations, and as we capture more diesel aftertreatment business, these substrate components have been increasing as a percentage of our revenue. While these substrates dilute our gross margin percentage, they are a necessary component of an emission control system. We view the growth of substrates as a key indicator that our value-add content in an emission control system is moving toward the higher technology hot-end gas and diesel business.

Our value-add content in an emission control system includes designing the system to meet environmental regulations through integration of the substrates into the system, maximizing use of thermal energy to heat up the catalyst quickly, efficiently managing airflow to reduce back pressure as the exhaust stream moves past the catalyst, managing the expansion and contraction of the emission control system components due to temperature extremes experienced by an emission control system, using advanced acoustic engineering tools to design the desired exhaust sound, minimizing the opportunity for the fragile components of the substrate to be damaged when we integrate it into the emission control system and reducing unwanted noise, vibration and harshness transmitted through the emission control system.

We present these substrate sales separately in the following table because we believe investors utilize this information to understand the impact of this portion of our revenues on our overall business and because it removes the impact of potentially volatile precious metals pricing from our revenues. While our original equipment customers generally assume the risk of precious metals pricing volatility, it impacts our reported revenues. Excluding substrate catalytic converter and diesel particulate filter sales removes this impact.

	Three Months Ended March 31, 2011				
	Revenues	Currency Impact	Revenues Excluding Currency	Substrate Sales Excluding Currency	Revenues Excluding Currency and Substrate Sales
			(Millions)		
North America Original Equipment					
Ride Control	$ 152	$ 2	$ 150	$	$ 150
Emission Control	526		526	249	277
Total North America Original Equipment	678	2	676	249	427
North America Aftermarket					
Ride Control	127	1	126		126
Emission Control	46	1	45		45
Total North America Aftermarket	173	2	171		171
Total North America	851	4	847	249	598
Europe Original Equipment					
Ride Control	139	3	136		136
Emission Control	376	16	360	122	238
Total Europe Original Equipment	515	19	496	122	374
Europe Aftermarket					
Ride Control	44	1	43		43

Emission Control	30	1	29		29
Total Europe Aftermarket	74	2	72		72
South America & India	152	7	145	25	120
Total Europe, South America & India	741	28	713	147	566
Asia	131	5	126	20	106
Australia	37	5	32	3	29
Total Asia Pacific	168	10	158	23	135
Total Tenneco	$ 1,760	$ 42	$ 1,718	$ 419	$ 1,299

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	Three Months Ended March 31, 2010				
	Revenues	Currency Impact	Revenues Excluding Currency	Substrate Sales Excluding Currency	Revenues Excluding Currency and Substrate Sales
			(Millions)		
North America Original Equipment					
Ride Control	$ 128	$	$ 128	$	$ 128
Emission Control	326		326	135	191
Total North America Original Equipment	454		454	135	319
North America Aftermarket					
Ride Control	113		113		113
Emission Control	38		38		38
Total North America Aftermarket	151		151		151
Total North America	605		605	135	470
Europe Original Equipment					
Ride Control	116		116		116
Emission Control	269		269	86	183
Total Europe Original Equipment	385		385	86	299
Europe Aftermarket					
Ride Control	39		39		39
Emission Control	27		27		27
Total Europe Aftermarket	66		66		66
South America & India	110		110	13	97
Total Europe, South America & India	561		561	99	462
Asia	111		111	25	86
Australia	39		39	2	37
Total Asia Pacific	150		150	27	123
Total Tenneco	$ 1,316	$	$ 1,316	$ 261	$ 1,055

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	Three Months Ended March 31, 2011 Versus Three Months Ended March 31, 2010 Dollar and Percent Increase (Decrease)			
	Revenues	Percent	Revenues Excluding Currency and Substrate Sales	Percent
	(Millions Except Percent Amounts)			
North America Original Equipment				
Ride Control	$ 24	19%	$ 22	17%
Emission Control	200	61%	86	45%
Total North America Original Equipment	224	49%	108	34%
North America Aftermarket				
Ride Control	14	13%	13	12%
Emission Control	8	20%	7	18%
Total North America Aftermarket	22	15%	20	13%
Total North America	246	41%	128	27%
Europe Original Equipment				
Ride Control	23	19%	20	17%
Emission Control	107	40%	55	31%
Total Europe Original Equipment	130	34%	75	26%
Europe Aftermarket				
Ride Control	5	13%	4	10%
Emission Control	3	12%	2	7%
Total Europe Aftermarket	8	12%	6	9%
South America & India	42	37%	23	22%
Total Europe, South America & India	180	32%	104	22%
Asia	20	17%	20	22%
Australia	(2)	(4)%	(8)	(18)%
Total Asia Pacific	18	12%	12	10%
Total Tenneco	$ 444	34%	$ 244	23%

Light Vehicle Industry Production by Region for Three Months Ended March 31, 2011 and 2010 (According to IHS Automotive, April, 2011)

Three Months Ended March 31,
Increase

	2011	2010	(Decrease)	% Increase
	(Number of Vehicles in Thousands)			
North America	3,261	2,894	367	13%
Europe	5,310	4,841	469	10%
South America	991	921	70	8%
India	949	779	170	22%
Total Europe, South America & India	7,250	6,541	709	11%
China	4,496	4,184	312	7%
Australia	52	62	(10)	(15)%

North American light vehicle production increased 13 percent, while industry Class 8 commercial vehicle production was up 56 percent and industry Class 4-7 commercial vehicle production was up five percent in the first quarter of 2011 when compared to the first quarter of 2010. Revenues from our North American operations increased in the first three months of 2011 compared to last year s first three months due to higher OE and aftermarket sales of both product lines. The increase in North American OE revenues was primarily driven by improved production volumes, which accounted for $221 million of the year-over-year change in revenues, on Tenneco-supplied vehicles such as the Ford Super-Duty pick-up, GM s crossover models and the Toyota Tundra. Also contributing to the increase were incremental commercial vehicle revenues and a favorable $2 million currency impact on OE revenue year-over-year. The increase in aftermarket revenue for North America was primarily due to higher customer demand in both product lines which resulted in a combined increase in revenue of $20 million. Favorable currency impacted aftermarket revenue by $2 million year-over-year.

Our European, South American and Indian segment s revenues increased in the first quarter of 2011 compared to last year s first quarter, due to increased sales in all European business units as well as in South America and India. The first quarter total European light vehicle industry production was up 10 percent, while industry Class 8 commercial vehicle production was up 52 percent and industry Class 4-7 commercial vehicle production was up 44 percent in the first three months of 2011 when compared to the first three months of 2010. Improved volumes due to higher OE production on platforms such as the VW Golf, BMW 1 and 3 Series and the Daimler Sprinter were the primary driver of our increased Europe OE revenues and contributed to an increase in revenue of $100 million. European OE revenue also benefited compared to last year, from improved pricing, mainly material cost recovery and favorable foreign currency which had a combined impact of $30 million. Excluding currency, European aftermarket revenues improved compared to last year on higher ride control sales volumes which had a $6 million impact, tied in part to heavy duty sales, as well as higher emission control sales volumes of $3 million. Light vehicle production increased eight percent in South America and 22 percent in India for the first quarter of 2011 when compared to the first quarter of 2010. South American and Indian revenues were higher in the first quarter of 2011 when compared to the prior year s first quarter primarily due to stronger OE and aftermarket volumes in both regions, which increased revenue by $32 million. Currency also added $7 million to South American and Indian revenue.

Industry light vehicle production for 2011 in the first quarter increased seven percent in China but decreased 15 percent in Australia year-over-year. Revenues from our Asia Pacific segment, which includes Australia and Asia, increased due to higher sales in Asia. Asian revenues for 2011 improved from last year, primarily due to $14 million from stronger production volumes, particularly in China on key Tenneco-supplied GM, VW and Nissan platforms. A $6 million negative impact on revenue due to lower OE production volumes drove the first quarter 2011 revenue decrease for Australia over the first quarter of 2010. Currency benefited revenue by $5 million each in Asia and Australia.

Earnings before Interest Expense, Income Taxes and Noncontrolling Interests (EBIT) for the Three Months Ended March 31, 2011 and 2010

	Three Months Ended March 31,		
	2011	2010	Change
		(Millions)	
North America	$ 62	$ 36	$ 26
Europe, South America and India	24	12	12
Asia Pacific	8	11	(3)
	$ 94	$ 59	$ 35

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The EBIT results shown in the preceding table include the following items, discussed below under Restructuring and Other Charges and Liquidity and Capital Resources Capitalization, which have an effect on the comparability of EBIT results between periods:

	Three Months Ended March 31, 2011	2010
	(Millions)	
North America		
Restructuring and related expenses	$	$ 4
Europe, South America and India		
Restructuring and related expenses	1	1
Asia Pacific		
Restructuring and related expenses		

EBIT for North American operations was $62 million in the first quarter of 2011, an increase of $26 million from $36 million in the first quarter one year ago. The benefits to EBIT from higher OE revenues, stronger margins on new light and commercial vehicle launches, lower depreciation and amortization expense and improved aftermarket revenues were partially offset by unfavorable pricing, mainly contractual price reductions, increased material spending and higher selling, general, administrative and engineering costs. There were no restructuring and related expenses in the first three months of 2011 compared to $4 million of restructuring and related expenses in the first three months of 2010.

Our European, South American and Indian segment s EBIT was $24 million for the first quarter of 2011, up $12 million from $12 million in the first quarter of 2010. The increase was driven by higher OE production volumes and the related manufacturing efficiencies, new platform launches, higher aftermarket sales and material cost management activities. Unfavorable pricing, mainly contractual price reductions and increased selling, general, and administrative costs partially offset the increase. Restructuring and related expenses of $1 million were included in EBIT for the first three months of both 2011 and 2010.

EBIT for our Asia Pacific segment, which includes Asia and Australia, decreased $3 million to $8 million in the first quarter of 2011 from $11 million in the prior year s first quarter. The EBIT improvement from higher volumes and material cost management in Asia were more than offset by volume declines in Australia, unfavorable pricing, mainly contractual price reductions, and increased selling, general, administrative costs to support new plants in China and Thailand and engineering costs to support growth projects in these markets and Japan. Currency had a $1 million unfavorable impact on 2011 EBIT for our Asia Pacific segment.

Currency had a $1 million unfavorable impact on overall company EBIT for 2011 as compared to the prior year.

EBIT as a Percentage of Revenue for the Three Months Ended March 31, 2011 and 2010

	Three Months Ended March 31, 2011	2010

North America	7%	6%
Europe, South America & India	3%	2%
Asia Pacific	5%	7%
Total Tenneco	5%	4%

In North America, EBIT as a percentage of revenue for the first quarter of 2011 was up one percentage point when compared to last year s first quarter. The increase in EBIT from higher OE revenues, new platform launches, lower depreciation and amortization expense, higher aftermarket revenues and decreased restructuring and related charges was partially offset as a percentage of revenue by unfavorable pricing, increased material spending and higher selling, general, administrative and engineering costs. In Europe, South America and India, EBIT margin for the first three months of 2011 was one percentage point higher than the prior year s first three months due to improved volumes, the related manufacturing efficiencies, new platform launches, material cost management actions, and higher aftermarket revenues partially offset by unfavorable pricing and increased selling, general, and administrative expenses. EBIT as a percentage of revenue for our Asia Pacific segment decreased two percentage points in the first quarter of 2011 versus the prior year s first quarter as higher volumes and material cost management activities in Asia were more than offset as a percentage of revenue by decreased volumes in Australia, unfavorable pricing, increased selling, general, administrative and engineering expenses and the negative impact of currency.

Interest Expense, Net of Interest Capitalized

We reported interest expense in the first quarter of 2011 of $28 million net of interest capitalized of $1 million ($27 million in our U.S. operations and $1 million in our foreign operations), down from $32 million net of interest capitalized of $1 million ($31 million in our U.S. operations and $1 million in our foreign operations) in the first quarter of 2010. Included in the first three months of 2011 was $1 million of expense related to our refinancing activities. Excluding the refinancing expenses, interest expense decreased in the first quarter of 2011 compared to the first quarter of the prior year as a result of our lower average borrowings due to our operating cash performance and lower rates due to last year s debt refinancing transactions.

On March 31, 2011, we had $990 million in long-term debt obligations that have fixed interest rates. Of that amount, $500 million is fixed through December 2020, $250 million is fixed through November 2015, $225 million is fixed through August 2018 and the remainder is fixed from 2011 through 2025. We also have $198 million in long-term debt obligations that are subject to variable interest rates. For more detailed explanations on our debt structure and senior credit facility refer to Liquidity and Capital Resources Capitalization later in this Management s Discussion and Analysis.

Income Taxes

Income tax expense was $14 million for the first quarter of 2011. The tax expense recorded for the first quarter 2011 differs from a statutory rate of 35 percent due to a net tax benefit of $10 million primarily related to U.S. taxable income with no associated tax expense due to our net operating loss position and income generated in lower tax rate jurisdictions, partially offset by the impact of recording a valuation allowance against the tax benefit for losses in certain foreign jurisdictions. In the first quarter of 2010, we recorded income tax expense of $15 million. The tax expense recorded differs from the expense that would have been recorded using a statutory rate of 35 percent because of $5 million in non-cash tax charges related to adjustments to prior year income tax estimates and the impact of not benefiting tax losses in the U.S. and certain foreign jurisdictions offset by a favorable mix of tax rates in the jurisdictions we pay taxes.

Restructuring and Other Charges

Over the past several years, we have adopted plans to restructure portions of our operations. These plans were approved by our Board of Directors and were designed to reduce operational and administrative overhead costs throughout the business. In 2010, we incurred $19 million in restructuring and related costs, of which $14 million was recorded in cost of sales and $5 million was recorded in depreciation and amortization expense. In the first quarter of 2011, we incurred $1 million in restructuring and related costs, all of which was recorded in cost of sales.