



**Pentair**

ANNUAL REPORT 2006

# financial SUMMARY

Pentair, Inc. and Subsidiaries	Years ended December 31				
	2006	2005	2004	2003	2002
(Dollars in thousands, except pershare data)					
<b>operations</b>					
Net sales	\$ 3,154,469	\$2,946,579	\$ 2,278,129	\$ 1,642,987	\$ 1,488,453
Operating income	306,986	323,072	247,242	170,210	131,295
Adjusted operating income (1)	321,162	339,460	247,242	170,210	131,295
Net income — continuing operations	183,767	185,049	137,024	98,150	74,999
Diluted EPS — continuing operations	1.81	1.80	1.35	0.99	0.75
Net cash provided by operating activities	231,611	247,858	264,091	262,939	270,794
Capital expenditures (2)	51,078	62,471	48,867	43,622	56,696
Proceeds from sale of property and equipment	684	17,111	—	—	—
Free cash flow (3)	181,217	202,498	215,224	219,317	214,098
Number of employees at year end	14,800	14,700	12,900	9,000	8,600
<b>other financial data</b>					
Total debt	744,061	752,614	736,105	806,493	735,085
Shareholders' equity	1,669,999	1,555,610	1,447,794	1,261,478	1,105,724
Total debt as a percent of total capital	30.8%	32.6%	33.7%	39.0%	39.9%
Return on average shareholders' equity	11.4%	12.3%	12.6%	11.9%	12.3%
Cash dividends declared per common share	0.56	0.52	0.43	0.41	0.37
Closing stock price	31.40	34.52	43.56	22.85	17.28
Effect of SFAS 123R, net of tax (4)	9,933	11,998	—	—	—
Diluted EPS effect of SFAS 123R (4)	0.10	0.12	—	—	—
Weighted-average shares — diluted	101,371	102,618	101,706	99,620	99,489

(1) Adjusted operating income excludes the impact of the adoption of SFAS 123R on 2005 and 2006 operating income to be comparable to prior years presented. The impact of adoption of SFAS 123R on operating income in 2005 and 2006 was \$16.4 million and \$14.2 million, respectively.

(2) 2002 includes \$23.0 million for the acquisition of a previously leased facility.

(3) Free cash flow defined as net cash provided by operating activities less capital expenditures plus proceeds from sale of property and equipment.

(4) Effective January 1, 2005 we adopted SFAS 123R which requires the fair value of stock options to be expensed. The standard did not require restatement of prior period amounts to be consistent with the current presentation. The amounts shown represent the impact of adoption in 2005 and 2006. Total pre-tax stock-based compensation in 2006 and 2005 was \$25.3 million and \$24.2 million, respectively.

# letter to our SHAREHOLDERS

After four years of solid earnings growth, Pentair's 2006 performance resulted in flat earnings. Breakthrough performance in the Technical Products Group in sales, operating income, return on sales and acquisition integration was negated by setbacks in the Water Group. There, strong global growth and improvements in pump did not overcome investments for growth, inefficiencies, and softness in the North American residential market — our largest served market. We took action to manage the impact of this challenging market, including specific steps to manage costs. Importantly, we also strengthened our core technical competencies in flow and filtration, expanded our thermal management capabilities to more effectively serve our Technical Products markets, and streamlined our leadership structure in 2006. These actions were designed to help address short-term economic conditions affecting our businesses while simultaneously improving our long-term prospects. For these reasons, we are confident in our roadmap to drive Pentair's performance higher in 2007 and beyond.

# letter to our shareholders continued

## 2006 Results

In 2006, Pentair delivered earnings per share of \$1.81. Details of the Company's 2006 performance include:

▶ Revenues increased 7 percent compared to the year earlier, reaching \$3.15 billion. Growth in North America was modest, due to the weakness in the residential water equipment market. Growth in Europe, the Middle East and Africa was solid as overall economic conditions were strong and growth investments paid off.

Growth in Asia was strong, and reflected

our investments in this attractive region.

Technical Products 2006 revenues

surpassed the \$1 billion threshold,

an increase of 23 percent

year-over-year.

▶ Operating margins decreased

year-over-year. Strong operating

performance in Technical Products led

to the 17<sup>th</sup> consecutive quarter of year-

over-year operating margin improvement for

the Group, though these results were offset by

the operating performance of the Water Group.

▶ Free cash flow for the year was \$181 million, which represented 99 percent conversion of net income, just shy of the Company's goal of 100 percent.

▶ Six acquisitions were signed in 2006. Approximately 85 percent of the acquired revenue is based outside of North America, reflecting the Company's growth strategy.

▶ Dividends increased for the 30<sup>th</sup> year in a row with no increase in net debt during 2006. At the end of 2006, Pentair's debt-to-total-capital ratio was 30.8 percent, 180 basis points lower than what it was at the end of 2005.

## Leading Positions in Attractive Markets

### Water

Pentair continues to deliver innovative solutions to address water quality and scarcity demands. Today, approximately 300 million people live in areas of severe water shortages; by some estimates, that number is expected to increase to 3 billion over the next two decades. Beyond meeting basic human needs for health and sanitation, water contributes to sustainable development: it is required for agricultural development and many industrial purposes, it is an untapped source of power in some regions of the world, and it is increasingly critical to the safety of communities when natural disasters strike. A leader in flow and filtration, Pentair expanded the solutions available to address water needs in 2006. In markets outside of North America, we improved our ability to provide regional solutions to regional needs through acquisitions in China and Germany.

### Technical Products

Pentair continues to serve a broad range of industries — from general manufacturing, medical and security to telecommunications — with a broad product range of products including enclosures, racks, heat exchangers and air

Pentair is a diversified operating company headquartered in Minnesota. Its Water Group is a global leader in providing innovative products and systems used worldwide in the movement, storage, treatment and enjoyment of water. Pentair's Technical Products Group is a leader in the global enclosures and thermal management markets, designing and manufacturing standard, modified and custom enclosures, and thermal management products and accessories that house and protect sensitive electronics and electrical components. With 2006 revenues of \$3.15 billion, Pentair employs approximately 14,800 employees worldwide.

## letter to our shareholders continued

conditioners that protect and house electronic and electrical equipment. For example, Pentair cabinets house medical equipment controls, and industrial controls in auto factories, food production facilities, and even border security installations. In 2006, the Group fully integrated its thermal management acquisition. Through the effective deployment of Pentair's Integrated Management System, these new businesses exceeded productivity and sales goals in their first full year.

### **Maintaining our Strategic Direction**

Though Pentair faced significant challenges last year, we have reaffirmed that our strategic initiatives — operations excellence, global expansion and differentiated growth — are correct. Pentair's 2006 performance reflects market weakness and execution shortfalls, which we have already begun to remedy. To do this, we streamlined our leadership organization, appointing Michael V. Schrock as Chief Operating Officer of the Water and Technical Products Groups. We reduced costs to better position Pentair for the difficult markets we are facing. We increased our investment in technology; most notably, we hired a new leader in Water technology to drive global product development and innovation. We also staffed seven global initiatives to drive growth. With me, Pentair's leadership team has reaffirmed our

strategic initiatives and committed to each one. Together, we are focused on improving performance to deliver the quality our customers expect and the value our shareholders deserve.

### **Winning Right for Forty Years**

In 2006, Pentair marked the 40<sup>th</sup> anniversary of the Company's founding. Since 1966, Pentair has consisted of varied businesses in varied industries — paper, lubrication, ammunition, and power tools, to name a few. Today, Pentair is focused on Water and Technical Products, two arenas in which we control our destiny. Throughout our history, one thing has remained constant: a strong commitment to Pentair's values. Integrity and high performance — or Win Right — remains at the core of all that we do. We believe this cultural focus is an enormous advantage for Pentair. Of course, it is only through the dedication of every Pentair employee that we earn our reputation for Winning Right, and I thank all Pentair employees for their efforts.

**John L. Stauch joined Pentair as Executive Vice President and Chief Financial Officer (CFO) in February 2007. He brings a breadth of experience in finance and investor relations, a proven understanding of operations, and strong leadership in complex global business environments to the Company. Prior to Pentair, Mr. Stauch held wide ranging finance leadership roles including investor relations, financial planning and analysis, and division CFO positions across a number of global industries in ten years at Honeywell International and its predecessor, Allied Signal.**



**JOHN L. STAUCH**  
*Executive Vice President and  
Chief Financial Officer*

### **Clear Roadmap for 2007**

We face some uncertain market segments in 2007, particularly in the North American residential and telecommunication markets. Our task, then, is to more effectively drive growth and higher performance to yield strong long-term shareholder value. By rigorously applying Pentair's Integrated

## letter to our shareholders continued

Management System, we expect to make real operating performance progress and to deliver on the promise of our Water business with a step up in operating margins while sustaining the excellent performance of Technical Products; to drive growth in all businesses through an intensified, global approach to vertical markets; and to accelerate the leverage of our increasingly global businesses.

We remain optimistic about Pentair's prospects. Energized by the challenges we face, Pentair employees demonstrate their commitment to our customers and our shareholders daily. Their purposeful enthusiasm inspires me and my confidence in our continued ability to Win Right. I'd like to acknowledge and express appreciation for the continued commitment of Pentair's employees, customers and shareholders. Thank you.

Sincerely,



  
RANDALL J. HOGAN  
*Chairman and Chief Executive Officer*



# technical products group OVERVIEW

## Protecting the technologies that connect, enable and inform.

Pentair's Technical Products Group is a leader in global enclosures and thermal management markets, designing and manufacturing thermal management products and standard, modified, and custom enclosures that house and protect sensitive electronics and electrical components.

### Electrical

### Electronic

### Thermal Management

#### MARKETS

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- ▶ Industrial including automotive, machine tool, food and beverage, pharmaceutical, water treatment, petrochemical, defense and security markets.
- ▶ Commercial including commercial and industrial new construction markets.

- ▶ Electronic including aerospace, computer networking, data communications, defense and security, industrial controls, medical, telecommunications, test and measurement, and semiconductor equipment markets.

- ▶ Industrial including automotive and machine tool; medical, datacommunications, telecommunications, and test and measurement markets.

#### BRANDS

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Hoffman®

Schroff®, Hoffman®, Taunus™, Pentair Electronic Packaging™, Electronic Solutions™, and Birtcher™.

McLean®, Hoffman®, Aspen Motion Technologies™, and Schroff®.

#### PRODUCTS

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Standard, modified, co-developed and custom enclosures, cabinets and accessories, and thermal management solutions to protect components and instruments.

Standard, modified and co-developed enclosures including racks, subracks and indoor and outdoor cabinets as well as stamped chassis, slide rail and cable management solutions, and integrated solutions with power supplies and backplanes.

Standard and custom thermal management solutions including air conditioners, heat exchangers, fan trays, motorized impellers, single and dual packaged blowers, AC and brushless DC motors, electronic controls and filter fans.

# water group OVERVIEW

## **A global leader in providing innovative products and systems used to deliver safe, clean water.**

While most of the earth is covered in water, only a small fraction of this water supply is practically available for the demands of the world's population. The accelerating need for safe clean water is driven by scarcity and quality concerns, as water use escalates to accommodate industrial expansion and population growth, and by infrastructure requirements, as both established and emerging regions seek to address them. Pentair is uniquely positioned to deliver quality solutions for our customers' water needs in flow and filtration.

### **Filtration and Purification**

#### MARKETS

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- ▶ **Commercial & Industrial:** Including aviation, foodservice, recreational vehicles and marine.
- ▶ **Municipal**
- ▶ **Residential**

#### BRANDS

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Everpure<sup>®</sup>, SHURflo<sup>®</sup>, Fleck<sup>®</sup>, CodeLine<sup>®</sup>, Structural<sup>™</sup>, Pentek<sup>™</sup>, SIATA<sup>™</sup>, WellMate<sup>™</sup>, American Plumber<sup>®</sup>, Armor<sup>®</sup>, OMNIFILTER<sup>®</sup>, Park International<sup>™</sup>, Fibredyne<sup>™</sup>, and Krystal Klear<sup>®</sup>.

#### PRODUCTS

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Products range from softener and filter control valves; filtration housings; replaceable cartridge elements; carbon filtration systems; drinking water filtration systems and components; fiberglass wound pressure tanks and vessels; to brine cabinets and storage tanks; in-ground boxes for irrigation and control valves; stainless steel vessels for industrial filtration markets; and booster pumps for drinking water systems.

## Pump Systems

### MARKETS

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- ▶ **Commercial and Industrial:** Including agricultural, car wash, fire protection, food service, HVAC, marine, treatment, water feature and general applications.
- ▶ **Municipal:** Including water supply, reverse osmosis, desalination, wastewater transport, wastewater process and flood control.
- ▶ **Residential**

### BRANDS

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STA-RITE®, Myers®, Aurora®, Hydromatic®, Fairbanks Morse®, Flotec®, Hypro®, Water Ace®, Berkeley®, Aermotor™, Simer®, Verti-Line™, Diamond™, Foam Pro®, Onga™, Nocchi™, ShurDri®, Edwards®, Jung, and Delta Environmental.

### PRODUCTS

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Products range from light-duty diaphragm pumps to high-flow turbine pumps and solid handling pumps designed for water and wastewater applications and agricultural spraying; pressure tanks for residential applications as well as residential and commercial on-site treatment.

## Pool and Spa

### MARKETS

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- ▶ **Commercial**
- ▶ **Municipal**
- ▶ **Residential**

For in-ground and above-ground pools, water features and parks, spas, jetted tubs, aquarium, ponds, and aquaculture applications.

### BRANDS

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Pentair Pool Products®, Pentair Water Pool and Spa®, National PoolTile Group®, Pentair Aquatics®, STA-RITE®, Paragon Aquatics®, Pentair Spa and Bath™, Kreepy Krauly®, Compool®, WhisperFlo®, PoolShark®, Legend®, Rainbow™, Ultra Jet®, FIBERWorks®, IntelliTouch®, Acu-Trol®, EasyTouch®, IntelliFlo®, IntelliPro™, MasterTemp®, and Max-E-Therm®.

### PRODUCTS

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A complete line of pool and spa equipment and accessories, including automation, pumps, filters, lights, cleaners, commercial starting blocks, lifeguard stands and deck equipment, barbeque island and outdoor grill equipment, aquatic pond products and accessories, pool tile and interior finishing surfaces, maintenance equipment, hydrotherapy fittings, and other accessories.

# corporate LEADERSHIP

## board of directors

**GLYNIS A. BRYAN** (1), 48  
*Executive Vice President and Chief Financial Officer*  
*Swift Transportation Co.*

**RICHARD J. CATHCART** (4), 62  
*Vice Chairman*  
*Pentair, Inc.*

**BARBARA B. GROGAN** (2, 3, 4), 59  
*Former Chairman and President*  
*Western Industrial Contractors, Inc.*

**CHARLES A. HAGGERTY** (2, 3, 4), 65  
*Chief Executive Officer*  
*LeConte Associates, LLC*

**RANDALL J. HOGAN** (4), 51  
*Chairman and Chief Executive Officer*  
*Pentair, Inc.*

**DAVID A. JONES** (2, 3), 57  
*Chairman and Chief Executive Officer*  
*Spectrum Brands, Inc.*

**AUGUSTO MEOZZI** (1, 4), 67  
*President of European operations*  
*ISOLA Group*

**RONALD L. MERRIMAN** (1), 62  
*Managing Director*  
*Merriman Partners*

**WILLIAM T. MONAHAN** (2, 3, 4), 59  
*Former Chairman and Chief Executive Officer*  
*Imation Corp.*

**KAREN E. WELKE** (1, 4), 62  
*Former Group Vice President for Medical Markets*  
*3M Company*

- (1) *Audit Committee*
- (2) *Compensation Committee*
- (3) *Governance Committee*
- (4) *International Committee*

## corporate officers

**RANDALL J. HOGAN**  
*Chairman and Chief Executive Officer*

**RICHARD J. CATHCART**  
*Vice Chairman*

**MICHAEL V. SCHROCK**  
*President and Chief Operating Officer*

**JOHN L. STAUCH**  
*Executive Vice President and*  
*Chief Financial Officer*

**LOUIS L. AINSWORTH**  
*Senior Vice President, General Counsel and Secretary*

**JACK J. DEMPSEY**  
*Senior Vice President, Operations and Technology*  
*President, Filtration*

**KAREN A. DURANT**  
*Senior Vice President, Finance and Analysis*

**FREDERICK S. KOURY**  
*Senior Vice President, Human Resources*

**MICHAEL G. MEYER**  
*Vice President, Treasury and Tax*

# investor INFORMATION

**annual meeting** The Annual Meeting of Pentair shareholders will take place on Thursday, May 3, 2007 in the Cinema auditorium of the Walker Art Center (1750 Hennepin Avenue, Minneapolis, MN 55403). Pentair management and directors encourage all shareholders to attend the annual meeting.

**investor information** Shareholders, securities analysts and investors seeking more information about the Company can access news releases describing significant Company events and earnings results for each quarter and the fiscal year, and Form 10-K and other Securities and Exchange Commission filings at [www.pentair.com](http://www.pentair.com). Information may also be obtained by request from the Pentair Investor Relations department, 5500 Wayzata Boulevard, Suite 800, Golden Valley, Minnesota 55416.

**stock exchange listing** New York Stock Exchange (symbol PNR)

**price range of common stock** As of December 31, 2006, there were 3,907 shareholders of record. The high, low, and closing sales price for Pentair's common stock and the dividends declared for each of the quarterly periods for 2006 and 2005 were as follows:

2006	High	Low	Close	Div.	2005	High	Low	Close	Div.
1Q	41.90	34.01	40.75	0.14	1Q	44.32	38.39	39.14	0.13
2Q	41.55	32.05	34.19	0.14	2Q	46.03	37.45	42.62	0.13
3Q	34.43	25.69	26.19	0.14	3Q	45.17	36.11	36.50	0.13
4Q	33.49	26.25	31.40	0.14	4Q	38.41	30.80	34.52	0.13

**dividends** Dividends are currently \$0.15 per share, paid quarterly in February, May, August and November. Pentair has paid 124 consecutive quarterly dividends.

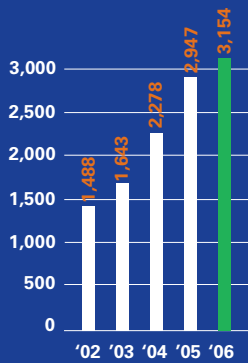
**dividend reinvestment** Pentair offers a Dividend Reinvestment Plan that allows shareholders of record the opportunity to automatically reinvest quarterly cash dividends and invest up to an additional \$3,000 per calendar quarter in Pentair common stock, with any costs of purchasing the shares paid by the Company. Plan and enrollment information are available from the Company or Wells Fargo Bank, N.A.

**registrar, stock transfer and dividend paying agent** Wells Fargo Bank, N.A., P.O. Box 64854, St. Paul, Minnesota 55164-0854, 1-877-536-3554, [https://www.wellsfargo.com/com/shareowner\\_services](https://www.wellsfargo.com/com/shareowner_services)

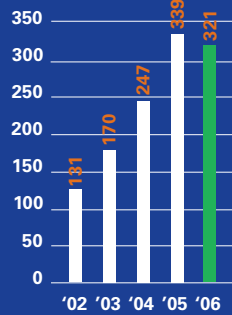
**certified public accounts** Deloitte & Touche LLP, Minneapolis, Minnesota

**forward-looking statements** This summary annual report may contain forward-looking statements that are based on current expectations, estimates and projections. These statements are not guarantees of future performance and involve risks and uncertainties which are difficult to predict. Important factors that could cause actual results to differ materially include changes in industry conditions, changes in business strategies, governmental and regulatory policies, general economic conditions and changes in operating factors. See Item 1A of the Company's 2006 Form 10-K, which is included with this report.

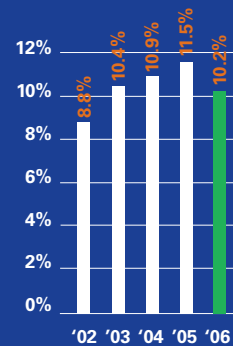
# financial HIGHLIGHTS



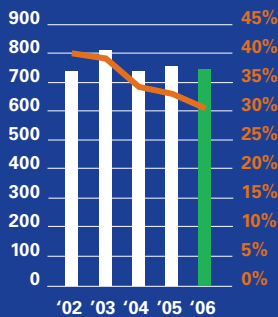
**net sales**  
(\$ in millions)



**adjusted operating income\***  
(\$ in millions)

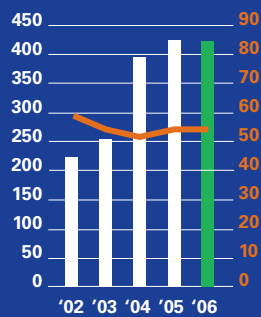


**adjusted operating income margin\***



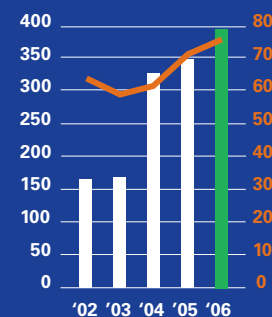
**total debt**  
(\$ in millions)

**debt/total capital**



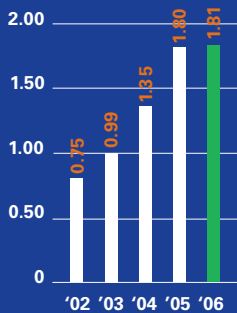
**accounts receivable**  
(\$ in millions)

**days sales outstanding**  
(13 month moving average)

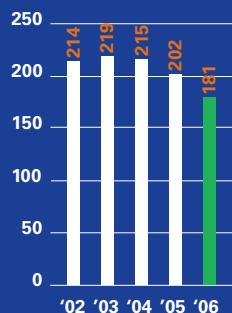


**inventories**  
(\$ in millions)

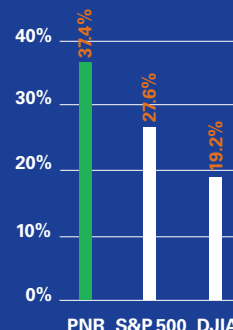
**days on hand**  
(13 month moving average)



**diluted eps**  
(\$ per share)



**free cash flow**  
(\$ in millions)



**3-year stock price appreciation**

\*As defined in the financial summary section on the inside front cover of this 2006 Pentair Annual Report.

**CERTIFICATIONS** The Company has filed as exhibits to its Annual Report on Form 10-K for the fiscal year ended December 31, 2006 the certifications of its Chief Executive Officer and Chief Financial Officer required by Section 302 of the Sarbanes-Oxley Act. The Company submitted to the New York Stock Exchange during 2006 the Annual CEO Certification required by Section 303A.12(a) of the New York Stock Exchange Listed Company Manual.

# CODE of business conduct

As an independent, publicly owned company, Pentair created the Code of Business Conduct and Ethics to guide its development and the conduct of its business.

- ▶ We will manage our business according to the highest business, ethical, moral and civic standards that apply to a public company.
- ▶ We will operate our businesses to earn the respect of our shareholders, employees, plant communities, customers, suppliers and all others with a stake in our success.
- ▶ We intend to make Pentair a top-performing company, managed and operated for the long-term benefit of all its constituents.

The Code of Business Conduct is the foundation for numerous specific practices, policies and guidelines that determine how Pentair and its employees conduct their day-to-day business. The Code is intended to set the tone and spirit for how Pentair operates.

As a company, by following the spirit of the Code, Pentair creates an operating environment where management sets clear goals, company leadership is engaged, and all operations are accountable for their performance and practices. Our business style is practical, with an emphasis on openness, informality and candid, conversational exchanges among employees. We expect all employees equally to uphold the Company's standards for ethics, integrity and work practices.

The full text of Pentair's Code of Business Conduct and Ethics can be found at <http://www.pentair.com/code.html>



**Pentair**

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