



Donaldson®

\$1.2 billion

\$1.4 billion

\$1.6 billion

\$1.7 billion

\$1.9 billion

**\$2.2 billion**

19 Consecutive Record Years

Donaldson Company, Inc.  
Annual Report 2008

Revenue up **16%** to **\$2.2 billion**

•

Operating Margin of **11%**

•

Earnings per share up **16%** to **\$2.12**

•

**19th** consecutive EPS record

•

**53rd** consecutive year of quarterly dividends

•

**19th** consecutive year shares outstanding  
have been reduced

## INDUSTRIAL FILTRATION SOLUTIONS

2008 Sales: \$600 million

Our filtration products are used to clean and filter in a variety of industrial processes and environments. We produce original equipment and replacement parts for the following applications:

- **Industrial Air Filtration Systems** to capture the dust, fumes, or mist generated by manufacturing operations. We market these products under the Torit® and Torit/DCE™ brand names.



- **Compressed Air and Gas Systems** that include air intake and oil filters to deliver clean, dry compressed air and gas throughout our Customers' manufacturing facilities. We market these products under the Donaldson Ultra-Filter™ brand.



## GAS TURBINE SYSTEMS

2008 Sales: \$213 million

We design and provide complete air intake systems for gas turbines and industrial compressors. We also provide aftermarket replacement filters, parts, and service.

Our products are used in our Customers' gas turbines, which provide base electricity, peaking capacity, and remote power. These turbines require inlet air filtration systems to protect the turbine from damage and help it run at peak efficiency.



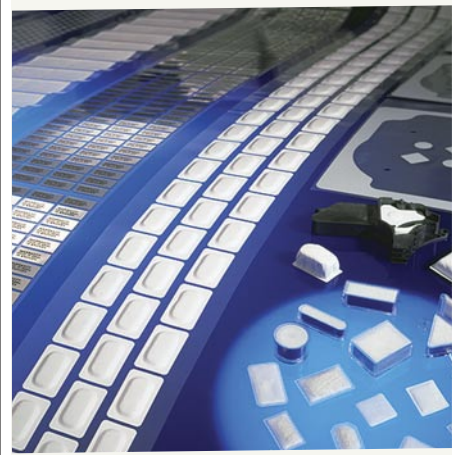
- **Industrial Liquid Filters** clean hydraulic fluids to keep manufacturing equipment running reliably. Our process filters purify steam, liquids, gases, and air used in the food, dairy, beverage, paint, and other industries.



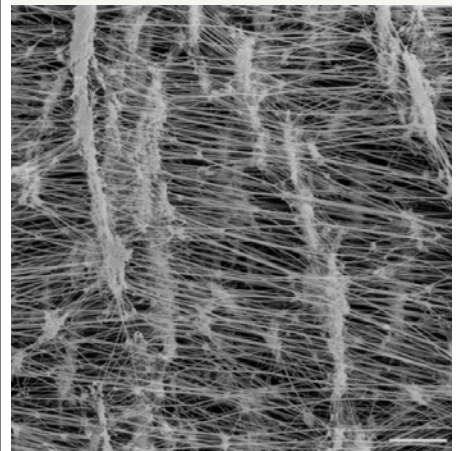
## SPECIAL APPLICATIONS

2008 Sales: \$190 million

We produce a wide variety of high efficiency air filters for the hard disk drive and semiconductor industries. We protect disk drives from dust, chemical contamination, and humidity. Our semiconductor process filters help our Customers optimize the production yields of their products. Our vent filters protect and increase the effectiveness of a variety of consumer electronic devices ranging from hearing aids to automotive sensors.



We manufacture expanded PTFE (polytetrafluoroethylene) membranes under the brand name Tetratex®. This advanced material (shown below magnified 1000x) is used in filtration products and other industrial applications.



**ORIGINAL EQUIPMENT**  
**2008 Sales: \$572 million**

We provide filtration and exhaust systems to construction, transportation, agriculture, defense, aerospace, and mining equipment manufacturers. Our filtration products protect heavy-duty engines in a variety of dirty on- and off-road environments. Simply put, we protect our Customers' engines by cleaning the air going into the engine, all of the fluids around the engine, and the exhaust gases coming out of the engine.



Our products incorporate proprietary and patented designs including PowerCore® and Spiracle™, as well as proprietary filter media such as Ultra-Web® and Synteq™. We typically brand products for our OEM Customers.

**ENGINE AFTERMARKET**  
**2008 Sales: \$657 million**

Our engine aftermarket product line includes a broad line of replacement oil, fuel, air, coolant, transmission, and hydraulic filters, accessories and exhaust and emission control components.

We sell our aftermarket parts to our Customers' OEM parts and service organizations, independent distributors, and private label marketers. We market our replacement filters and parts under both our OEM Customers' brands and the Donaldson brand.



Applications include all types of diesel-powered equipment from pick-up trucks to off-road haul trucks, to on-road heavy-duty trucks and buses, to military and civilian helicopters and airplanes. We have distribution centers strategically located around the world to support the needs of our Customers.

Donaldson is a leading worldwide provider of air and liquid filtration systems and replacement parts that:

- improve people's lives,
- enhance our Customers' equipment performance, and
- protect our environment.

We are a technology-driven company committed to satisfying our Customers' needs for solutions through innovative research and development, application expertise, and global presence. Our 13,000 employees contribute to the Company's success by supporting our Customers at more than 100 sales, manufacturing, and distribution locations around the world.

For over two decades, our financial objective has been and continues to be to build value for our shareholders through superior share price appreciation and consistent dividend payouts. We believe superior shareholder value is created by delivering consistent financial performance and growth in earnings per share. Our business growth will be achieved by pursuing new opportunities in our existing and related markets. Consistency will be reinforced by continuing to expand our diversified portfolio of related businesses around the world.

## DEAR SHAREHOLDERS:

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Milestones tell us where we are at a given moment, where we have been, and how far we have come.

We achieved several milestones this year. Among the most significant was the achievement of our first \$2 billion sales year. This is a great example of the continued successful execution of the plans set forth by my predecessors, Frank Donaldson, Jr., Bill Hodder, and Bill Van Dyke. The foundation of their vision was to leverage our technology and geographic investments to more broadly diversify our Company. The objective of our diversification focus continues to be building a more stable platform which we can use to deliver **consistent** financial results for you, our Shareholders.

We take great pride that our technology investments allow us to supply filtration solutions to our Customers around the globe for applications as varied as the filters in disk drives used in laptop computers, to giant filtration systems installed at power plants that protect large gas turbine engines. Our filtration systems now span the entire spectrum of commerce—from dust collectors used in almond nut processing, to air and liquid filters protecting massive construction vehicles used in the world's mines.

**Bottom line—anywhere there is a critical need for air or liquid filtration, you are likely to find our filters.**

While the foundation of our strategy is growth through diversification, this foundation has really been a “means” to a new “end.” **Since the 1980s, with our growth through diversification approach, we have used this to deliver a different “end”—i.e., consistent financial performance.** For us, “consistent” is defined by three objectives:

- sales growth of 10–12% per year;
- a new Earnings per Share (EPS) record each year; and
- a minimum Return on Investment (ROI) of 15%.

The execution of our growth through diversification strategy allowed us to achieve our second critical milestone this year—our 19th consecutive year of record EPS.

Highlights from the year included:

- Sales totaled \$2.2+ billion, up 16%.
- Our operating margins again hit our 11% target.
- Nearly all business units in our Engine and Industrial segments reported strong operating results, with Engine sales up 13% and Industrial up 20%.
- Extraordinary efforts by hundreds of my fellow employees across our Company helped us restore Customer service levels despite a significant operational challenge at our main U.S. distribution center.
- Our EPS of \$2.12 represented an increase of 16% from \$1.83 last year.

### FOCUS ON DIVERSIFICATION

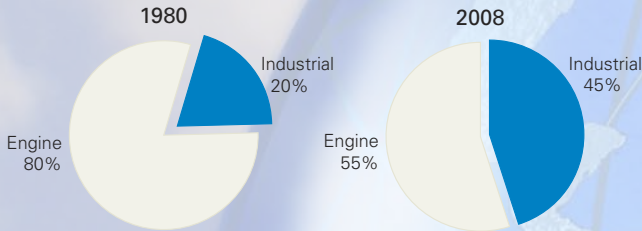
While there were some challenges in the global economy, our continued focus on diversification allowed us to offset the weakness in any one specific business. When we think about our diversification objectives, we measure ourselves on three dimensions:

- our Engine and Industrial segments;
- our first-fit solutions and replacement filters; and
- our Americas-based businesses (North and South) and our International businesses (Europe, Middle East, Africa, and Asia Pacific).

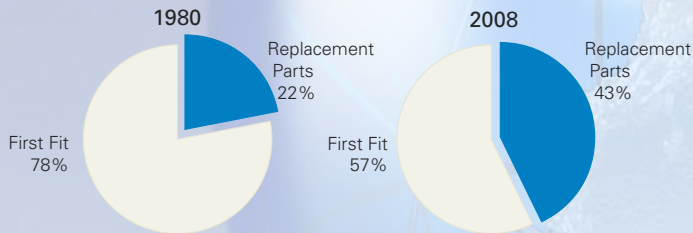
Our goal has been to achieve a 50/50 balance on each of these dimensions. We believe that achieving this balance will further insulate our financial performance from the dramatic impact of any single end market or geographic cycle.

As you can see in the accompanying pie charts, we have come a long way since our start of supplying air filters for farm tractors, sold primarily just in the U.S. Today, 45% of our sales come from our Industrial Products, 43% are replacement filters, and 57% are from our International businesses.

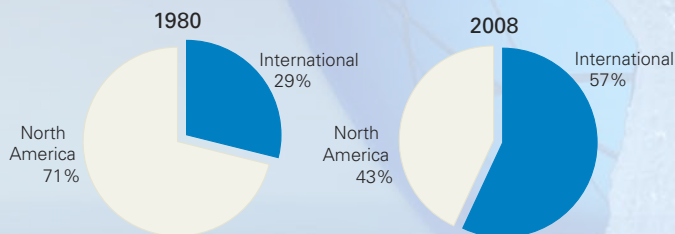
### BUSINESS DIVERSIFICATION



### PORTFOLIO DIVERSIFICATION



### GEOGRAPHIC DIVERSIFICATION



To be clear, all parts of our business are important, but our focus is on diversification—the continued development of our portfolio of different filter businesses around the world.

### INVESTMENTS FOR OUR FUTURE

We continue to make many investments in new technologies, new products, and geographic expansions. We believe that these investments position us to extend our track record into the future. There are too many accomplishments to be able to cover all of them in this letter, so the following are some highlights.

- We invested \$72 million in capital expenditures, much of that for new plants and expansions to extend our geographic reach to support our Customers.
- In Gurgaon, India, we have an expansion under way to triple the size of our existing plant. This expanded plant is positioned for the growth foreseen with our Indian Engine and Industrial Customers.

- We completed a major expansion to our existing plant in Klasterec, Czech Republic. The expansion of this air filter plant will allow us to better serve our European, Russian, and Middle Eastern Customers.



Klasterec, Czech Republic

- In Thailand, as a result of the continued growth of our disk drive filter business for our Hard Disk Drive Customers, we are expanding our clean room filter manufacturing facilities.



Rayong, Thailand  
Disk Drive Filter Clean Room

- And finally, we are back in Brazil! We were in Brazil from the mid-70s to the mid-90s when we exited due to the economic turmoil. The Brazilian economy is now doing well and our Customers are entering or expanding their operations. With the opening of our plant near Sao Paulo, we will be there to support them.

A number of new product platforms were introduced this year. This is consistent with our strategy of leveraging our technologies to offer our Customers both new products and the best value.

- PowerCore® filtration technology was a revolutionary air filtration product when we introduced it five years ago. It allowed us to offer our Customers improved performance and filter life in a significantly smaller size. Our PowerCore sales were up 43% in FY08.

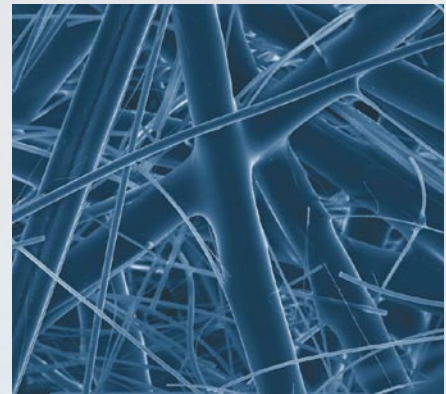


- In FY08, we raised the bar again—introducing two new PowerCore product lines. In our Engine segment we introduced PowerCore Generation 2 (or G2). PowerCore G2 allows us to further reduce the system size by another 30%, which helps our Customers introduce their new engine technologies and better meet equipment space and weight constraints.

- In our Industrial segment we introduced the Torit® PowerCore dust collector that offers improved performance, less maintenance, and is 50% smaller than the traditional baghouse product it replaces.
- In liquid filtration, we introduced our Synteq® XP media, the next generation of our original Synteq technology. Synteq XP's unique resin-free construction provides our Customers with higher filtration efficiency and longer filter life in both our Engine and Industrial markets.



We made one acquisition, LMC West, during FY08. LMC West is a dust collection manufacturer in the U.S. and offers us access to new products, Customers, and markets. We welcome the employees of LMC West to Donaldson!



Synteq XP Liquid Filter Media (600x magnification)

## LOOKING FORWARD

As we enter FY09, the global economic outlook is uncertain and is showing signs of being weaker than in recent years; consequently, we are anticipating sales growth (excluding any new acquisitions) to be 9% to 11%.

We expect our Engine segment sales will grow 10% to 12%, aided by continued strength in mining, agricultural, and heavy construction equipment, but dampened by weaker production rates for smaller equipment used in residential construction. We had a great year in FY08 with our Defense and Aerospace business with both new vehicle and retrofit programs, and we expect another good year in FY09. Finally, we expect replacement filter sales to grow as we continue to create proprietary replacement opportunities for our Customers with new technologies, such as PowerCore G2, and as we further develop new geographies internationally.

In our Industrial segment, we see sales growing at 8% to 10%. Within this segment, current open order backlogs in our Industrial Filtration Solutions business are good, suggesting a strong start to FY09. In our Gas Turbine filter business, we expect that demand for our Customers' gas turbines will remain strong and, therefore, sales of our filter systems will continue to grow through FY11. Finally, we anticipate our Special Applications business will grow, led by continued strength in our PTFE membrane filtration products.

In summary, this forecasted sales growth, combined with our relentless focus on operational excellence, cost reductions, and working capital utilization improvements, should allow us to deliver record sales, our targeted margins and ROI, and EPS of \$2.30 to \$2.40.

**Achieving this will result in Year 20, our 20th consecutive earnings record.**

### CELEBRATING MILESTONES

As I mentioned at the beginning of my letter, we achieved our first \$2 billion sales year. None of this would have been possible without the investment by you, our Shareholders, the dedication of my fellow employees around the world, and our Customers.

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### SAFE HARBOR STATEMENT

The Company desires to take advantage of the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 (the "Act") and is making this cautionary statement in connection with such safe harbor legislation. Some of the information provided in this annual report constitutes forward-looking statements which reflect the Company's current views with respect to future events and financial performance, but involve uncertainties that could significantly impact results. All forecasts and projections are "forward-looking" statements and are based on management's current expectations of the Company's near-term results. There can be no assurance that actual results will not differ materially from its expectations. For a more detailed explanation of the safe harbor statement and the risks, see the Company's Form 10-K filed with the SEC.



Donaldson Rings The Closing Bell at the NYSE on September 4, 2008

To mark this achievement and to have a little fun, our employees guessed the day when we would cross the \$2 billion sales mark. Approximately 6,000 of our employees from all parts of the world submitted entries. Kim Webster, a senior buyer from our Leicester, United Kingdom plant, was one of 150 employees who guessed the correct date, which was June 30.

Kim celebrated our achievement by ringing The Closing Bell at the New York Stock Exchange on September 4. This ceremony helped mark that milestone for us—reminding us of how far we have come, and also where we are heading on the path to reach our next set of milestones, including our 20th consecutive year of record EPS in FY09 and sales of \$3 billion in FY11.

Sincerely,

Bill Cook





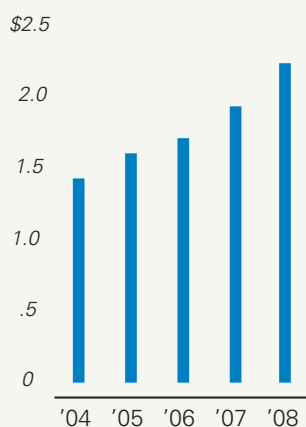
## FIVE-YEAR COMPARISON OF RESULTS

July 31, 2008

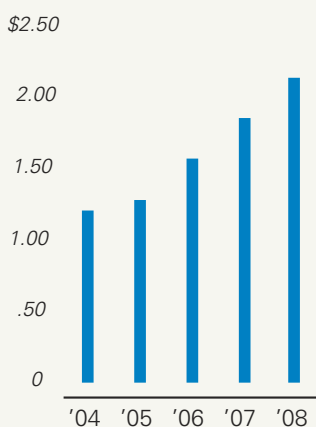
*(dollars in millions, except share and per share amounts)*

	2008	2007	2006	2005	2004
<b>Operating Results</b>					
Net sales	<b>\$2,232.5</b>	\$1,918.8	\$1,694.3	\$1,595.7	\$1,415.0
Gross margin percentage	<b>32.5%</b>	31.5%	32.8%	31.7%	31.6%
Operating income percentage	<b>11.0%</b>	11.0%	11.4%	9.8%	10.0%
Effective income tax rate	<b>27.2%</b>	26.4%	30.1%	28.6%	25.0%
Net earnings	<b>\$ 172.0</b>	\$ 150.7	\$ 132.3	\$ 110.6	\$ 106.3
Return on sales	<b>7.7%</b>	7.9%	7.8%	6.9%	7.5%
Return on average shareholders' equity	<b>25.2%</b>	25.7%	24.7%	20.6%	21.3%
Return on investment	<b>20.6%</b>	21.5%	20.8%	17.7%	18.1%
<b>Financial Position</b>					
Total assets	<b>\$1,548.6</b>	\$1,319.0	\$1,124.1	\$1,111.8	\$1,001.6
Current debt	<b>\$ 145.1</b>	\$ 156.8	\$ 79.9	\$ 109.8	\$ 54.1
Long-term debt	<b>\$ 176.5</b>	\$ 129.0	\$ 100.5	\$ 103.3	\$ 70.9
Total debt	<b>\$ 321.5</b>	\$ 285.8	\$ 180.4	\$ 213.1	\$ 124.9
Shareholders' equity	<b>\$ 740.0</b>	\$ 624.7	\$ 546.8	\$ 524.6	\$ 549.3
Long-term capitalization ratio	<b>19.3%</b>	17.1%	15.5%	16.5%	11.4%
Property, plant and equipment, net	<b>\$ 415.2</b>	\$ 364.4	\$ 317.4	\$ 275.5	\$ 261.5
Net expenditures on property, plant and equipment	<b>\$ 70.8</b>	\$ 76.6	\$ 77.6	\$ 50.2	\$ 43.0
Depreciation and amortization	<b>\$ 56.7</b>	\$ 49.6	\$ 44.7	\$ 44.3	\$ 41.6
<b>Shareholder Information (adjusted for splits)</b>					
Net earnings per share—assuming dilution	<b>\$ 2.12</b>	\$ 1.83	\$ 1.55	\$ 1.27	\$ 1.18
Dividends paid per share	<b>\$ 0.42</b>	\$ 0.36	\$ 0.32	\$ 0.24	\$ 0.21
Shareholders' equity per share	<b>\$ 9.55</b>	\$ 7.90	\$ 6.80	\$ 6.32	\$ 6.38
Shares outstanding (millions)	<b>77.5</b>	79.0	80.5	83.0	86.1
Common stock price range, per share					
High	<b>\$ 52.33</b>	\$ 38.97	\$ 36.00	\$ 34.45	\$ 30.75
Low	<b>\$ 34.40</b>	\$ 31.83	\$ 28.60	\$ 25.11	\$ 23.55

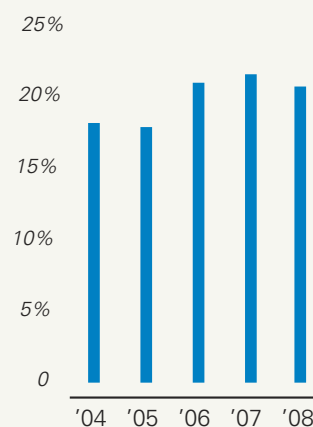
**NET SALES**  
*(in billions)*



**EARNINGS PER SHARE**  
*(in dollars)*



**RETURN ON INVESTMENT**  
*(in percent)*



## CORPORATE INFORMATION

### CORPORATE OFFICERS

WILLIAM M. COOK, 55  
*Chairman, President and CEO*

CHARLES J. McMURRAY, 54  
*Senior Vice President,  
Industrial Products*

LOWELL F. SCHWAB, 60  
*Senior Vice President,  
Global Operations*

JAY L. WARD, 44  
*Senior Vice President,  
Engine Products*

TOD E. CARPENTER, 49  
*Vice President,  
Europe and Middle East*

PEGGY A. HERRMANN, 52  
*Vice President, Disk Drive and  
Microelectronics*

DENNIS D. JANDIK, 54  
*Vice President, Global Engine OEM Sales*

SANDRA N. JOPPA, 43  
*Vice President, Human Resources*

JOSEPH E. LEHMAN, 53  
*Vice President,  
Global Engine Aftermarket*

NORMAN C. LINNELL, 49  
*Vice President, General Counsel  
and Secretary*

MARY LYNNE PERUSHEK, 50  
*Vice President and  
Chief Information Officer*

DAVID W. TIMM, 55  
*Vice President, Asia Pacific*

THOMAS R. VERHAGE, 55  
*Vice President and Chief Financial Officer*

DEBRA L. WILFONG, 53  
*Vice President and  
Chief Technology Officer*

### BOARD OF DIRECTORS

F. GUILLAUME BASTIAENS, 65  
*Retired Vice Chairman  
Cargill, Inc.; Minneapolis, MN*

WILLIAM M. COOK, 55  
*Chairman, President and CEO  
Donaldson Company, Inc.*

JANET M. DOLAN, 58  
*President  
Act 3 Enterprises, LLC; Minneapolis, MN*

JACK W. EUGSTER, 62  
*Retired Chairman, President and CEO  
The Musicland Group, Inc.;  
Minneapolis, MN*

JOHN F. GRUNDHOFER, 69  
*Retired Chairman and CEO  
U.S. Bancorp; Minneapolis, MN*

MICHAEL J. HOFFMAN, 53  
*Chairman, President and CEO  
The Toro Company; Minneapolis, MN*

PAUL DAVID MILLER, 66  
*Retired Chairman and CEO  
Alliant Techsystems, Inc.;  
Minneapolis, MN*

JEFFREY NODDLE, 62  
*Chairman and CEO  
SUPERVALU, Inc.; Minneapolis, MN*

WILLARD D. OBERTON, 50  
*President and CEO  
Fastenal Company; Winona, MN*

JOHN P. WIEHOFF, 47  
*Chairman, President and CEO  
C.H. Robinson Worldwide, Inc.;  
Minneapolis, MN*

### SHAREHOLDER INFORMATION

Our CEO and CFO Certifications required under Sarbanes-Oxley Section 302 were filed as exhibits to our Form 10-K.

#### NYSE Listing

The common shares of Donaldson Company, Inc. are traded on the New York Stock Exchange under the symbol DCI. The annual CEO Certification that Donaldson is in compliance with the NYSE corporate governance listing standards was submitted to the NYSE on December 4, 2007, as required by Section 303A.12(a) of the New York Stock Exchange Listed Company Manual.

### Shareowner Services

For any concerns relating to your shareholdings, please contact Shareowner Services at (800) 468-9716 or (651) 450-4064.

### Dividend Reinvestment Plan

As of September 23, 2008, 1,131 of Donaldson Company's approximately 1,853 shareholders of record were participating in the Dividend Reinvestment Plan. Under the plan, shareholders can invest dividends in additional shares of Company stock.

The Plan is provided without service charges or brokerage commissions. Shareholders may obtain a brochure giving further details by writing Wells Fargo Bank Minnesota, N.A., Shareowner Services, P.O. Box 64854, St. Paul, MN 55164-0854.

### Annual Meeting

The annual meeting of shareholders will be held on November 21, 2008, 1:00 p.m., at Donaldson Company, 2001 West 94th Street, Bloomington, MN 55431. Shareholders are welcome to attend.

### Investor Relations

You can access investor relations information, including our SEC filings, on our website at [www.donaldson.com](http://www.donaldson.com). For investor inquiries, contact Rich Sheffer, Director of Investor Relations, at (952) 887-3753 or [richard.sheffer@donaldson.com](mailto:richard.sheffer@donaldson.com).

### Independent Registered Public Accounting Firm

PricewaterhouseCoopers LLP  
Minneapolis, MN

### Transfer Agent

Wells Fargo Bank, N.A.  
South St. Paul, MN

### Diversity

Donaldson is focused on creating a globally inclusive culture. Our goal is to create an atmosphere of mutual respect where individual differences are valued and all employees can contribute to their full potential.

### 2008 Sustainability Report

Donaldson is committed to delivering quality products and being a responsible corporate citizen. A copy of Donaldson's 2008 Sustainability Report is available online at [www.donaldson.com](http://www.donaldson.com).



Donaldson Company, Inc.  
PO Box 1299  
Minneapolis, MN 55440-1299  
952 887 3131

[www.donaldson.com](http://www.donaldson.com)