DONALDSON CO INC
Form 10-K
September 25, 2009
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-K

x **Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934** for the fiscal year ended July 31, 2009 or

o **Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**
for the transition period from __________ to __________

Commission File Number: 1-7891

DONALDSON COMPANY, INC.

(Exact name of registrant as specified in its charter)

Delaware	**41-0222640**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1400 West 94th Street, Minneapolis, Minnesota	**55431**
(Address of principal executive offices)	(Zip Code)

Registrant s telephone number, including area code: (952) 887-3131
Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, $5 Par Value	New York Stock Exchange
Preferred Stock Purchase Rights	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: NONE

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No o

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

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 x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, 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 short period that the registrant was required to submit and post such files) Yes o No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. 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 x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

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

As of January 31, 2009, the last business day of the registrant s most recently completed second fiscal quarter, the aggregate market value of voting and non-voting common stock held by non-affiliates of the registrant was $2,375,100,091 (based on the closing price of $31.12 as reported on the New York Stock Exchange as of that date).

As of August 31, 2009, there were approximately 77,279,071 shares of the registrant s common stock outstanding.

Documents Incorporated by Reference

Portions of the registrant s Proxy Statement for its 2009 annual meeting of stockholders (the 2009 Proxy Statement) are incorporated by reference in Part III, as specifically set forth in Part III.

DONALDSON COMPANY, INC.

ANNUAL REPORT ON FORM 10-K

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PART I

Item 1. Business

General

Donaldson Company, Inc. (Donaldson or the Company) was founded in 1915 and organized in its present corporate form under the laws of the State of Delaware in 1936.

The Company is a worldwide manufacturer of filtration systems and replacement parts. The Company s product mix includes air and liquid filtration systems and exhaust and emission control products. Products are manufactured at 40 plants around the world and through three joint ventures. The Company has two reporting segments: Engine Products and Industrial Products. Products in the Engine Products segment consist of air filtration systems, exhaust and emissions systems, liquid filtration systems and replacement parts. The Engine Products segment sells to original equipment manufacturers (OEMs) in the construction, mining, agriculture, aerospace, defense, and truck markets and to independent distributors, OEM dealer networks, private label accounts and large equipment fleets. Products in the Industrial Products segment consist of dust, fume and mist collectors, compressed air purification systems, liquid filtration systems, air filter systems for gas turbines, and specialized air filtration systems for diverse applications including computer hard disk drives. The Industrial Products segment sells to various industrial end-users, OEMs of gas-fired turbines and OEMs and end-users requiring clean air.

The table below shows the percentage of total net sales contributed by the principal classes of similar products for each of the last three fiscal years:

	Year Ended July 31		
	2009	2008	2007
Engine Products segment			
Off-Road Equipment Products (including Aerospace and Defense products)	20%	20%	18%
On-Road Products	4%	6%	9%
Aftermarket Products (including replacement part sales to the Company s OEM s)	30%	29%	30%
Industrial Products segment			
Industrial Filtration Solutions Products	27%	27%	27%
Gas Turbine Systems Products	11%	10%	8%
Special Applications Products	8%	8%	8%

Financial information about segment operations appears in Note J in the Notes to Consolidated Financial Statements on page 51.

The Company makes its annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, and amendments to those reports, available free of charge through its website, at www.donaldson.com, as soon as reasonably practicable after it electronically files such material with (or furnishes such material to) the Securities and Exchange Commission. Also available on the Company s website are corporate governance documents, including the Company s code of business conduct and ethics, corporate governance guidelines, Audit Committee charter, Human Resources Committee charter, and Corporate Governance Committee charter. These documents are available in print, free of charge to any shareholder who requests them. The information contained on the Company s website is not incorporated by reference into this Annual Report on Form 10-K and should not be considered to be part of this Form 10-K.

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Seasonality

In general, the Company s Engine and Industrial Products segments are not considered to be seasonal. However, a number of the Company s end markets are dependent on the construction, agricultural and power generation industries, which are generally stronger in the second half of the Company s fiscal year.

Competition

Principal methods of competition in both the Engine and Industrial Products segments are technology, price, geographic coverage, service and product performance. The Company competes in a number of highly competitive filtration markets in both segments. The Company believes it is a market leader with many of its product lines. The Company believes within the Engine Products segment it is a market leader in its Off-Road Equipment and On-Road Products lines for OEMs and is a significant participant in the aftermarket for replacement filters. The Engine Products segment s principal competitors include several large global competitors and regional competitors, especially in the Engine Aftermarket Products business. The Industrial Products segment s principal competitors vary from country to country and include several large regional and global competitors and a significant number of smaller competitors who compete in a specific geographical region or in a limited number of product applications.

Raw Materials

The principal raw materials that the Company uses are steel, filter media and plastics. The Company purchases a variety of types of steel. Commodity prices were high during the first half of the year, but decreased during the second half such that the full year was comparable with Fiscal 2008. The Company experienced no significant supply problems in the purchase of its raw materials. The Company typically has multiple sources of supply for the raw materials essential to its business. The Company is not required to carry significant amounts of raw material inventory to secure supplier allotments. However, the Company does stock finished goods inventory at its regional distribution centers in order to meet anticipated Customer demand.

Patents and Trademarks

The Company owns various patents and trademarks, which it considers in the aggregate to constitute a valuable asset, including patents and trademarks for products sold under the Ultra-Web®, PowerCore®, and Donaldson® trademarks. However, it does not regard the validity of any one patent or trademark as being of material importance.

Major Customers

There were no Customers that accounted for over 10 percent of net sales in Fiscal 2009. Sales to Caterpillar Inc. and its subsidiaries (Caterpillar) accounted for 10 percent of net sales in Fiscal 2008 and Fiscal 2007. Caterpillar has been a customer of the Company for many years and purchases many models and types of products for a variety of applications. Sales to the U.S. Government do not constitute a material portion of the Company s business. There were no Customers over 10 percent of gross accounts receivable in Fiscal 2009 or 2008.

Backlog

At August 31, 2009, the backlog of orders expected to be delivered within 90 days was $259,181,000. All of this backlog is expected to be shipped during Fiscal 2010. The 90-day backlog at August 31, 2008, was $415,078,000. Backlog is one of many indicators of business conditions in the Company s markets. However, it is not always indicative of future results for a number of reasons, including short lead times in the Company s replacement parts business and the timing of orders in many of the Company s Engine OEM and Industrial markets.

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Research and Development

During Fiscal 2009, the Company spent $40,643,000 on research and development activities. Research and development expenses include basic scientific research and the application of scientific advances to the development of new and improved products and their uses. The Company spent $43,757,000 in Fiscal 2008 and $36,458,000 in Fiscal 2007 on research and development activities. Substantially all commercial research and development is performed in-house.

Environmental Matters

The Company does not anticipate any material effect on its capital expenditures, earnings or competitive position during Fiscal 2010 due to compliance with government regulations regulating the discharge of materials into the environment or otherwise relating to the protection of the environment.

Employees

The Company employed over 10,600 persons in worldwide operations as of August 31, 2009.

Geographic Areas

Financial information about geographic areas appears in Note J of the Notes to Consolidated Financial Statements on page 51.

Item 1A. Risk Factors

There are inherent risks and uncertainties associated with our global operations that involve the design, manufacturing and sale of products for highly demanding Customer applications throughout the world. These risks and uncertainties associated with our business could adversely affect our operating performance and financial condition. The following discussion, along with discussions elsewhere in this report, outlines the risks and uncertainties that we believe are the most material to our business. In light of the current global economic slowdown, we want to further highlight the risks and uncertainties associated with: world economic factors; the reduction in sales volume and orders due to decreased global demand and Customers aggressively working to reduce their levels of inventory; increased governmental laws and regulations, including the unprecedented financial actions being undertaken by governments around the world; a significant tightening of credit availability; and potential global health outbreaks. We undertake no obligation to publicly update or revise any forward-looking statements.

Operating internationally carries risks which could negatively affect our financial performance.

We have sales and manufacturing operations throughout the world, with the heaviest concentrations in North America, Europe and Asia. Our stability, growth and profitability are subject to a number of risks of doing business internationally that could harm our business, including:

- political and military events,
- legal and regulatory requirements, including import, export and defense regulations,
- tariffs and trade barriers,
- potential difficulties in staffing and managing local operations,
- credit risk of local Customers and distributors,
- difficulties in protecting intellectual property,
- local economic, political and social conditions, specifically in China and Thailand where we have significant investments, and
- potential global health outbreaks.

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Maintaining a competitive advantage requires continuing investment with uncertain returns.

We operate in highly competitive markets and have numerous competitors who may already be well established in those markets. We expect our competitors to continue improving the design and performance of their products and to introduce new products that could be competitive in both price and performance. We believe that we have certain technological advantages over our competitors, but maintaining these advantages requires us to continually invest in research and development, sales and marketing and Customer service and support. There is no guarantee that we will be successful in maintaining these advantages. We make investments in new technologies that address increased performance and regulatory requirements around the globe. There is no guarantee that we will be successful in completing development or achieving sales of these products or that the margins on such products will be acceptable. Our financial performance may be negatively impacted if a competitor s successful product innovation reaches the market before ours or gains broader market acceptance.

Several of our major OEM Customers also manufacture filtration systems. Although these OEM Customers rely on us and other suppliers for some of their filtration systems, they sometimes choose to manufacture additional filtration systems for their own use. There is also a risk that a Customer could acquire one or more of our competitors.

We may be adversely impacted by changes in technology that could reduce or eliminate the demand for our products. These risks include:

- breakthroughs in technology which provide a viable alternative to diesel engines, and
- reduced demand for disk drive products if flash memory or a similar technology which would eliminate the need for our filtration solutions.

We participate in highly competitive markets with pricing pressure. If we are not able to compete effectively our margins and results of operations could be adversely affected.

The businesses and product lines in which we participate are very competitive and we risk losing business based on a wide range of factors, including technology, price, delivery, product performance and Customer service. Large Customers continue to seek productivity gains and lower prices from their suppliers. We may lose business or negatively impact our margins if we are unable to deliver the best value to our Customers.

Demand for our products relies on economic and industrial conditions worldwide.

Demand for our products tends to respond to varying levels of construction, agricultural, mining and industrial activity in the United States and in other industrialized nations.

Sales to Caterpillar accounted for slightly less than 10 percent of our net sales in Fiscal 2009 and 10 percent of our net sales in Fiscal 2008. An adverse change in Caterpillar s financial performance or a material reduction in our sales to Caterpillar could negatively impact our operating results.

Changes in our product mix impacts our financial performance.

We sell products that have varying profit margins. Our financial performance can be impacted depending on the mix of products we sell during a given period.

Unavailable or higher cost materials could result in our Customers being dissatisfied.

We obtain raw material, including steel, filter media and plastics, and other components from third-party suppliers and tend to carry limited raw material inventories. An unanticipated delay in delivery by our suppliers could result in the inability to deliver on-time and meet the expectations of our Customers. This could negatively affect our financial performance. An increase in commodity prices during a recession or an otherwise challenging business and economic environment could result in lower operating margins.

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Difficulties with the Company s information technology systems could adversely affect the Company s results.

The Company has many information technology systems that are important to the operation of its businesses. The Company could encounter difficulties in developing new systems or maintaining and upgrading existing systems. Such difficulties could lead to significant expenses due to disruption in business operations and could adversely affect the Company s results.

Unfavorable fluctuations in foreign currency exchange rates could negatively impact our results and financial position.

We have operations in many countries. Each of our subsidiaries reports its results of operations and financial position in its relevant foreign currency, which is then translated into U.S. dollars. This translated financial information is included in our consolidated financial statements. The strengthening of the U.S. dollar in comparison to the foreign currencies of our subsidiaries could have a negative impact on our results and financial position.

Acquisitions may have an impact on our results.

We have made and continue to pursue acquisitions. We cannot guarantee that these acquisitions will have a positive impact on our results. These acquisitions could negatively impact our profitability due to operating and integration inefficiencies, the incurrence of debt, contingent liabilities and amortization expenses related to intangible assets. There are also a number of other risks involved in acquisitions. We could lose key existing Customers, have difficulties in assimilating the acquired operations, assume unanticipated legal liabilities or lose key employees.

Compliance with environmental laws and regulations can be costly.

We are subject to many environmental laws and regulations in the jurisdictions in which we operate. We routinely incur costs in order to comply with these laws and regulations. We may be adversely impacted by new or changing laws and regulations that affect both our operations and our ability to develop and sell products that meet our Customers requirements.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The Company s principal office and research facilities are located in Bloomington, Minnesota, a suburb of Minneapolis, Minnesota. The principal European administrative and engineering offices are located in Leuven, Belgium. The Company also has extensive operations in the Asia-Pacific region.

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The Company s principal plant activities are carried out in the United States and internationally. Following is a summary of the principal plants and other materially important physical properties owned or leased by the Company.

Americas
Auburn, Alabama (E)
Riverbank, California (I)*
Valencia, California (E)*
Dixon, Illinois
Frankfort, Indiana
Cresco, Iowa
Grinnell, Iowa (E)
Nicholasville, Kentucky
Bloomington, Minnesota
Chillicothe, Missouri (E)
St. Charles, Missouri* (E)
Philadelphia, Pennsylvania (I)
Greeneville, Tennessee
Baldwin, Wisconsin
Stevens Point, Wisconsin
Sao Paulo, Brazil (E)*
Athens, Canada (I)
Aguascalientes, Mexico
Monterrey, Mexico

Joint Venture Facilities
Most, Czech Republic (E)
Champaign, Illinois (E)
Jakarta, Indonesia
Dammam, Saudi Arabia (I)

Distribution Centers
Brugge, Belgium
Rensselaer, Indiana
Aguascalientes, Mexico
Johannesburg, South Africa

Europe / Middle East / Africa
Kadan, Czech Republic (I)
Klasterec, Czech Republic
Domjean, France (E)
Paris, France (E)
Dulmen, Germany (E)
Flensburg, Germany (I)
Haan, Germany (I)
Ostiglia, Italy
Barcelona, Spain (I)
Hull, United Kingdom
Leicester, United Kingdom (I)
Cape Town, South Africa
Johannesburg, South Africa*

Australia
Wyong, Australia

Asia
Hong Kong, China*
Wuxi, China
New Delhi, India
Gunma, Japan
Rayong, Thailand (I)

Third-Party Logistics Providers
Alsip, Illinois
Plainfield, Indiana (I)
New Hampton, Iowa
Waterloo, Iowa (E)
Greeneville, Tennessee (I)
Singapore

The Company s properties are utilized for both the Engine and Industrial Products segments except as indicated with an (E) for Engine or (I) for Industrial. The Company leases certain of its facilities, primarily under long-term leases. The facilities denoted with an asterisk (*) are leased facilities. In Wuxi, China, a portion of the operations are conducted in leased facilities. The Company uses third-party logistics providers for some of its product distribution and neither leases nor owns the facilities. The Company considers its properties to be suitable for their present purposes, well-maintained and in good operating condition.

Item 3. Legal Proceedings

In accordance with SFAS No. 5, Accounting for Contingencies, (SFAS No. 5), the Company records provisions with respect to identified claims or lawsuits when it is probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Claims and lawsuits are reviewed quarterly and provisions are taken or adjusted to reflect the status of a particular matter. The Company believes the recorded reserves in its consolidated financial statements are adequate in light of the probable and estimable outcomes. Any recorded liabilities were not material to the Company s financial position, results of operation and liquidity and the Company does not believe that any of the currently identified claims or litigation will materially affect its financial position, results of operation and liquidity.

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

No matters were submitted to a vote of security holders of the Company during the quarter ended July 31, 2009.

Executive Officers of the Registrant

Current information regarding executive officers is presented below. All terms of office are for one year. There are no arrangements or understandings between individual officers and any other person pursuant to which the officer was selected as an executive officer.

Name	Age	Positions and Offices Held	First Year Elected or Appointed as an Executive Officer
Tod E. Carpenter	50	Vice President, Europe and Middle East	2008
William M. Cook	56	Chairman, President and Chief Executive Officer	1994
Sandra N. Joppa	44	Vice President, Human Resources	2005
Norman C. Linnell	50	Vice President, General Counsel and Secretary	1996
Charles J. McMurray	55	Senior Vice President, Industrial Products	2003
Mary Lynne Perushek	51	Vice President and Chief Information Officer	2006
Lowell F. Schwab	61	Senior Vice President, Global Operations	1994
David W. Timm	56	Vice President, Asia-Pacific	2007
Thomas R. VerHage	56	Vice President and Chief Financial Officer	2004
Jay L. Ward	45	Senior Vice President, Engine Products	2006
Debra L. Wilfong	54	Vice President and Chief Technology Officer	2007

Mr. Carpenter joined the Company in 1996 and has held various positions, including Gas Turbine Systems General Manager from 2002 to 2004; General Manager, Industrial Filtration Systems (IFS) Sales from 2004 to 2006; General Manager, IFS Americas in 2006; and Vice President, Global IFS from 2006 to 2008. Mr. Carpenter was appointed Vice President, Europe and Middle East in August 2008.

Mr. Cook joined the Company in 1980 and has held various positions, including CFO and Senior Vice President, International from 2001 to 2004 and President and CEO from 2004 to 2005. Mr. Cook was appointed Chairman, President and CEO in July 2005.

Ms. Joppa was appointed Vice President, Human Resources and Communications in November 2005. Prior to that time Ms. Joppa held various positions at General Mills, a consumer food products company, from 1989 to 2005, including service as Director of Human Resources for several different operating divisions from 1999 to 2005.

Mr. Linnell joined the Company in 1996 as General Counsel and Secretary and was appointed Vice President, General Counsel and Secretary in 2000.

Mr. McMurray joined the Company in 1980 and has held various positions, including Director, Global Information Technology from 2001 to 2003; Vice President, Human Resources from 2004 to 2005; and Vice President, Information Technology, Europe, South Africa and Mexico from 2005 to 2006. Mr. McMurray became Senior Vice President, Industrial Products, in September 2006.

Ms. Perushek was appointed Vice President and Chief Information Officer in November 2006. Prior to that time, Ms. Perushek was Vice President of Global Information Technology at H.B. Fuller Company, a worldwide manufacturer of adhesive products, from 2005 to 2006 and Chief Information Officer for Young America Corporation, a marketing company, from 1999 to 2004.

Mr. Schwab joined the Company in 1977 and has held various positions, including Senior Vice President, Operations from 1994 to 2004 and Senior Vice President, Engine Products from 2004 to 2008. Mr. Schwab was appointed Senior Vice President, Global Operations, in August 2008.

Mr. Timm joined the Company in 1983 and has held various positions, including General Manager, Disk Drive from 1995 to 2005 and General Manager, Gas Turbine Systems Products from 2005 to 2006. Mr. Timm was appointed Vice President, Asia-Pacific in December 2006.

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Mr. VerHage was appointed Vice President and Chief Financial Officer in March 2004. Prior to that time, Mr. VerHage was a partner for Deloitte & Touche, LLP, an international accounting firm, from 2002 to 2004.

Mr. Ward joined the Company in 1998 and has held various positions, including Director, Operations from 2001 to 2003; Director, Product and Business Development, IFS Group from 2003 to 2004; Managing Director, Europe from 2004 to 2006; and Vice President, Europe and Middle East from 2006 to 2008. Mr. Ward was appointed Senior Vice President, Engine Products in August 2008.

Ms. Wilfong was appointed Vice President and Chief Technology Officer in May 2007. Prior to that time, Ms. Wilfong held various director positions in research and development at 3M Company, an international consumer products company, from 2000 to 2007, most recently as Director, Research and Development for the 3M Automotive Division from 2006 to 2007.

PART II

Item 5. Market for Registrant s Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The common shares of the Company are traded on the New York Stock Exchange under the symbol DCI. The amount and frequency of all cash dividends declared on the Company s common stock for Fiscal 2009 and 2008 appear in Note N of the Notes to Consolidated Financial Statements on page 55. As of September 23, 2009, there were 2,109 shareholders of record of common stock.

The low and high sales prices for the Company s common stock for each full quarterly period during Fiscal 2009 and 2008 were as follows:

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
Fiscal 2008	$34.40	44.59	$35.14	48.40	$38.83	44.29	$40.95	52.33
Fiscal 2009	$28.04	49.00	$23.40	36.29	$21.82	34.37	$31.00	38.93

The following table sets forth information in connection with purchases made by, or on behalf of, the Company or any affiliated purchaser of the Company, of shares of the Company s common stock during the quarterly period ended July 31, 2009.

Period	Total Number of Shares Purchased (1)	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
May 1-May 31, 2009				930,210
June 1-June 30, 2009	18,972	$ 36.12		930,210
July 1-July 31, 2009				930,210
Total	18,972	$ 36.12		930,210

(1) On March 31, 2006, the Company announced that the Board of Directors authorized the repurchase of up to 8.0 million shares of common stock. This repurchase authorization, which is effective until terminated by the Board of Directors, replaced the existing authority that was authorized on January 17, 2003. There were no repurchases of common stock made outside of the Company s current repurchase authorization during the quarter ended July 31, 2009. However, the Total Number of Shares Purchased column of the table above includes 18,972 previously owned shares tendered by option holders in payment of the exercise price of options. While not considered repurchases of shares, the Company does at times withhold shares that would otherwise be issued under equity-based awards to cover the withholding taxes due as a result of exercising stock options or payment of equity-based awards.

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The graph below compares the cumulative total stockholder return on the Company s Common Stock for the last five fiscal years with the cumulative total return of the Standard & Poor s 500 Stock Index and the Standard & Poor s Index of Industrial Machinery Companies. The graph and table assume the investment of $100 in each of the Company s Common Stock and the specified indexes at the beginning of the applicable period, and assume the reinvestment of all dividends.

COMPARISON OF 5 YEAR CUMULATIVE TOTAL RETURN
Among Donaldson Company, Inc., The S&P 500 Index
And The S&P Industrial Machinery Index

	Year ended July 31,					
	2009	2008	2007	2006	2005	2004
Donaldson Company, Inc.	$ 150.18	$ 175.88	$ 140.46	$ 125.67	$ 123.27	$ 100.00
S&P 500	99.33	124.10	139.58	120.19	114.05	100.00
S&P Industrial Machinery	102.93	133.98	146.65	113.48	108.37	100.00

Item 6. Selected Financial Data

The following table sets fourth selected financial data for each of the fiscal years in the five-year period ended July 31, 2009 (in millions, except per share data):

	Year ended July 31,				
	2009	2008	2007	2006	2005
Net sales	$ 1,868.6	$ 2,232.5	$ 1,918.8	$ 1,694.3	$ 1,595.7
Income from continuing operations	131.9	172.0	150.7	132.3	110.6
Diluted earnings per share	1.67	2.12	1.83	1.55	1.27
Total assets	1,334.0	1,548.6	1,319.0	1,124.1	1,111.8
Long-term obligations	253.7	176.5	129.0	100.5	103.3
Cash dividends declared per share	0.460	0.430	0.370	0.410	0.180
Cash dividends paid per share	0.455	0.420	0.360	0.320	0.235

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operation

Results of Operation

The following discussion of the Company s financial condition and results of operations should be read in conjunction with the Consolidated Financial Statements and Notes thereto and other financial information included elsewhere in this report.

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Overview

The Company manufactures and distributes filtration systems and replacement parts. The Company s core strengths are leading filtration technology, strong Customer relationships and global presence. The Company operates through two reporting segments, Engine Products and Industrial Products, and has a product mix including air and liquid filters and exhaust and emission control products. As a worldwide business, the Company s results of operations are affected by conditions in the global economic environment. Under normal economic conditions, the Company s diversity between its original equipment and replacement parts Customers, its diesel engine and industrial end markets, and its North American and international end markets has helped to limit the impact of weakness in any one product line, market or geography on the consolidated results of the Company. However, the global recession had a dramatic negative impact on the Company s results in Fiscal 2009 as nearly every product group and geographic area was impacted.

The Company reported sales in Fiscal 2009 of $1,868.6 million, down 16.3 percent from $2,233.5 million in the prior year. The Company s results were negatively impacted by foreign currency translation. The impact of foreign currency translation decreased sales by $76.8 million. Excluding the current year impact of foreign currency translation, worldwide sales decreased 12.9 percent during the year.

Although net sales excluding foreign currency translation is not a measure of financial performance under GAAP, the Company believes it is useful in understanding its financial results and provides a comparable measure for understanding the operating results of the Company between different fiscal periods excluding the impact of foreign currency translation. The following is a reconciliation to the most comparable GAAP financial measure of this non-GAAP financial measure (in millions):

	July 31, 2009	July 31, 2008
Net sales, excluding foreign currency translation	$ 1,945.4	$ 2,110.0
Foreign currency translation impact	(76.8)	122.5
Net sales	$ 1,868.6	$ 2,232.5

Although not as large as the impact on net sales, the Company s net earnings were also negatively impacted by foreign currency translation. The impact of foreign currency translation during the year decreased net earnings by $3.8 million. Excluding the current year impact of foreign currency translation, net earnings decreased 21.1 percent.

Although net earnings excluding foreign currency translation is not a measure of financial performance under GAAP, the Company believes it is useful in understanding its financial results and provides a comparable measure for understanding the operating results of the Company between different fiscal periods excluding the impact of foreign currency translation. The following is a reconciliation to the most comparable GAAP financial measure of this non-GAAP financial measure (in millions):

	July 31, 2009	July 31, 2008
Net earnings, excluding foreign currency translation	$ 135.7	$ 159.1
Foreign currency translation impact, net of tax	(3.8)	12.9
Net earnings	$ 131.9	$ 172.0

The Company reported diluted earnings per share of $1.67, a 21.2 percent decrease from $2.12 in the prior year.

Included in the results are pre-tax restructuring charges of $17.8 million resulting primarily from workforce reductions of 2,800 since the beginning of the year. Gross margin and operating expenses include $10.1 million and $7.7 million of restructuring expenses, respectively. The Company also realized $43.0 million in cost savings from restructuring actions completed throughout the year.

The effective tax rate for Fiscal 2009 was 18.3 percent compared to 27.2 percent in Fiscal 2008. This decrease is attributable to a number of discrete tax items, partially offset by increased expense from the repatriation of foreign earnings. Absent these items, the underlying tax rate for the Fiscal 2009 has decreased

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from Fiscal 2008 by 1.2 points to 30.4 percent. The reinstatement of the U.S. Research and Experimentation credit, changes in current year unrecognized tax benefits, reduced statutory tax rates and the mix of earnings between foreign jurisdictions all contributed to the reduction in the underlying rate.

The Company continued to improve an already strong liquidity position which allowed for continued investment in business and debt reduction while increasing cash reserves and maintaining its dividend. While Fiscal 2009 was significantly impacted by the global recession, there are signs that some of the Company s end markets have begun to stabilize. While the Company s future visibility remains limited and it s too early to call a recovery, the Company believes that the worst of the global economic downturn is behind it in many of its early and mid-cycle end markets, including the heavy truck, construction, special applications and replacement parts markets. This view is factored into the Fiscal 2010 outlook discussed below.

Following is financial information for the Company s Engine and Industrial Products segments. Corporate and Unallocated includes corporate expenses determined to be non-allocable to the segments and interest income and expense. See further discussion of segment information in Note J of the Company s Notes to Consolidated Financial Statements.

	Engine Products	Industrial Products	Corporate & Unallocated	Total Company
		(thousands of dollars)		
2009				
Net sales	$ 1,001,961	$ 866,668	$	$ 1,868,629
Earnings before income taxes	83,797	89,526	(11,898)	161,425
2008				
Net sales	$ 1,229,171	$ 1,003,350	$	$ 2,232,521
Earnings before income taxes	158,931	102,420	(25,188)	236,163
2007				
Net sales	$ 1,084,262	$ 834,566	$	$ 1,918,828
Earnings before income taxes	140,762	80,321	(16,222)	204,861

During Fiscal 2009, the Company s Engine Products segment net sales decreased as a percent of total net sales to 53.6 percent compared to 55.1 percent in the prior year. For the Company s Industrial Products segment, net sales as a percent of total net sales increased to 46.4 percent from 44.9 percent in the prior year.

Factors within the Company s reporting segments that contributed to the Company s results for Fiscal 2009 included a significant impact from the Company s distributors and OEM customers aggressively working down their inventory levels. In the Engine Products segment, the Company experienced weak business conditions in most end markets and regions. Spending in the construction and mining end-markets in the United States, Europe and Asia was down, resulting in a decrease in off-road equipment related sales. This decrease was partially offset by an increase in Aerospace and Defense sales and the benefit of the acquisition of Western Filter Corporation in October 2008. On-road Products sales decreased in the United States, Europe and Asia due to a drop in demand for new trucks, which lowered new truck build rates. Aftermarket sales also decreased due to decreases in equipment utilization in most off-road end markets and decreased freight activity which impacted on-road markets, partially offset by increases in retrofit emissions sales in the United States. In the Industrial Products segment, demand was also weak in all markets across all regions. Demand for Industrial Filtration Solutions Products was down as a result of the decline in general industrial activity. Also contributing to the decrease in Industrial Filtration Solutions Products sales was the sale of the air dryer business in Maryville, Tennessee, in October 2008, partially offset by the benefit from the acquisition of LMC West, Inc. in February of 2008. Worldwide sales in Gas Turbine Products weakened late in the year and full year sales were slightly lower as compared to the prior year. Gas Turbine Products sales are typically large systems and, as a result, the Company s shipments and revenues fluctuate from quarter to quarter. Sales of Special Applications Products were weak due to decreased demand for semiconductor fabrications and industrial uses for PTFE membranes and a sudden contraction of the disk drive market that resulted in decreased demand for the Company s hard disk drive filters.

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Following are net sales by product within both the Engine and Industrial Products segments:

	2009	2008 (thousands of dollars)	2007
Engine Products segment:			
Off-Road Products*	$ 362,785	$ 448,681	$ 352,065
On-Road Products	71,958	123,146	166,370
Aftermarket Products**	567,218	657,344	565,827
Total Engine Products segment	1,001,961	1,229,171	1,084,262
Industrial Products segment:			
Industrial Filtration Solutions Products	503,611	600,526	515,022
Gas Turbine Products	206,760	213,138	158,025
Special Applications Products	156,297	189,686	161,519
Total Industrial Products segment	866,668	1,003,350	834,566
Total Company	$ 1,868,629	$ 2,232,521	$ 1,918,828

* Includes Aerospace and Defense products.

** Includes replacement part sales to the Company s OEM Customers.

Outlook

While it appears that conditions may have stabilized at many of the Company s Customers and in many of its end markets, the Company continues to have limited visibility into the future. Consequently, the Company remains cautious in the near-term about forecasting a return to growth.

The Company is planning its total Fiscal 2010 sales to be between $1.65 and $1.75 billion, or approximately the pace of the past two quarters. For the full year Fiscal 2010 versus Fiscal 2009, sales are projected to be down 6 to 12 percent. Foreign currency translation is expected to provide a small benefit based on the Company s planned rates for the Euro of US$1.39 and 98 Yen to the US Dollar for Fiscal 2010.

The Company did not complete all of its planned restructuring actions by the end of the fourth quarter of Fiscal 2009 and anticipates there could be additional restructuring charges of up to $17 million in Fiscal 2010. Including these costs, the full year Fiscal 2010 operating margin is still expected to be between 9.5 to 10.5 percent.

The Company expects its full year Fiscal 2010 tax rate to be between 30 and 32 percent. The Company does not anticipate significant discrete tax benefits as occurred in Fiscal 2009.

The Company expects that cash generated by operating activities will exceed $150 million in Fiscal 2010. Capital spending in Fiscal 2010 is planned at $30.0 million to $40.0 million. The Company will continue to use its cash flow for dividends, potential acquisitions, capital projects and maintenance of its strong liquidity position.

Engine Products The Company expects full year sales to decrease 3 to 8 percent, inclusive of the impact of foreign currency translation.

In its On-Road Products businesses, the Company believes that global build rates for heavy- and medium-duty trucks are stabilizing at the current levels.

The Company is forecasting slightly lower sales for its Aerospace and Defense Products as the level of Customer demand for defense products is decreasing.

The Company expects activity in the global construction and mining end markets to remain at their current levels during the first half of Fiscal 2010, and anticipates Customer demand in the farm equipment market outside of North America to continue its current decline.

The Company s Aftermarket sales are expected to improve slightly from their current levels as utilization rates for both heavy trucks and off-road equipment are stabilizing. The Company expects

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to benefit from the increasing amount of equipment in the field with PowerCore® technology as well as its other proprietary filtration systems.

Industrial Products The Company forecasts full year Fiscal 2010 sales to decrease 11 to 16 percent, inclusive of the impact of foreign currency translation.

Industrial Filtration Solutions sales are projected to decrease 10 to 15 percent for the year due to difficult comparable sales in the first half of Fiscal 2010. The Company expects general manufacturing activity to remain near its current level.

The Company expects full year sales of its Gas Turbine Products to decrease 21 to 26 percent due the slowdown in demand for large power generation projects.

Special Applications Products sales are projected to be flat to down 5 percent, as conditions appear to have stabilized in the hard disk drive market but may continue to weaken in the short-term in the Company s membrane products industrial end-markets.

Fiscal 2009 Compared to Fiscal 2008

Engine Products Segment The Engine Products segment sells to OEMs in the construction, mining, agriculture, aerospace, defense, and truck markets and to independent distributors, OEM dealer networks, private label accounts and large equipment fleets. Products include air filtration systems, exhaust and emissions systems, liquid filtration systems and replacement filters.

Sales for the Engine Products segment were $1,002.0 million, a decrease of 18.5 percent from $1,229.2 million in the prior year. International Engine Products sales decreased 24.3 percent and sales in the United States decreased 12.4 percent from the prior year. The impact of foreign currency decreased sales by $38.9 million, or 3.2 percent. Earnings before income taxes as a percentage of Engine Products segment sales of 8.4 percent decreased from 12.9 percent in the prior year. The Engine Products segment has been negatively impacted by lower absorption of fixed manufacturing costs due to the drop in sales volumes and increased costs related to restructuring, offset by cost savings as a result of workforce reductions already completed, improved distribution efficiencies as compared to the prior year and the impact of cost control measures including reductions in incentive compensation.

Worldwide sales of Off-Road Products were $362.8 million, a decrease of 19.1 percent from $448.7 million in the prior year. Sales in the United States decreased 7.2 percent. Global mining activity started declining due to decreased commodity prices in the second quarter of Fiscal 2009, and remained weak throughout the remainder of the year. Spending in U.S. residential and non-residential construction markets was down more than 27 percent and 5 percent, respectively, over prior year, resulting in a decrease in the sales of the Company s products into those markets. Domestic Aerospace and Defense sales benefited from the recent acquisition of Western Filter Corporation, which resulted in $15.4 million of incremental sales over the prior year, and continued strong demand for filters for military equipment. Internationally, sales of Off-Road Products were down 31.3 percent from the prior year, with sales decreasing in both Europe and Asia by 32.5 percent and 29.5 percent, respectively. Sales in the European construction equipment end market decreased due to a decline in construction activity related to the economic downturn. Sales to the European agricultural end market also decreased. In Asia, sales have declined significantly in Japan in the construction end markets.

Worldwide sales of On-Road Products were $72.0 million, a decrease of 41.6 percent from $123.1 million in the prior year. On-Road Products sales in the United States decreased 43.2 percent from the prior year, primarily as a result of a 29 percent decrease in Class 8 truck build rates, 40 percent decrease in medium duty truck build rates by the Company s Customers and a reduction in high value product mix over the prior year. International On-Road Products sales decreased 39.6 percent from the prior year, driven by decreased sales in Europe and Asia of 51.0 percent and 32.5 percent, respectively, reflecting the current economic downturn for freight activity and new truck build rates.

Worldwide Engine Aftermarket Products sales of $567.2 million decreased 13.7 percent from $657.3 million in the prior year. Sales in the United States decreased 9.5 percent over the prior year, driven by inventory adjustments at the Company s Customers and decreases in utilization rates in the mining, construction and transportation industries, partially offset by increases in retrofit emission sales of $5.2 million. International sales decreased 17.4 percent from the prior year, primarily driven by sales decreases in Europe and Asia of 26.1 percent and 8.0 percent, respectively, due to weak economic conditions.

Industrial Products Segment The Industrial Products segment sells to various industrial end-users, OEMs of gas-fired turbines, and OEMs and end-users requiring highly purified air. Products include dust, fume and mist collectors, compressed air purification systems, liquid filters and parts, air filter systems, PTFE membrane and laminates, and specialized air filtration systems for applications including computer hard disk drives.

Sales for the Industrial Products segment were $866.7 million, a decrease of 13.6 percent from $1,003.4 million in the prior year. International Industrial Products sales decreased 14.2 percent and sales in the United States decreased 12.3 percent from the prior year. The impact of foreign currency decreased sales by $37.9 million, or 3.8 percent. Despite the 13.6 percent decrease in sales, earnings before income taxes as a percentage of Industrial Products segment sales of 10.3 percent increased from 10.2 percent in the prior year. The improvement in earnings as a percent of sales over the prior year was driven by better execution on large project shipments, cost savings from restructuring actions and the impact of cost control measures including reductions in incentive compensation expense. These were slightly offset by lower absorption of fixed costs and restructuring costs.

Worldwide sales of Industrial Filtration Solutions Products of $503.6 million decreased 16.1 percent from $600.5 million in the prior year. Sales in the United States and Europe decreased 18.3 percent and 21.0 percent, respectively. Sales in Asia remained relatively flat as compared to the prior year. The decline in Europe was due to reduced demand for industrial dust collectors and compressed air purification systems which fell with the downturn in general manufacturing activity during the year. Domestic sales decreased from the prior year as a result of this same decline in general industrial activity. The results in the year were also influenced by the sale of the air dryer business in Maryville, Tennessee, on October 31, 2008 and the acquisition of LMC West, Inc. (LMC West) in February of Fiscal 2008. The sale of the air dryer business in Maryville, Tennessee, decreased sales $7.6 million over last year. The acquisition of LMC West contributed to $7.0 million of sales during the twelve months of Fiscal 2009 and $4.7 million during the latter six months of Fiscal 2008.

Worldwide sales of Gas Turbine Products were $206.8 million, a decrease of 3.0 percent from $213.1 million in the prior year. Gas Turbine Products sales are typically large systems and, as a result, the Company s shipments and revenues fluctuate from quarter to quarter. Incoming orders declined 58 percent in Fiscal 2009 versus Fiscal 2008, a reflection of the reduced demand for power generation projects globally. This trend is expected to continue in Fiscal 2010.

Worldwide sales of Special Applications Products were $156.3 million, a 17.6 percent decrease from $189.7 million in the prior year. Domestic Special Application Products sales decreased 10.0 percent. International sales of Special Application Products decreased 18.7 percent over the prior year. The primary decreases internationally were in Europe and Asia, which decreased 25.5 and 17.3 percent, respectively, due to a significant reduction in demand for hard disk drive filters, semiconductor filtration systems and PTFE membrane filtration products. The reduction in demand is primarily a result of a worldwide contraction in the end markets for computers, data storage devices and other electronic products that began in the second quarter of Fiscal 2009.

Consolidated Results The Company reported net earnings for Fiscal 2009 of $131.9 million compared to $172.0 million in Fiscal 2008, a decrease of 23.3 percent. Diluted net earnings per share was $1.67, down 21.2 percent from $2.12 in the prior year. The Company s operating income of $170.0 million decreased from prior year operating income of $245.8 million by 30.9 percent.

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The table below shows the percentage of total operating income contributed by each segment for each of the last three fiscal years. Corporate and Unallocated includes corporate expenses determined to be non-allocable to the segments and interest income and expense:

	2009	2008	2007
Engine Products	44.5%	61.1%	62.9%
Industrial Products	51.8%	42.1%	37.8%
Corporate and Unallocated	3.7%	(3.2%)	(0.7%)
Total Company	100%	100%	100%

International operating income, prior to corporate expense allocations, totaled 77.9 percent of consolidated operating income in Fiscal 2009 as compared to 89.4 percent in Fiscal 2008. Total international operating income decreased 39.8 percent from the prior year. This decrease is attributable to restructuring charges internationally exceeding domestic restructuring costs, weaker foreign currencies and overall weak business conditions abroad. The table below shows the percentage of total operating income contributed by each major geographic region for each of the last three fiscal years:

	2009	2008	2007
United States	22.1%	10.6%	22.3%
Europe	23.3%	43.3%	34.8%
Asia	43.5%	37.9%	38.6%
Other	11.1%	8.2%	4.3%
Total Company	100%	100%	100%

Gross margin for Fiscal 2009 was 31.6 percent, a decrease from 32.5 percent in the prior year. The Company had $10.1 million in restructuring costs which reduced gross margin in the year. In addition, lower absorption of fixed costs due to the drop in production volumes, net of savings from completed restructuring related activities, negatively impacted gross margin by approximately $23 million. Partially offsetting these factors were the positive impacts of improved product mix, improved distribution efficiencies and better execution on large project shipments. During Fiscal 2008, the Company began using a new warehouse management system at its main U.S. distribution center. The company encountered start-up problems during the transition to the new systems which, although now resolved, resulted in $7.6 million in unanticipated charges in Fiscal 2008 that did not recur in Fiscal 2009. The Company also incurred a charge of approximately $5.0 million to pretax income related to the use of the Last-In, First-Out (LIFO) accounting method for its U.S. inventories, which charges increasing commodity costs to income immediately. As commodity costs were relatively flat in Fiscal 2009, the Company did not experience a similar impact from rising commodity prices.

Operating expenses for Fiscal 2009 were $419.8 million or 22.5 percent of sales, as compared to $480.1 million or 21.5 percent in the prior year. Operating expenses as a percent of sales increased due to sales volume declines and $7.7 million in restructuring cost during the year, offset by $19.4 million in benefits from restructuring actions taken and $19.5 million of lower incentive compensation expense as compared to the prior year. The Company s expense reduction programs remain in effect.

Interest expense of $17.0 million increased $0.4 million from $16.6 million in the prior year as a result of higher debt levels. Net other income totaled $8.5 million in Fiscal 2009 up from $6.9 million in the prior year. Components of other income for Fiscal 2009 were as follows: interest income of $1.6 million, earnings from non-consolidated joint ventures of $2.3 million, royalty income of $6.1 million, charitable donations of $0.6 million, foreign exchange losses of $0.4 million and other miscellaneous income and expense items resulting in expenses of $0.5 million.

The effective tax rate for Fiscal 2009 was 18.3 percent compared to 27.2 percent in Fiscal 2008. The decrease in effective rate is primarily due to the settlements of long-standing court cases and examinations in various jurisdictions for tax years 2003 through 2006, the reassessment of the corresponding unrecognized tax benefits for the subsequent open years and a favorable resolution of a foreign tax matter. Partially offsetting these effects, the Company s Fiscal 2009 tax rate was unfavorably impacted by an increased expense from the repatriation of foreign earnings. Absent these items, the underlying tax rate for the Fiscal

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2009 has decreased from Fiscal 2008 by 1.2 points to 30.4 percent. The reinstatement of the U.S. Research and Experimentation credit, changes in current year unrecognized tax benefits, reduced statutory tax rates and the mix of earnings between foreign jurisdictions all contributed to the reduction in the underlying rate.

Total backlog at July 31, 2009, was $528.0 million, down 33.7 percent from the same period in the prior year. Backlog is one of many indicators of business conditions in the Company s markets. However, it is not always indicative of future results for a number of reasons, including short lead times in the Company s replacement parts businesses and the timing of receipt of orders in many of the Company s Engine OEM and Industrial markets. In the Engine Products segment, total open order backlog decreased 31.8 percent from the prior year. In the Industrial Products segment, total open order backlog decreased 36.8 percent from the prior year. Because some of the change in backlog can be attributed to a change in the ordering patterns of the Company s Customers and/or the impact of foreign exchange translation rates, it may not necessarily correspond to future sales.

Fiscal 2008 Compared to Fiscal 2007

Engine Products Segment Sales for the Engine Products segment were $1.229 billion, an increase of 13.4 percent from $1.084 billion in the prior year, reflecting increases in the Off-Road and Aftermarket Products businesses, partially offset by decreased On-Road Products sales in the NAFTA region. The impact of foreign currency increased sales by $60.6 million, or 5.6 percent. Earnings before income taxes as a percentage of Engine Products segment sales of 12.9 percent decreased from 13.0 percent in the prior year. The Engine Products segment as a percent of sales was down slightly from last year due the impact of distribution inefficiencies and start-up costs related to the implementation of a new warehouse management system at our Rensselaer, Indiana distribution center, offset by stronger global volume across most business units.

Worldwide sales of Off-Road Products were $448.7 million, an increase of 27.4 percent from $352.1 million in the prior year. Sales in the United States showed an increase of 27.1 percent, primarily driven by the impact of the acquisition of Aerospace Filtration Systems, Inc. in March of Fiscal 2007 and robust sales in the Company s defense business due to the combination of replacement parts sales growth, new vehicle programs (including the Mine Resistant Ambush Protected armored vehicles) and retrofit programs for the Abrams Tank and military helicopters including the Black Hawk. In addition, strong sales in agriculture, mining and non-residential construction markets more than offset a decrease in residential construction markets. Internationally, sales of Off-Road Products were up 27.8 percent from the prior year, with sales increasing in both Europe and Asia by 24.4 percent and 36.3 percent, respectively, reflecting strength in the heavy construction market and increased demand for mining and agricultural equipment internationally.

Worldwide sales of On-Road Products were $123.1 million, a decrease of 26.0 percent from $166.4 million in the prior year. On-Road Products sales in the United States decreased 43.3 percent from the prior year as a result of lower new truck build rates at the Company s Customers following the implementation of the 2007 Environmental Protection Agency diesel emission regulations. International On-Road Products sales increased 14.9 percent from the prior year. On-Road Products sales in Europe benefited from stronger build rates resulting in a sales increase of 28.1 percent.

Worldwide Engine Aftermarket Products sales of $657.3 million increased 16.2 percent from $565.8 million in the prior year. Sales in the United States increased 4.6 percent over the prior year. International sales increased 28.4 percent with sales increasing in Europe, Asia and Mexico by 25.3 percent, 23.5 percent and 77.0 percent, respectively. The large percentage increase in Mexico is partially a result of transferring some Customer relationships to the Company s Mexican subsidiary from the United States to better serve the Customers. Geographic expansion and high equipment utilization rates contributed to the overall increases. In addition, sales continue to benefit from the increasing amount of equipment in the field with the Company s PowerCore filtration systems. Sales of PowerCore replacement filters increased 58.9 percent over the prior year.

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Industrial Products Segment Sales for the Industrial Products segment were $1,003.4 million, an increase of 20.2 percent from $834.6 million in the prior year, resulting from stronger sales in Industrial Filtration Solutions Products, Special Application Products and Gas Turbine Systems Products across all regions. The impact of foreign currency increased sales by $62.0 million, or 7.4 percent. Earnings before income taxes as a percentage of Industrial Products segment sales of 10.2 percent increased from 9.6 percent in the prior year. The improvement in earnings as a percent of sales over the prior year was driven by cost leverage across most business units due to strong global volumes offset slightly lower margins on a few large projects in both our Gas Turbine and Industrial Air Filtration business units.

Worldwide sales of Industrial Filtration Solutions Products of $600.5 million increased 16.6 percent from $515.0 million in the prior year. Sales in the United States, Europe, Asia and South Africa increased 9.9 percent, 22.0 percent, 16.5 percent and 25.0 percent, respectively. U.S. sales included the impact of the acquisition of LMC West, Inc. in February of Fiscal 2008. Demand was strong worldwide but specifically in Europe, where manufacturing investment conditions were favorable throughout the fiscal year.

Worldwide sales of Gas Turbine Products were $213.1 million, an increase of 34.9 percent from $158.0 million in the prior year. Growth globally has been strong in both the power generation and oil and gas markets. The Gas Turbine Products sales are typically large systems and, as a result, the Company s shipments and revenues fluctuate from quarter to quarter.

Worldwide sales of Special Applications Products were $189.7 million, a 17.4 percent increase from $161.5 million in the prior year. Sales in the United States, Europe, and Asia increased 8.3 percent, 25.3 percent, and 17.8 percent, respectively, from the prior year as sales of disk drive filters and PTFE membranes remained strong.

Consolidated Results The Company reported record net earnings for Fiscal 2008 of $172.0 million compared to $150.7 million in Fiscal 2007, an increase of 14.1 percent. Diluted net earnings per share was a record $2.12, up 15.8 percent from $1.83 in the prior year. The Company s operating income of $245.8 million increased from prior year operating income of $211.1 million by 16.4 percent.

The table below shows the percentage of total operating income contributed by each segment for each of the last three fiscal years. Corporate and Unallocated includes corporate expenses determined to be non-allocable to the segments and interest income and expense:

	2008	**2007**	**2006**
Engine Products	61.1%	62.9%	67.7%
Industrial Products	42.1%	37.8%	33.6%
Corporate and Unallocated	(3.2%)	(0.7%)	(1.3%)
Total Company	100%	100%	100%

International operating income, prior to corporate expense allocations, totaled 89.4 percent of consolidated operating income in Fiscal 2008 as compared to 77.7 percent in Fiscal 2007. Total international operating income increased 34.0 percent from the prior year. This increase is attributable to stronger foreign currencies, the favorable impact of new plants globally and overall strong business conditions. The table below shows the percentage of total operating income contributed by each major geographic region for each of the last three fiscal years:

	2008	**2007**	**2006**
United States	10.6%	22.3%	22.8%
Europe	43.3%	34.8%	32.7%
Asia	37.9%	38.6%	37.5%
Other	8.2%	4.3%	7.0%
Total Company	100%	100%	100%

Gross margin for Fiscal 2008 was 32.5 percent, an increase from 31.5 percent in the prior year. The primary drivers for the improved gross margin include higher production volumes, a favorable product mix, cost controls and productivity improvements. Partially offsetting the improvements was a charge of $5.0 million to pretax income related to the use of the Last-In, First-Out (LIFO) accounting method for its

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U.S. inventories, which charges increasing commodity costs to income immediately. Also partially offsetting the improvements in gross margin were higher than expected distribution costs associated with implementing the investments made to increase the Company s distribution capabilities and higher purchased commodity costs. During the second quarter, the Company began utilizing a new warehouse management system at its main U.S. distribution center. The Company encountered start-up problems during the transition to the new system. There were incremental expenses related to refining the system which resulted in $7.6 million in unanticipated charges for the year. Gross margin in Fiscal 2007 was also negatively impacted by a higher mix of systems sales versus replacement part sales and higher than expected distribution costs in Europe from the integration of new distribution facilities while Customer demand ramped up beyond expectations. Plant rationalization and start-up costs for new facilities were $0.6 million in Fiscal 2008, down from $5.3 million in the prior year. Operating expenses for Fiscal 2008 were $480.1 million or 21.5 percent of sales, up from $393.8 million or 20.5 percent in the prior year. This increase was driven by the impact of foreign exchange as well as investments in research and development to support essential product development initiatives and the development of next generation technologies and products across many product lines. The Company also increased its investment in information technology to improve Customer support capabilities and enhance its internal system infrastructure capabilities.

Interest expense of $16.6 million increased $2.0 million from $14.6 million in the prior year as a result of increased borrowing costs associated with the increases in working capital and the Aerospace Filtration Systems, Inc. acquisition in March of 2007. Net other income totaled $6.9 million in Fiscal 2008 compared to $8.3 million in the prior year. Components of other income for Fiscal 2008 were as follows: interest income of $1.5 million, earnings from non-consolidated joint ventures of $1.9 million, royalty income of $7.6 million, charitable donations of $0.9 million, foreign exchange losses of $3.1 million and other miscellaneous income and expense items resulting in expenses of $0.1 million.

The effective income tax rate for Fiscal 2008 was 27.2 percent. The effective income tax rate for Fiscal 2007 was 26.4 percent. The Company s Fiscal 2008 tax rate benefited from the effect of changes in foreign statutory tax rates on outstanding deferred tax positions and reduced state tax expense due to lower U.S. earnings. U.S. earnings were also a significantly lower percentage of total earnings, emphasizing the fact that the average tax rate continues to reflect the significant contribution from the Company s international operations, the majority of which have statutory tax rates below those of the U.S. Offsetting these favorable effects, the Company s Fiscal 2008 tax rate was also impacted by a reduced U.S. dividends received deduction, a reduced benefit from the repatriation of foreign earnings, the expiration of some foreign tax incentives, and the expiration of the U.S. Research and Experimentation credit.

Total backlog at July 31, 2008, was $771.2 million, up 25.2 percent from the same period in the prior year. Backlog is one of many indicators of business conditions in the Company s markets. However, it is not always indicative of future results for a number of reasons, including short lead times in the Company s replacement parts businesses and the timing of receipt of orders in many of the Company s Engine OEM and Industrial markets. In the Engine Products segment, total open order backlog increased 24.9 percent from the prior year. In the Industrial Products segment, total open order backlog increased 25.6 percent from the prior year. Because some of the change in backlog can be attributed to a change in the ordering patterns of the Company s Customers and/or the impact of foreign exchange translation rates, it may not necessarily correspond to higher future sales.

Liquidity and Capital Resources

Financial Condition At July 31, 2009, the Company s capital structure was comprised of $35.1 million of current debt, $253.7 million of long-term debt and $688.6 million of shareholders equity. The Company had cash and cash equivalents of $143.7 million at July 31, 2009. The ratio of long-term debt to total capital was 26.9 percent and 19.3 percent at July 31, 2009 and 2008, respectively.

Total debt outstanding decreased $32.8 million during the year to $288.7 million outstanding at July 31, 2009. Short-term borrowings outstanding at the end of the year were $109.8 million lower as compared to the prior year, and long-term debt increased $77.0 million (including current maturities) from the prior year.

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The increase in long-term debt was comprised of a new note agreement. On November 14, 2008, the Company issued an $80 million senior unsecured note, due on November 14, 2013. The debt was issued at face value and bears interest payable semi-annually at a rate of 6.59 percent. The proceeds from the note were used to refinance existing debt and for general corporate purposes.

The following table summarizes the Company s cash obligations as of July 31, 2009, for the years indicated (thousands of dollars):

		Payments Due by Period			
Contractual Obligations	**Total**	**Less than 1 year**	**1 - 3 years**	**3 5 years**	**More than 5 years**
Long-term debt obligations	$ 257,879	$ 4,982	$ 47,678	$ 97,434	$ 107,785
Capital lease obligations	1,291	514	718	59	
Interest on long-term debt obligations	79,030	13,484	25,344	19,952	20,250
Operating lease obligations	21,290	8,422	8,924	3,750	194
Purchase obligations(1)	125,599	106,621	18,500	478	
Pension and deferred compensation(2)	78,643	6,416	10,100	9,725	52,402
Total(3)	$ 563,732	$ 140,439	$ 111,264	$ 131,398	$ 180,631

(1) Purchase obligations consist primarily of inventory, tooling, contract employment services and capital expenditures. The Company s purchase orders for inventory are based on expected Customer demand, and quantities and dollar volumes are subject to change.

(2) Pension and deferred compensation consists of long-term pension liabilities and salary and bonus deferrals elected by certain executives under the Company s deferred compensation plan. Deferred compensation balances earn interest based on a treasury bond rate as defined by the plan and are payable at the election of the participants.

(3) In addition to the above contractual obligations, the Company may be obligated for additional cash outflows of $16.9 million of potential tax obligations. The payment and timing of any such payments is affected by the ultimate resolution of the tax years that are under audit or remain subject to examination by the relevant taxing authorities, and are therefore not currently capable of estimation by period.

As a result of its past contribution practices, the Company does not have a minimum required contribution under the Pension Benefit Guarantee Corporation requirements for its U.S. pension plans for Fiscal 2010. As such, there is no current intention to make a U.S. pension contribution in Fiscal 2010. For its non-U.S. pension plans, the Company estimates that it will contribute approximately $5 million in Fiscal 2010 based upon the local government prescribed funding requirements. Future estimates of the Company s pension plan contributions may change significantly depending on the actual rate of return on plan assets, discount rates and regulatory requirements.

The Company has a five-year, multi-currency revolving facility with a group of banks under which the Company may borrow up to $250 million. This facility matures on April 2, 2013. The agreement provides that loans may be made under a selection of currencies and rate formulas including Base Rate Advances or Off Shore Rate Advances. The interest rate on each advance is based on certain market interest rates and leverage ratios. Facility fees and other fees on the entire loan commitment are payable over the duration of this facility. There was $20.0 million outstanding at July 31, 2009, and $70.0 million outstanding at July 31, 2008. The amount available for further borrowing reflects a reduction for issued standby letters of credit, as discussed below. At July 31, 2009 and 2008, $210.0 million and $161.5 million, respectively, was available for further borrowing under such facilities. The weighted average interest rate on these short-term borrowings outstanding at July 31, 2009 and 2008, was 0.56 percent and 2.73 percent, respectively.

The Company also has three uncommitted credit facilities in the United States, which provide unsecured borrowings for general corporate purposes. At July 31, 2009 and 2008, there was $70.0 million available for use. There was $9.6 million and $28.0 million outstanding under these facilities at July 31, 2009 and 2008, respectively. The weighted average interest rate on these short-term borrowings outstanding at July 31, 2009 and 2008, was 0.53 percent and 2.79 percent, respectively.

The Company also has a 100 million program for issuing treasury notes for raising short, medium and long-term financing for its European operations. There were no amounts outstanding on this program at

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July 31, 2009 and 2008. Additionally, the Company s European operations have lines of credit with an available limit of 72.9 million. There were no amounts outstanding on these lines of credit as of July 31, 2009. As of July 31, 2008, there was 23.5 million, or $36.9 million outstanding. The weighted average interest rate of these short-term borrowings outstanding at July 31, 2008, was 5.60 percent.

Other international subsidiaries may b